GLOBAL BUSINESS ALLIANCE | *Investing in America*

Restore the DA – 163(j)

Pursuant to Section 163(j), the deduction for a company's interest expense is generally limited to 30 percent of the company's Adjusted Taxable Income. In 2022, a change was made to the Section 163(j) calculation stemming from the 2017 Tax Cuts and Jobs Act (TCJA), which eliminated the addition of depreciation and amortization to determine Adjusted Taxable Income. This changed the calculation from an EBITDA standard (Earnings Before Interest, Taxes, Depreciation & Amortization) to an EBIT standard. It is noteworthy that EBITDA is the standard recommended by the OECD, is used in nearly all countries with a similar limitation and is the appropriate measure commonly used by lenders to determine a company's credit rating and ability to pay back a loan.

GBA asks that depreciation and amortization be restored to the OECD-recommended EBITDA standard used to calculate the Section 163(j) limitation.

The new current EBIT-based computation of the Section 163(j) interest expense limitation reduces the Adjusted Taxable Income base by depreciation and amortization (the DA portion). This results in less deductible interest expense, leading to less investment. This use of EBIT has nothing to do with a company's ability to borrow, is out of step with the OECD and countries competing with the U.S. for investment and is contrary to normal business practices.

Depreciation is intended to measure a tangible asset's life – say, a $100,000 machine for a manufacturing facility. Once the machine is placed in service, a prescribed percentage of the cost is deducted to determine a company's taxable income. Assuming the machine has a 20-year useful life and straight-line depreciation, $5,000 would be deducted each year. In recent years with bonus depreciation, a quicker deduction (perhaps the entire amount in the year of purchase) for depreciation is available to promote investment (see more on that point below). Amortization is akin to depreciation but for intangible assets – like a secret recipe or the value of a brand a company may have acquired.

A bipartisan bill (H.R. 2788/S. 1232) introduced by Rep. Adrian Smith (R-NE) and Rep. Joseph Morelle (D-NY) and Sen. Shelley Capito (R-WV) and Sen. Kyrsten Sinema (I-AZ), would restore both depreciation and amortization to recreate the EBITDA formula. We ask that your boss co-sponsor this bill and support legislation including its passage.

Research and Development - 174

The U.S. has a long history of recognizing research and development's value in increasing innovation. Congress has allowed businesses to fully deduct their R&D expenses under Section 174 in the year they are incurred. Since 2022, businesses must now amortize such expenses over a longer period of five years. This has increased the tax cost for research by companies and will potentially lead to thousands of jobs lost over the next five years[1].

Requiring amortization of these R&D expenses makes the United States a global outlier, as nearly every country permits full deductibility, and some even provide tax benefits greater than 100 percent deductibility. Legislation to repeal this provision will ensure that the R&D tax credit and the ability to deduct R&D expenses remain an effective engine for American innovation.

A bipartisan bill introduced this Congress by Sen. Maggie Hassan (D-NH) and Sen. Todd Young (R-IN) and Rep. Ron Estes (R-KS), *The American Innovation and Jobs Act* (S. 866/H.R. 2673) to restore incentives for long-term R&D investment. We ask that you co-sponsor the *American Innovation and Jobs Act* (S.866/H.R. 2673) and support legislation including its passage.

Bonus Depreciation

Significant progress has been made in recent years in improving the cost recovery treatment of business investment. Bonus depreciation allows the immediate write-off of most business assets; however, beginning in 2023, it is scheduled to begin to phase out.

Suppose a company invested $1 million in new equipment to increase capacity; 100 percent bonus depreciation would allow the company to deduct the investment from its taxable income in the first year. Alternatively, straight-line depreciation allows the company to deduct a fixed percentage (e.g., 20 percent) of its original investment each year until the entire amount has been deducted.

Bonus depreciation creates an incentive to encourage investment since companies can deduct the full cost of their investment from taxable income. This lowers the cost of capital, which induces more investment and higher productivity, leading to increased jobs, higher wages and economic growth.

Beginning in 2023, however, instead of 100 percent bonus depreciation, a phase-out begins, which allows for 20 percent less bonus depreciation each year until 2027 as follows:

- 2023 – 80%
- 2024 – 60%
- 2025 – 40%
- 2026 – 20%
- 2027 – 0%

The primary objective of the tax code is to pursue economic growth. We encourage Congress to reconsider this phase-out and support the *Accelerate Long-Term Investment Growth Now* (ALIGN) *Act* (S. 1117/H.R. 2406) legislation allowing bonus depreciation to continue.

Endnotes

1 See EY, Impact of the Amortization of Certain R&D Expenditures on R&D Spending in the U.S., released October 2019. https://investinamericasfuture.org/wp-content/uploads/2019/10/EY-RD-Coalition-TCJA-R-and-D-amortization-report-Oct-2019-1.pdf .