



Statement for the Record by:

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On Behalf of the Small Business & Entrepreneurship Council

"American Ingenuity: Promoting Innovation Through the Tax Code"

June 6, 2023

Small Business Committee

Subcommittee on Economic Growth, Tax, and Capital Access

U.S. House of Representatives

The Honorable Dan Meuser, Chairman

The Honorable Greg Landsman, Ranking Member

On behalf of the Small Business & Entrepreneurship Council (SBE Council), thank you hosting this important hearing and for the opportunity to submit a statement for the record. There is a long list of policy measures that Congress can and must consider to promote U.S. innovation and we are particularly pleased that the subcommittee is exploring how the tax code can encourage investment, which is the fuel for innovation and a vibrant competitive economy.

SBE Council has long supported tax measures and tax reforms that promote capital formation and investment. Our organization strongly supports 100% bonus depreciation, as it is a critical measure for encouraging investment, innovation and keeping the U.S. economy and our businesses competitive. This statement will focus on immediate expensing for qualified R&D expenditures, and our organization's support for restoring, enhancing and making permanent this important measure. SBE Council supports the bipartisan "American Innovation and Jobs Act" [introduced by Senators Maggie Hassan \(D-NH\) and Todd Young \(R-IN\)](#) in the U.S. Senate, and the bipartisan "American Innovation and R&D Competitiveness Act" [introduced by Representatives Ron Estes \(R-KS\) and John Larson \(D-CT\)](#) in the U.S. House.

As background, SBE Council is an advocacy, research and education organization dedicated to promoting entrepreneurship and protecting small businesses. For nearly 30 years, SBE Council has worked to advance a wide range of policy and private sector initiatives to improve the ecosystem for strong startup activity and small business growth. Our network of more than 100,000 member supporters, including entrepreneurs and small business owners, state and local business organizations, corporate partners and associations work with us to strengthen the environment for entrepreneurship, investment, innovation and job creation. Since our founding in 1994, SBE Council has helped to strengthen the ecosystem for small business and entrepreneurial success not only in the U.S., but across the globe.

Tax Certainty is Critical During This Period of Time

Inflation and economic uncertainty continue to bear down on small business America. On top of high prices, small firms are enduring labor shortages and higher labor costs, a more difficult time accessing capital, and an economy that remains challenging. That is why Congress must identify practical solutions to help entrepreneurs through this uncertain economic period, and beyond.

Small business owners and their employees across industries have had to continuously innovate in order to survive and thrive over the last several years. While the COVID economy imposed significant burdens and restrictions on small businesses, digital tools and changing consumer needs provided opportunities for innovation and new risk-taking. Many entrepreneurs and new startups tapped into immediate R&D expensing to support innovative investments and business growth.

For several decades, American businesses of all sizes have expensed R&D investments in the same year they occurred. This tax measure has helped to fuel hundreds of billions of dollars in R&D investments each year, and by extension has powered U.S. innovative leadership in the global marketplace. The tax credit's value to U.S. economic and technological leadership alone should move Congress to not only restore the credit but improve it so that more startups and new firms can effectively utilize it.

The immediate expensing of R&D investments has remained a long-term policy priority – through Democratic and Republican administrations alike – and right now is an ideal time to restore this effective policy. The stakes are quite high for this expensing measure.

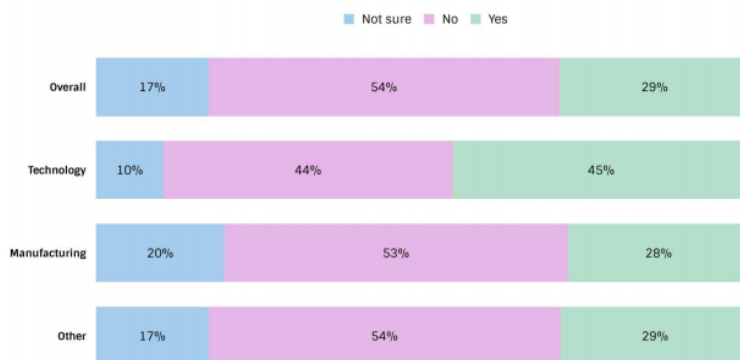
Failing to restore immediate R&D expensing would put all American businesses – but especially small businesses – at a competitive disadvantage. If not restored, the change in R&D tax credits would require companies to amortize their R&D expenses over five years. That extended timeline significantly limits businesses’ ability to develop new products, from medical devices to everyday consumer products. For smaller firms operating on thin margins and in a competitive and challenging environment, the inability to expense R&D costs for a given year means they cannot recover those costs in the same year. This makes it even more difficult for small businesses to effectively compete, invest, and take on bigger risks. Moreover, many small businesses are now looking at an expensive tax bill that threatens the competitiveness and innovative capacity of their firms, and the survival for a surprising number of firms.

Costly Impact for Small Businesses

In a new SBE Council/TechnoMetrica survey that will be released on June 6 – “Emerging Technology, Innovation and Small Business” – we specifically explore the small business impact of not restoring immediate R&D expensing. The results reveal harm and damage for our economy, local economies, investment, employees, and to the small businesses who have utilized this tax incentive.

The survey reveals that 29% of the small businesses we surveyed used immediate R&D expensing, and that 72% of those business owners who reported they used it knew that the write off was no longer available. So, for 28% of small business owners who used this tax incentive but were unaware that it is was no longer available, this was shocking news to a fair number of the entrepreneurs we surveyed.

R&D Tax Credit Is Used By One In Four Small Businesses, With Over Half Of All Small Technology Companies Taking Advantage Of It.

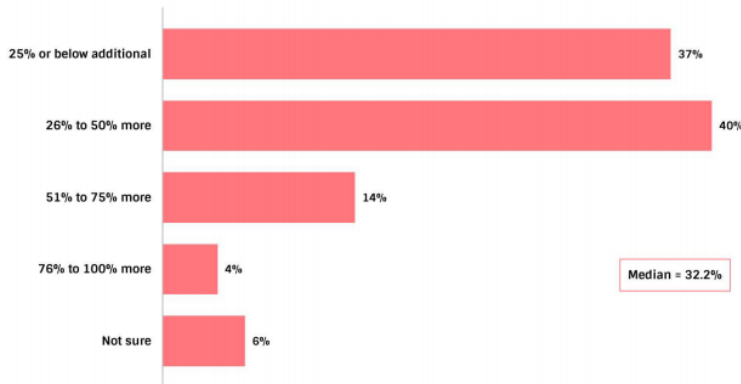


- Overall, 29% of small businesses have used the R&D tax credit.
- 54% have *not* used it, and another 17% are unsure.
- The usage is highest among tech companies at 45%.
- The use of the R&D tax credit by manufacturing companies at 28% is very similar to the overall 29%.

Q13: Many small businesses use the Research and Development (R&D) tax credit that allows for immediate expensing of research and development costs in the year these costs are incurred. Has your small business used this tax credit?, +/-4.7 PTS

In terms of financial impact, the small business owners we surveyed reported that the new (and unexpected for some) tax burden would be significant (see following two graphs). The median "tax hit" for small businesses is a 32% increase in their tax bill. The median dollar estimate is \$59,000. For some firms, the burden is much higher.

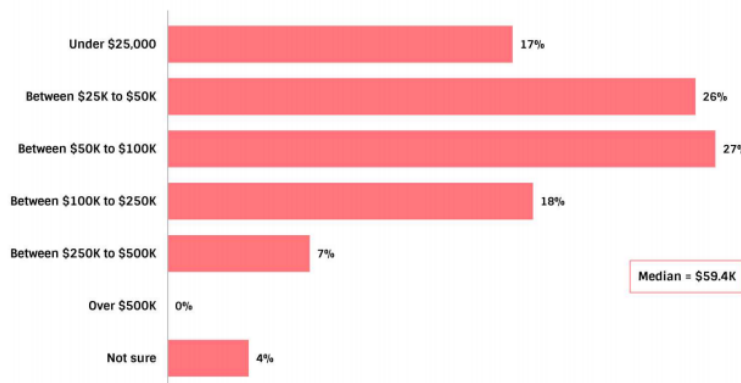
The Median Additional "Tax Hit" Is 32% If The R&D Tax Credit Is Not Renewed



Q15. If the R&D tax credit is not extended or made permanent for 2023, what is your business's approximate "tax hit"? How much will your tax bill go up? Base: 150 businesses that used R&D tax credit +/- 8.2 PTS

- Almost one-fifth of the small businesses who have used the tax credit, 18%, anticipate paying more than 50% extra in taxes.
- Four in ten, 40%, will pay 26%-50% more.
- A similar share, 37% will pay 25% or less extra.

The Median Additional Tax Hit Small Businesses Face Is \$59K

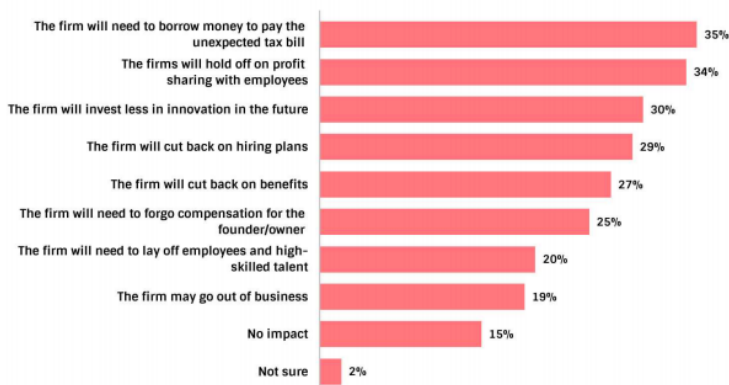


Q16. Approximately how much does this percentage equate to in actual dollars? Base: 150 businesses that used R&D tax credit +/- 8.2 PTS

- One-fourth of R&D tax credit users, 25%, expect \$100K+ additional tax hit.
- Another fourth, 27%, expect \$50K-\$100K. A similar share, 26% anticipates \$25K to \$50K in additional taxes.
- One in six, 17%, face under \$25K additional tax hit.

The negative effects of ending immediate R&D expensing extends beyond the financial strain on businesses. Indeed, 35% of small business owners report they will need to borrow money to pay the new tax bill, and 19% report that their firm *may go out of business*. Other impacts include: holding off profit sharing for employees, decreased investment in future innovations, scaled-back hiring plans, reduced employee benefits, laying off employees, and forgoing compensation for the owners or founder.

Negative Impact Of Ending R&D Tax Credits: Financial Strain, Hiring Cuts, and Dampened Innovation



Q17. If the R&D tax credit is not extended or made permanent for 2023, how will this impact the future of your business? (Please select all that apply)? (Please select all that apply). Base: 150 businesses that used R&D tax credit - / - 8.2 PTS

- The impact of not extending R&D tax credits for small businesses is far reaching.
- Financial strain: Small businesses may need to borrow money to pay unexpected tax bills (35%).
- Employee impact: Profit sharing with employees is likely to be delayed (34%).
- Reduced innovation: Investment in future innovation decreases (30%).
- Hiring and benefits cuts: Hiring plans are scaled back (29%), and employee benefits are reduced (27%).

Not surprisingly, small business owners that have utilized immediate R&D expensing overwhelmingly support bipartisan legislation to restore and make it permanent. Approximately 86% of small enterprises support a bill that aims to make immediate expensing of R&D costs a permanent provision, with additional enhancements for small businesses. Only 6% oppose this legislation, while 8% remain unsure.

As an important sidenote, I would like to add that the firms we surveyed are true small businesses. Of the 461 small businesses surveyed, only 11% are firms with between 51-100 employees. The remainder have 50 employees and fewer. The median number of employees on the payroll of small businesses surveyed was 11.5, and 36% have between 2 and 5 employees. These are the small businesses that drive innovation and local economies. Therefore, a new “tax hit” on the magnitude of between \$25,000-\$50,000 or more is very significant. It is likely why we see that 19% of the business owners we surveyed report that they may need to close the business due to this new financial burden. We anticipate that many of these businesses will also have a more difficult time accessing the loans that are needed to pay these new tax bills.

Challenging economic forecasts on top of the enduring pain points that have kept small businesses reeling for several years demand a policy response that will promote investment, certainty, and relief. Measures that stand behind and support the innovative practices and

investments of American small businesses are especially important now - for boosting the economy, moving to full recovery, and reaffirming America's role as an innovation powerhouse.

Small business owners and their employees need our elected leaders to come together on key issues such as this one. Immediate R&D expensing must be restored, made permanent, and hopefully enhanced without delay. Please let SBE Council how we can help the committee in advancing this important issue, or answering any questions you may have.

Thank you for your consideration in submitting this statement into the official record of this important hearing.

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