Plymouth Institute for Free Enterprise

Remove Tax Penalties Against Foreign R&D

Preston Brashers, Research Fellow

ADVANCING AMERICAN FREEDOM

TOPLINE: Congress should end the tax penalty against American companies that conduct research and development (R&D) outside the United States, except for in countries of concern like China.

BACKGROUND: Full and immediate deductions of legitimate business expenses ensure that companies pay taxes only on their profits. Deviations from full deductibility of valid expenses are problematic, as they can cause unprofitable companies to be taxed as though they were profitable.

Prior to 2022, businesses could immediately deduct R&D expenditures, as they can most other legitimate business expenses. Then, Congress allowed a delayed provision of the 2017 Tax Cuts and Jobs Act to take effect, which put in place 5-year amortization for domestic R&D and 15-year amortization for R&D conducted outside the United States. Companies that incurred domestic R&D costs could only deduct 20% of the expense per year over a 5-year period. Companies that incurred *foreign* R&D costs could deduct only about *6.7%* of the expense per year over a 15-year period. The One Big Beautiful Bill fixed the *domestic* R&D provision, once again allowing full and immediate expensing, but the 15-year amortization of foreign R&D was left in place.

Action Items (Congress):

- **End 15-year amortization for foreign R&D and allow full and immediate expensing** (except for R&D performed in countries of concern like China).

How It Would Make Life More Affordable:

- Removing barriers to companies performing R&D where it's most cost-effective would reduce the cost of bringing new products to consumers.
- It would encourage more robust competition in the development of innovative new technologies.
- It would make American companies more competitive by reducing their taxes and giving them more freedom to determine where business activities should be performed.
- It would better allow American workers to specialize in the activities where they are most productive and command the highest wages.

R&D Performed Abroad Often Results in New U.S.-Owned IP:

- U.S.-owned companies often have arrangements with foreign affiliates that give the U.S. company the rights to intellectual property resulting from R&D performed abroad.

BOTTOMLINE: There's no good economic justification for the tax code penalizing companies for conducting R&D. Congress should unleash more development of new and innovative products at lower costs by scrapping this misguided policy.