

**TESTIMONY OF THEA M. LEE  
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CONGRESS OF INDUSTRIAL ORGANIZATIONS  
BEFORE THE SENATE FINANCE COMMITTEE**

**"An Examination of U.S. Tax Policy and Its Effect on the Domestic  
and International Competitiveness of U.S.- Based Operations"**

**July 8, 2003**

Mr. Chairman, Senator Baucus, members of the Committee, I thank you for the opportunity to testify today on behalf of the 13 million working men and women of the AFL-CIO and the unions of the Industrial Union Council on the issue of U.S. tax policy and the state of American manufacturing.

We believe this hearing is timely for several reasons. First, with 56,000 more manufacturing jobs lost last month—the 35<sup>th</sup> straight month of industrial job loss—it is clear the crisis in this sector is deep, prolonged, and requires immediate attention. Second, the Senate will have an opportunity through its debate on a replacement for the Foreign Sales Corporation/Extra-Territorial Income Exclusion tax (FSC/ETI) to boost manufacturing in the United States, while also bringing our tax code into compliance with WTO rulings.

My testimony will focus on four key points: the dimensions of the crisis in manufacturing; the arguments in favor of a manufacturing tax benefit to replace the FSC/ETI; a critique of an alternative plan put forward by some in the Congress to replace the FSC/ETI with primarily offshore tax breaks; and the need to address the manufacturing crisis in a comprehensive way, including through health care reform and reform of our flawed trade policies.

**THE CRISIS IN MANUFACTURING**

According to last Thursday's unemployment figures, 56,000 manufacturing workers lost their jobs in June alone. For 35 straight months, manufacturing has lost jobs, the longest such stretch since the Great Depression. Since July of 2000, the United States has lost 2.6 million manufacturing jobs, nearly 13 percent of the total manufacturing workforce. Manufacturing job loss accounts for a staggering 90 percent-plus of total U.S. job loss since March 2001. As the chart I have included with my testimony shows, nearly every state in the nation has suffered heavy manufacturing job loss.

Unless these trends are reversed, America's working families – and the nation's economy – will continue to suffer serious and long-term damage. Manufacturing historically has been a major generator of good, high-skilled, well-paid jobs, with strong

linkages to jobs in non-manufacturing sectors, and it remains a mainstay of local and state economies throughout the nation. Because productivity growth (and therefore the potential for non-inflationary wage gains) has traditionally been greater in manufacturing than in services, the decline of manufacturing affects not only workers in manufacturing, but also contributes to the stagnation in all workers' wages. Moreover, the massive scale of manufacturing plant closings and job layoffs is contributing directly to the serious fiscal crises afflicting virtually every state in the nation.

The forthcoming debate on the FSC/ETI repeal gives Congress a crucial opportunity to help U.S.-based manufacturing by reorienting tax policy to help—rather than harm—the sector.

### **MANUFACTURING TAX BENEFIT**

Replacing the FSC/ETI with incentives to create and support U.S.-based manufacturing jobs is vital for the health of the industry and our entire economy. We believe that H.R. 1769, the Crane-Rangel-Manzullo-Levin bill, will help boost U.S.-based manufacturing, which is why the AFL-CIO strongly supports it. We look forward to working with a broad bipartisan coalition in Congress to build support for the bill.

H.R. 1769 would provide a tax benefit for production of goods in the United States, adjusted for the percentage of a company's worldwide production that takes place domestically. For instance, a company that makes all of its goods in the U.S. would be eligible for the entire benefit, while a company making half of its goods in the U.S. would receive half the benefit. In this way, the legislation would create an effective tax incentive to keep production in the United States. The legislation would also phase out FSC/ETI benefits over five years, allowing time for workers and companies who were FSC/ETI beneficiaries to adjust to a new system.

### **OFFSHORE TAX BREAKS**

Rep. Bill Thomas (R-Calif.), chairman of the House Ways and Means Committee, last year put forward a proposal to repeal the FSC/ETI and replace it with a collection of corporate tax cuts, most of which would mainly benefit companies with overseas production facilities. We urge the Senate to reject this approach.

Multinational corporations could accumulate untaxed profits overseas more easily because "base company" rules would be repealed. These rules now subject companies' profits to taxes in one or more countries. Multinational corporations would also get tax breaks by using rules that allow profits made in countries like Germany and France to be converted into tax deductions by paying "expenses" to wholly or partly owned companies in tax havens like the Cayman Islands.

This proposal, quite simply, would ship more manufacturing jobs abroad. According to news accounts last year, "Even some supporters of the [Thomas] bill said the ability of companies to avoid taxes on profits from factories abroad so long as they

were not returned to the United States encouraged American companies to invest, and create jobs, overseas.”<sup>1</sup>

It is bad enough that bureaucrats at the World Trade Organization (WTO) are requiring changes in our tax system, but it is even worse that some in Congress would respond to this challenge by making domestic manufacturing *less* competitive. The Thomas approach, though it has not yet been formally reintroduced this year, appears to define “enhancing American competitiveness” as boosting the profitability of multinational corporations to produce anywhere they choose, so long as they keep an American mailbox. We strongly encourage the Senate to reject it.

Our existing tax system—through foreign profit tax deferral, the foreign tax credit, and other provisions—already places American-based manufacturers at a terrible disadvantage compared to multinational firms that generate most production offshore. Those tax policies also urgently need to be fixed.

### **THE BROADER AGENDA**

The manufacturing tax benefit, taken alone, will have only a small effect on enhancing the competitiveness of U.S. manufacturing. It will improve our tax policy, but the AFL-CIO believes Congress should make other significant policy changes.

America’s manufacturing workers are the most productive in the world. But they operate under enormous competitive disadvantages resulting from several factors in addition to tax policy, such as unfair trade agreements, an overvalued dollar and foreign currency manipulation, inadequate investment incentives, health care costs not borne by overseas producers, and foreign government subsidies. Unless these problems are addressed soon, American manufacturing capacity and jobs may end up permanently lagging. And our economic strength may be permanently weakened: U.S. productivity and wage gains have been largely driven by the performance of our manufacturing sector.

We urge the Congress to start with passing a manufacturing tax benefit, but to make that only the first step of a more comprehensive effort. Thank you.

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<sup>1</sup> David Cay Johnston, “Bill Closing Bermuda Loophole Also Includes Tax Breaks,” *New York Times*, July 17, 2002.