

17 is Not Enough: The Case for a More Robust R&D Tax Credit

BY ROBERT D. ATKINSON AND SCOTT ANDES | FEBRUARY 2011

President Obama's call to increase the R&D tax credit from 14 to 17 percent is an important first step in restoring America's global innovation-based competitiveness. But if our nation is to really address the challenge—the “Sputnik moment” in the President's words—17 percent is not enough. Increasing the Alternative Simplified Credit (ASC) from 14 to 17 percent will move the United States from 17th place amongst OECD nations to 13th—an improvement to be sure—but one that will leave the United States far behind the global frontrunners in terms of R&D tax incentives. We urge Congress to take up the President's call to expand the credit, but expand it to at least 20 percent, as some in Congress have proposed.

The United States was first nation to realize the importance of spurring R&D through the tax code, putting in place the R&D credit in 1981. As a result, throughout the 1980s the United States had the most generous R&D tax incentive in the world. However, other nations learned from our success and began to not just copy us, but go beyond us. By 1996 the United States had fallen to seventh in R&D tax generosity among the 30 OECD nations, behind Spain, Australia, Canada, Denmark, the Netherlands, and France. And the slide continued. By 2004 we had fallen to 17th.¹ Even with the recent expansion of the ASC from 12 to 14 percent the United States was only able to hold position at 17th (and 19th for small businesses R&D incentives), as other nations also expanded their R&D tax incentives.² However it is not just OECD nations that have overtaken the United States, a number of other nations, including China, India, Brazil, and Singapore, provide more generous tax treatment for R&D expenditures.

This is one key reason why ITIF found that the United States ranked 30th of 40 nations in the rate of growth in corporate R&D from 1999 to 2006.³ Other nations are simply outcompeting us for research and development investments, and the jobs and economic activity that flow from them.

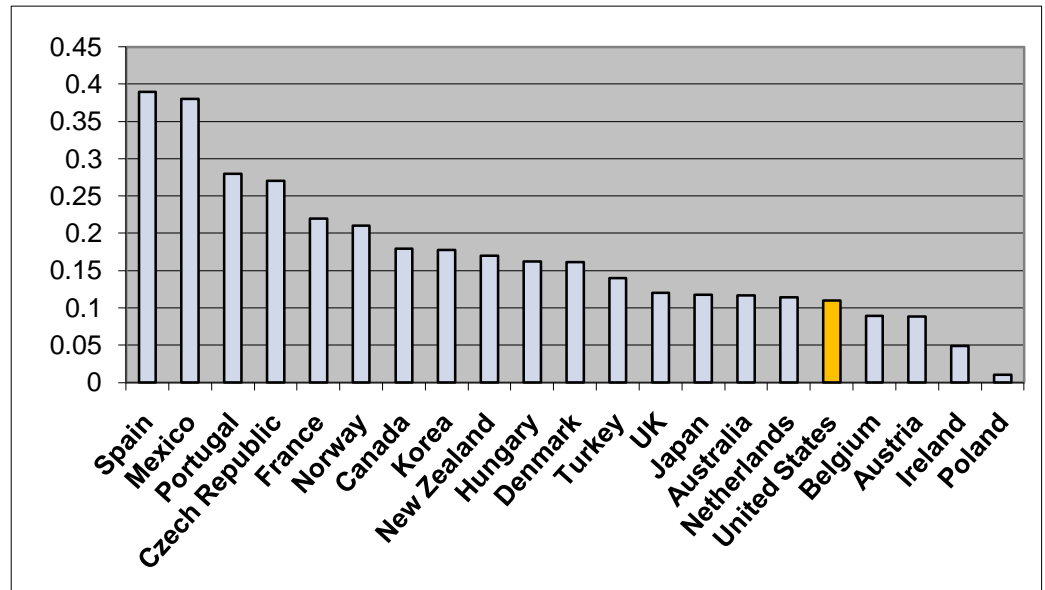


Figure 1: R&D Tax Generosity in OECD Nations, 2008

If the United States is to be more competitive for global R&D investment it needs expand the R&D tax credit beyond the President's proposal. Expanding the Alternative Simplified Credit as from 14 to 17 percent for would only move the United States from 17th in the OECD to 13th. If the United States increased the ASC to 20 percent it would move to 10th place. If we wanted to move to 5th place we would need a credit of 31 percent, to be number one, we'd need an ASC of 47 percent.

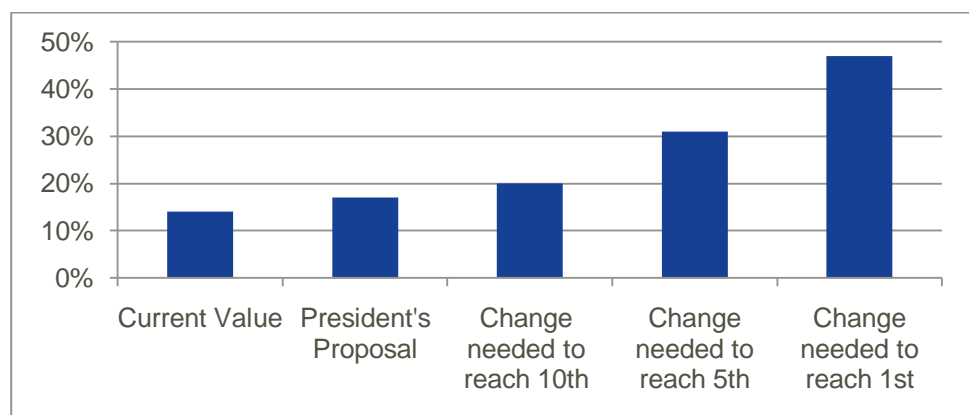


Figure 2: Value of the U.S. Alternative Simplified Credit change needed to increase OECD rank

R&D tax incentives have become a linchpin of tax policy throughout the world because they have proven to be an effective tool to increasing private sector innovation and

boosting economic growth. As ITIF has shown, increasing the R&D credit is not only an effective strategy for growing the U.S. economy it will also lead to more tax revenue, patents and jobs.⁴ There have been a wide range of studies by independent academic economists on the effect of R&D tax incentives on private sector research. For example, Bloom, Griffith and Van Reenen found that the credit stimulates an additional \$1.10 of research in the United States for every dollar of lost tax revenue.⁵

Moreover, as ITIF has estimated that expanding the Alternative Simplified Credit (ASC) from 14 percent to 20 percent would spur the creation of 162,000 jobs in the short run (and an additional, but unspecified, number of jobs in the longer run), increase GDP by \$66 billion annually and the number of patents filed by an estimated 3,800.⁶ Moreover, ITIF estimates that the credit would actually pay for itself in increased tax revenues over the course of 15 years. With the stakes so high, and the benefits so clear, now is the time to put in a place an R&D credit whose size matches the size of the challenge we face.

ENDNOTES

1. Jacek Warda, "Tax Treatment of Investment in Intellectual Assets: An International Comparison," *OECD Science, Technology and Industry Working Papers* 4 (Paris: OECD, 2006).
2. Jacek Warda, "R&D Tax Treatment in OECD Countries: Comparisons and Evaluations," (Paris: OECD, 2008).
3. Robert D. Atkinson and Scott Andes, "The Atlantic Century," The Information Technology and Innovation Foundation, Washington, D.C., 2009.
4. Robert Atkinson, "The Research and Experimental Tax Credit: A Critical Policy Tool for Boosting Research and Enhancing U.S. Economic Competitiveness," The Information Technology and Innovation Foundation, Washington, D.C., 2009.
5. Ibid.
6. Robert Atkinson, "Create Jobs by Expanding the R&D Tax Credit," The Information Technology and Innovation Foundation, Washington, D.C., 2010.

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The Information Technology and Innovation Foundation (ITIF) is a Washington, D.C.-based think tank at the cutting edge of designing innovation policies and exploring how advances in information technology will create new economic opportunities to improve the quality of life. Non-profit, and non-partisan, we offer pragmatic ideas that break free of economic philosophies born in eras long before the first punch card computer and well before the rise of modern China. ITIF, founded in 2006, is dedicated to conceiving and promoting the new ways of thinking about technology-driven productivity, competitiveness, and globalization that the 21st century demands.

ITIF publishes policy reports, holds forums and policy debates, advises elected officials and their staff, and is an active resource for the media. It develops new and creative policy proposals, analyzes existing policy issues through the lens of bolstering innovation and productivity, and opposes policies that hinder digital transformation and innovation.

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