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TECHNOLOGY COUNCILS OF NORTH AMERICA

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Submitted to:

House Committee on Small Business
2361 Rayburn House Office Building
Washington, D.C. 20515

Senate Committee on Small Business and Entrepreneurship
428A Russell Senate Office Building
Washington, D.C. 20510

Subject: Statement for the Record on Joint House & Senate Full Committee Hearing on Tax: "Prosperity on Main Street: Keeping Taxes Low for Small Businesses"

Chairwoman Ernst, Ranking Member Markey, Chairman Williams, Ranking Member Velázquez, and Members of the Committees:

Thank you for the opportunity to submit this written testimony. My name is Jennifer Young, and I serve as the Chief Executive Officer of the Technology Councils of North America (TECNA). TECNA represents approximately 60 regional technology trade organizations that collectively serve over 22,000 innovative, technology-driven small businesses throughout North America. These companies—ranging from enterprise software developers and medical device startups to AI research firms and manufacturing system engineers—are the engine of innovation and job creation in the United States.

Small businesses play a central role in America's innovation economy—driving nearly all net new job creation, generating breakthrough technologies, and powering the industries that define our future. The lifeblood of this innovation economy is research and development (R&D), which fuels new products, improves productivity, opens new markets, and enables U.S. companies to stay competitive in a rapidly evolving global landscape. Their ability to remain globally competitive hinges on robust, continuous investment in R&D. Unfortunately, the changes to Section 174 of the Internal Revenue Code, enacted as part of the Tax Cuts and Jobs Act (TCJA), have placed these businesses under immense financial strain, putting their growth, R&D capacity, and workforce at risk.

The Harmful Impact of Section 174 Amortization on Innovative Small Businesses

For nearly 70 years, U.S. companies could fully deduct R&D expenses in the year they were incurred—promoting innovation, attracting investment, and driving scientific and economic progress. However, since 2022, businesses must amortize these expenses over five years dramatically increasing their tax burden in the short term.

This policy shift has proven devastating for small, innovation-driven firms. Unlike large corporations with deep cash reserves, small businesses operate with tight margins and reinvest profits directly into engineering and product development. Amortization of R&D expenses effectively penalizes companies for doing what policymakers say they want to encourage: investing in the future.

TECNA members report consequences including:

- Dramatic tax increases despite no change in business fundamentals.
- The need to take out loans for the first time in decades just to cover tax bills.
- Layoffs of highly skilled engineers whose work is foundational to innovation.
- Lost market share to subsidized foreign competitors.

Member Case Studies: IntervalZero and DMSi Inc.

Let me share the stories of two innovative small businesses—IntervalZero in Massachusetts and DMSi Inc. in Nebraska—that are members of regional technology councils within the TECNA network. Their experiences exemplify the systemic harm caused by Section 174.

IntervalZero (Waltham, MA)

IntervalZero is a 54-person software company that helps run the robots and control systems behind many everyday products—like the aircraft you fly on, the cars you drive, and even the phones and computers you use. From training pilots in flight simulators to guiding robots that weld car frames or machines that cut and polish smartphone glass, IntervalZero's software is embedded in the manufacturing backbone of modern life.

Founded in 2008, IntervalZero grew steadily by prioritizing R&D – 68% of its team was dedicated to engineering, and profits were reinvested in innovation. But the changes to Section 174 upended their model. The shift from expensing to amortizing R&D meant that every dollar spent on innovation suddenly came with an additional tax liability. What was once a deliberate and successful business model—lean on management, heavy on engineering —became a cash-flow liability.

In 2022, Despite averaging just $222,000 in annual pre-tax profit, the company was hit with an unsustainable tax imbalance:

- $800,000 in 2022
- $600,000 in 2023
- $400,000 in 2024
- Projected $200,000 in 2025

These taxes weren't on profit—they were on payroll. The burden crushed cash flow and left IntervalZero scrambling to preserve its most valuable asset: its people. Letting go of even one engineer meant losing years of institutional knowledge, so the company froze hiring, wages, and spending. While they raised prices to stay afloat, global competitors—especially in China and Germany—slashed theirs, eroding the market share IntervalZero had built over a decade and sending revenues into decline.

To cover the growing tax burden and make payroll, IntervalZero first tapped its line of credit. But as revenue dropped, the bank withdrew it. With no other choice, the CEO and his wife used $1 million of personal savings just to make payroll and keep the team intact. Eventually, the company was forced to take on $1 million in loans, personally guaranteed by the CEO, to stay afloat. By the end of Q3 2024, the company had taken on $2 million in support—$1 million in loans and $1 million in personal savings—just to cover approximately $1.8 million in Section 174-related tax obligations.

In January 2025, after exhausting every alternative, they laid off 19 employees—35% of their workforce—including highly specialized engineers they had fought hard to retain. The result: lost productivity, delayed innovation, and a deep erosion of competitive advantage.

Despite returning to modest profitability in 2025, the company now faces nearly $1.5 million in loans and faces an estimated $170,000 in Section 174 taxes (down from $200,000 due to the layoff.) At its current pace, it will take at least five years—possibly a full decade—to recover enough to resume meaningful R&D investment. By then, the industry may have moved on, and with it, America's technological leadership in this critical sector.

DMSi Inc. (Omaha, NE)

DMSi is a true Main Street American success story. Based in Omaha, Nebraska, this homegrown tech company has quietly become the digital backbone of the U.S. lumber and building materials industry. Since 1976, DMSi has built software that helps local suppliers and lumber yards manage everything from inventory and customer orders to accounting, mobile apps, and business intelligence. Today, hundreds of companies across thousands of locations rely on DMSi's tools to operate efficiently, powering an essential industry that touches construction sites, small towns, and local economies across the country.

With a team of over 250 employees—nearly half of whom are software engineers—DMSi has grown by continually reinvesting in innovation. But when Section 174 amortization took effect, that model was turned upside down. In 2022, the company's taxable income shot to three times its book income, and its tax bill increased to four times what it had been—despite no substantial increase in actual revenue. In 2023, nearly all of DMSi's book income was projected to go to taxes, leaving little to invest in its people, products and growth. That math simply doesn't work for small, private businesses.

This is exactly the kind of company that Section 174 hurts the most—a deeply rooted, middle-America employer that serves an essential, real-world industry and reinvests in its workforce. Without relief, companies like DMSi will struggle to sustain growth, retain talent, and continue innovating—all while facing tax burdens that favor their larger or international competitors.

<u>Macroeconomic Implications</u>

What's happening to our members is not an anomaly—it's a warning sign. And it's not just a tax issue – it's a direct threat to America's innovation economy. The impact of Section 174 amortization is rippling through the economy, stalling innovation, costing jobs, and putting U.S. leadership at risk.

Since the amortization requirement took effect in 2022, the rate of growth in R&D spending has slowed dramatically. After growing at an average annual rate of 6.4% over the five years prior, R&D growth has decelerated for 10 consecutive quarters and now sits at less than half the pre-2022 rate[1]. This is not just a dip—it is a structural shift that, if not reversed soon, could lead to permanent reductions in R&D investment as projects are shelved and budgets are cut.

This is not the global standard. The United States is now one of only two developed countries that requires R&D amortization instead of allowing immediate expensing. In contrast, 17 countries offer super deductions, some of which allow deductions of more than 100% of eligible R&D expenses. China, for instance, has permanently expanded its R&D deduction, offering 20 times greater first-year deductibility than the U.S. for the same investment. These incentives matter, and capital is moving accordingly.

The implications go beyond economics—they touch national security. As outlined in the White House's *2024 Quadrennial Science and Technology Review*, "Science and technology are central to today's geopolitical competition and to the future of our national security, economy, and democracy. U.S. and allied leadership in science, technology, and innovation has long underpinned our economic prosperity and military strength." The report further emphasizes that "our national research, development, and engineering capabilities across the public and private sector" are essential to protecting national security. Weakening America's innovation base weakens our strategic posture and our ability to lead.

Congress must act this year to restore full, immediate deductibility of R&D expenses and protect the innovation capacity of American businesses—especially the small and mid-sized companies that are most vulnerable. Failure to act risks not only our economy, but our future.

<u>Our Request to Congress</u>

TECNA respectfully urges Congress to restore 100% immediate expensing of R&D costs under Section 174—and provide retroactive relief to 2022 for small businesses.

We recognize that fully retroactive relief for all companies may face fiscal constraints. However, a targeted, retroactive carve-out for small businesses is both achievable and essential. These companies lacked financial flexibility to weather the sudden change in tax policy and, unlike large corporations, had no reserves or international tax strategies to buffer the impact. As a result, they were forced to take on debt, drain personal savings, lay off skilled workers, and halt innovation.

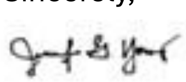
Providing retroactive relief for small, R&D-intensive businesses would:

- Allow innovative companies to recover unjust tax burdens that were applied to salaries and investments already made in good faith.
- Enable repayment of emergency loans and personal capital used just to keep operations afloat and teams intact.
- Restart stalled hiring and product development cycles, reenergizing the innovation pipeline at the heart of U.S. job creation.
- Reaffirm America's global leadership in innovation, particularly among the small firms that drive agility, competition, and technological breakthroughs.

This is a pivotal moment. The damage from Section 174 is real, measurable, and growing. Without swift legislative action, we risk watching some of our most promising tech innovators downsize, sell to foreign competitors, or shut their doors entirely.

Thank you for your time and for your commitment to supporting America's innovation economy.

Sincerely,



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[1] https://fred.stlouisfed.org/series/Y006RX1Q020SBEA#0