October 7, 2024

The Honorable Lloyd Smucker
Chair, Main Street Tax Team
Committee on Ways and Means
U.S. House of Representatives
Washington, D.C. 20515

The Honorable Greg Steube
Vice Chair, Main Street Tax Team
Committee on Ways and Means
U.S. House of Representatives
Washington, D.C. 20515

Dear Chair Smucker, Vice Chair Steube and Members of the Main Street Tax Team:

On behalf of the National Association of Wholesaler-Distributors (NAW), I urge you to extend key tax policies enacted in the *Tax Cuts and Jobs Act of 2017 (TCJA)*. These policies help wholesaler-distributors and main street businesses across the country.

Specifically, I urge you to make the 199A deduction for small businesses permanent in order to ensure wholesaler-distributors can continue investing in their workforce and local communities. Individual tax rates should be extended to provide continued tax relief for small businesses that file through the individual side of the code, and for the six million workers employed by the industry. In addition, the death tax should be repealed to provide family-owned businesses relief

About NAW & The Wholesale Distribution Industry

NAW is one of America's leading trade associations, representing the $8 trillion wholesale distribution industry. Founded in 1946, NAW comprises national, regional, and state employers of all sizes, industry trade associations, partners, and stakeholders spanning all distribution sectors.

There are more than 250,000 wholesale distribution companies that operate across North America, including all 50 states. These businesses collectively employ over 6.1 million workers, ranging in size from small, closely held family businesses to Fortune 500 companies. The majority are small or medium sized businesses and 81% of companies in the industry have less than 20 employees.

Wholesale distribution is a business-to-business industry: wholesaler-distributors purchase inventory, generally from manufacturers, and sell it to their customers, which include retailers, consumers, contractors, and small businesses.

Wholesaler-distributors are typically high tax, low margin businesses. The industry pays one of the highest effective income tax rates of all industries, with many businesses paying an average effective rate of 30% in combined federal and state taxes. Although the data varies among distributors of different product lines, a significant number of companies report after-tax profit margins of less than 1%, with the average margin of about 2%.

Wholesaler-distributors also offer well-paying, skilled jobs with a culture of living in and giving back to the communities they serve. Employee costs including wages, benefits, and taxes make up half to three-fourths of total expenses for wholesaler-distributors. As of August 2024, the average hourly wage for production and nonsupervisory workers in the industry of $31.28 per hour, higher than the typical private sector non-supervisory wage.[1] 89% of wholesaler-distributors offer healthcare, 89% offer paid sick leave and 84% offer retirement benefit plans.[2]

The 199A Small Business Deduction is Crucial to Wholesaler-Distributors

The majority of businesses, including most wholesaler-distributors, are organized as pass-through businesses (S-corporations, LLCs, sole proprietorships, or partnerships) and pay taxes through the individual income tax section of the code, rather than the corporate tax rate. Over 95% of businesses in the U.S. are pass-throughs and collectively employ more than 78 million Americans.

These businesses benefit from the 20% Section 199A small business deduction, created by the TCJA. In combination with the reduction of the individual tax rate to 37%, the TCJA lowered the top tax rate on pass-through businesses to 29.6%.

This tax cut helped wholesaler-distributors reinvest in their workforce by giving them more resources to hire, raise wages, and provide benefits while also allowing them to devote more resources toward expanding their business and contributing to their local communities.

NAW members invest heavily in their workforce by providing extensive benefits and career development programs including health & retirement benefits, formal profit-sharing, quarterly cash bonuses and personal benefits such as financial workshops and volunteer paid time off.

Unfortunately, because of budgetary rules this tax cut expires at the end of 2025. If lawmakers fail to act, pass-throughs could face a top tax rate of 39.6%, which will threaten the ability of the industry to continue re-investing in workers and communities. It will also make it more challenging for pass-through businesses to compete with large, publicly traded C-corporations, especially in attracting and retaining talent given today's tight labor market.

With the 199A small business deduction in law, S-corps and other pass-through businesses have effective tax rates of between 27% and 34%, rates comparable to C-corporations, which face effective rates between 25% and 31%, according to EY.[3] On the other hand, if 199A expires, passthroughs will face significantly higher effective rates as high as 41%.

This will harm businesses across the country. According to IRS Statistics of Income (SOI) data, almost 25.7 million taxpayers claimed the 199A deduction in tax year 2021.[4] The deduction currently supports 2.6

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[1] U.S. Bureau of Labor Statistics. (2024, September 6). *Table B-8. average hourly and weekly earnings of production and nonsupervisory employees on private nonfarm payrolls by industry sector, seasonally adjusted(1) - 2024 M08 results*. U.S. Bureau of Labor Statistics. https://www.bls.gov/news.release/empsit.t24.htm
[2] U.S. Bureau of Labor Statistics. (n.d.). *Industries at a glance: Wholesale trade: NAICS 42*. U.S. Bureau of Labor Statistics. https://www.bls.gov/iag/tgs/iag42.htm
[3] *The Importance of 199A*. The S Corporation Association. (2023, June 22). https://s-corp.org/2023/06/the-importance-of-199a/
[4] *SOI Tax Stats - Historic table 2*. Internal Revenue Service. (n.d.). https://www.irs.gov/statistics/soi-tax-stats-historic-table-2

million jobs, $161 billion in annual employee compensation, and $325 billion in GDP when accounting for direct, supplier, and consumer economic activity, according to EY.[5]

The 199A deduction also includes guardrails to ensure it goes to small businesses that are creating jobs and that the provision is not abused.[6] According to Treasury, these guardrails reduce qualifying 199A income by about 40%, so the starting rate for a pass-through can easily be higher than the 29.6% rate created by the deduction. The provision is also not a giveaway to "the rich" as some critics have alleged. According to a report by the Congressional Research Service (CRS), the 199A deduction is distributionally neutral as it reduces taxes for pass-through businesses equally across all income levels:

> "The Section 199A deduction appears to have little effect on vertical equity, as it does not appear to diminish the progressivity of the federal income tax."[7]

Since it was enacted into law, the 199A deduction has helped small businesses including wholesaler-distributors reinvest in their local communities and their workforce. It has helped these businesses create quality, high paying jobs and grow the economy. Lawmakers should extend the provision.

Lawmakers Should Keep Individual Tax Rates Low

In addition to cutting small business taxes through the creation of the 20% pass-through deduction, the TCJA also reduced individual tax rates paid by pass-through businesses. Not only did this provide tax reduction for S-corporations, LLCs, and other pass-through entities, but it also reduced taxes for workers at every income level.

The TCJA reduced marginal tax rates, raised thresholds at which the higher brackets phased in, and doubled the standard deduction. Similar to the 199A deduction, these tax cuts are set to sunset at the end of 2025 and should be extended by lawmakers.

These tax cuts provided especially strong tax reduction for lower income taxpayers. According to IRS SOI data, Americans with adjusted gross income (AGI) of $50,000 to $100,000 saw a reduction in average tax liabilities of over 13% between 2017 and 2018, while Americans with AGI of $1 million or above saw a 5.8% reduction.[8]

Given wholesaler-distributors collectively employ more than six million workers, these tax provisions helped both small businesses and the workers they employ.

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[5] EY Prepared on behalf of the S Corporation Association. (2024, August). Economic activity supported by the Section 199A deduction. S Corporation Association. https://s-corp.org/wp-content/uploads/2024/09/EY-SCA-Economic-activity-supported-by-Section-199A-deduction-August-2024-FINAL.pdf

[6] *The "Experts" Get 199A Wrong, Part 2*. The S Corporation Association. (2024, June 5). https://s-corp.org/2024/06/the-experts-get-199a-wrong-part-2/

[7] Guenther, G. (2024, February 28). *Section 199A Deduction: Economic Effects and Policy Issues*. Congressional Research Service. https://crsreports.congress.gov/product/pdf/R/R46650

[8] *ICYMI: IRS Data: Middle class Americans saw biggest tax reduction from Trump Tax Cuts: U.S. senator Chuck Grassley of Iowa.* Home. (2020, September 23). https://www.grassley.senate.gov/news/news-releases/icymi-irs-data-middle-class-americans-saw-biggest-tax-reduction-trump-tax-cuts

However, if these tax cuts are allowed to expire, workers at every income level and small businesses across the country will see a tax increase in 2025 at a time that businesses and families have recently been hit hard by rising prices, supply chain breakdown and economic uncertainty. ‘

The Death Tax Imposes Unfair Burdens on Family-owned Wholesaler-Distributors

In addition to providing continued tax rate reduction, lawmakers should ensure small businesses have relief from the death tax, also known as the estate tax.

The death tax imposes a 40% tax on family-owned businesses tax every time the next generation takes over the business. Family-owned businesses employ over 60% of the U.S. workforce and contribute over 60% of GDP, which has a significant economic impact.[9]

While there is currently a $13 million exemption on the death tax, this figure is on total assets, not on income and is scheduled to be cut in half at the end of 2025.

Since the tax is imposed on assets, not income, businesses are often forced to liquidate assets such as structures, equipment, and land to pay the tax. This significantly hinders entrepreneurial activity because many family businesses do not have sufficient cash to pay estate tax liabilities.

Wealthy Americans frequently mitigate or avoid the death tax through the creation of trusts and foundations, however these tactics are often not available to cash-poor, asset-rich family-owned businesses. As a result, the tax disproportionately falls on these businesses, which include many wholesaler-distributors and an estimated 40% of NAW members.

Wholesaler-distributors hit with the death tax have to take out loans, liquidate existing assets or defer new investments in technology or equipment, hiring new workers or upskilling existing workers, and expanding their business.

In addition, many family businesses below this threshold must devote time and resources to estate planning in the event they may one day have to pay the tax. While this cost may or may not be significant by itself, this is yet another expense faced by wholesaler-distributors on top of complying with existing and new regulations, mitigating supply chain disruptions, and rising costs including energy, health care, and labor costs.

This is another competitive disadvantage that family-owned businesses face compared to publicly traded corporations, which never die and never face the death tax. It makes these businesses vulnerable to acquisition by large corporations or foreign entities, and often forces family-owned businesses to liquidate a portion of the business to pay for the tax.

[9] Van Der Vliet, D. (2021, June 2). *Measuring the Financial Impact of Family Businesses on the US Economy*. Family Business. https://familybusiness.org/content/measuring-the-financial-impact-of-family-businesses-on-the-US-ec

Conclusion

Thank you for the opportunity to submit comments to the Main Street Tax Team. As a vital part of the nation's supply chain, wholesaler-distributors depend on sound, pro-growth tax policies that help businesses re-invest in their workforce and their local communities, and continue growing and expanding. We urge you to make key tax provisions permanent including the 199A small business deduction and lower individual tax rates, and fully repeal the death tax.

If you or your staff have any questions, please reach out directly to me or to Alex Hendrie, Associate Vice President, Government Relations at 202-872-0885.

Sincerely,

Brian Wild
Chief Government Relations Officer
National Association of Wholesaler-Distributors