Investing in America: A Policy Framework to Stop Corporate Offshoring and Strengthen the Middle Class

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Highlights

- There is evidence of a troubling, decades-long trend of a shrinking middle class, due in part to a decline in manufacturing employment and short-term corporate decision-making.
- Just as corporations have an obligation to shareholders, policymakers have a responsibility to taxpayers, working families, and the American economy.
- That responsibility should be reflected in federal policy, which must be designed to encourage companies to invest domestically and penalize those that ship jobs to countries like Mexico and China.

Recommendations

- Tax incentives intended to support United States businesses and the domestic economy should go to companies that invest here at home.
- Federal contracts, funded by taxpayers, should go to American companies that employ American workers.
- Federal policies should encourage businesses to return foreign jobs to the United States to invest in low-income and rural communities.

I. Introduction

The United States was built on a social contract between businesses and workers—a mutual understanding that the success of one contributes to the success of the other. Yet, in recent decades, the U.S. has witnessed a shift of domestic manufacturing to low-cost, low-wage countries. While this shift is the result of a number of factors—including the rise of the global economy, global trade policies, and a corporate focus on short-term profits—the loss of U.S. manufacturing jobs and the shrinking middle class have devastated families and communities in states like Indiana. There must be an effort by policymakers to reverse the decades-long trend of the middle class losing economic ground.

Perhaps more troubling is that federal policy too often rewards and even encourages the movement of American jobs overseas and does not do enough to encourage investment in the foundation of the economy—American workers, their families, and communities. This paper provides an overview of corporate offshoring—the practice of moving business activities to foreign countries to take advantage of lower costs—and outlines policy recommendations designed to strengthen the economy by rewarding American companies that invest here and penalizing those that ship jobs abroad.

II. Two Thousand Hoosier Jobs to Mexico; More to Follow?

In February 2016, United Technologies Corporation—a Fortune 50 company that owns both Carrier and UTEC—announced that it will eliminate 2,100 jobs at their Indiana facilities in order to aggressively cut costs by pursuing low-wage labor in Mexico.[1,2]

Since the 1950s, workers in Indiana have helped build the Carrier brand into a leading manufacturer of furnace and air-conditioning systems. The strength of the brand has contributed to record profits for United Technologies—including more than $6 billion last year alone. United Technologies also benefits from billions of dollars in federal contracts purchased with taxpayer dollars.

Despite the dedicated workforce in Indiana and the financial support of taxpayers, the company argues that the relocation to Mexico is necessary to cut costs by taking advantage of $3 an hour wages, significantly lower than $20 an hour average wages paid to current employees.[3] In fact, executives from United Technologies confirmed that every dollar—$65 million—saved in the move will come from cheaper labor.[4,5]

More troublesome, Robert McDonough, President of United Technologies Climate, Controls & Security, subsequently told investors that the company sees further opportunities to cut costs by shifting more U.S. jobs to low-wage countries.[6]

This corporate decision was the ultimate betrayal for the Hoosier workers at Carrier and UTEC. A profitable company built upon American labor, ingenuity, and infrastructure, with mostly an American customer base, is now shifting production and distribution to Mexico. The decision-making at United Technologies is reflective of broader problems in the American economy, particularly the shrinking middle class, and misplaced policy priorities.

III. Corporate Short-Termism and the Shrinking Middle Class

Corporations have an obligation to shareholders to build and maintain strong, profitable companies, and executive job security and compensation are often tied to increasing shareholder value. These pressures, however, have translated into a phenomenon known as

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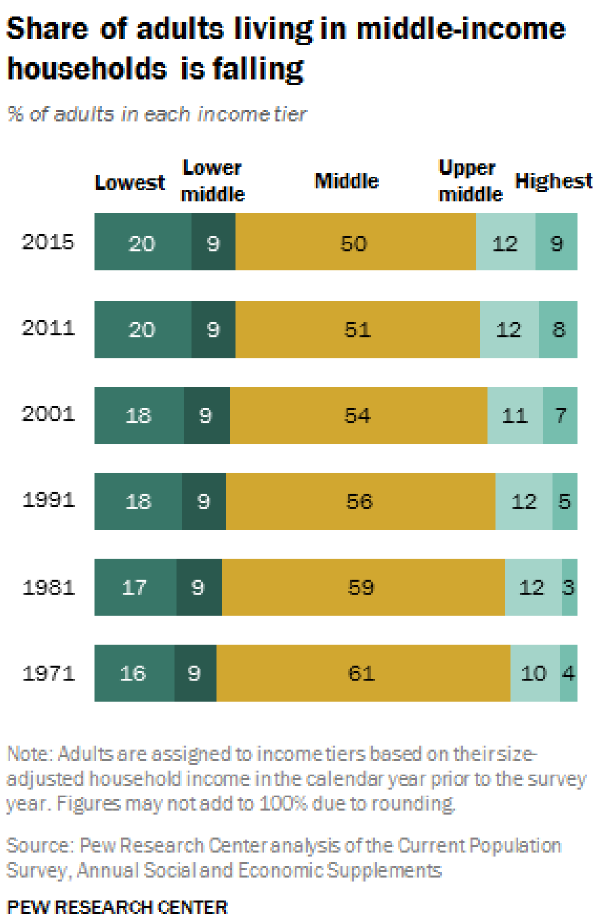
1 http://fortune-500.silk.co/page/United-Technologies
2 https://www.carrier.com/carrier/en/us/news/statements/
3 http://abcnews.go.com/Business/1400-workers-devastated-carriers-plan-move-indianapolis-facility/story?id=36986150
4 http://www.theindychannel.com/news/local-news/call-6-carrier-said-it-might-stay-if-workers-cut-their-pay-to-585-an-hour
5 http://www.donnelly.senate.gov/newsroom/press/donnelly-statement-following-meeting-with-united-technologies-executive
6 http://www.donnelly.senate.gov/newsroom/press/donnelly-statement-on-united-technologies-executive-confirming-corporations-moving-jobs-to-mexico-to-chase-cheap-wages

"corporate short-termism"—the prioritization of quick profits, often at the expense of the long-term viability of the company.

The concern with short-termism is shared by BlackRock CEO Larry Fink, head of the world's biggest investment company, who recently sent a letter to S&P 500 CEOs lamenting that "many companies continue to engage in practices that may undermine their ability to invest for the future." He suggests, instead, that CEOs focus on "long-term value creation."[7]

Demands from shareholders and the resulting focus on short-term gains, along with declining manufacturing employment as described below, are among the many factors that have contributed to a shrinking middle class in America. As a recent Pew Research Center report detailed, "since 1971, each decade has ended with a smaller share of adults living in middle-income households than at the beginning of the decade."[8]

Chart 1: THE SHRINKING MIDDLE CLASS



Source: Pew Research Center:
http://www.pewsocialtrends.org/2015/12/09/the-american-middle-class-is-losing-ground/

[7] http://www.businessinsider.com/blackrock-ceo-larry-fink-letter-to-sp-500-ceos-2016-2
[8] http://www.pewsocialtrends.org/2015/12/09/the-american-middle-class-is-losing-ground/

In order to build and maintain a successful business, executives have a responsibility not just to investors, but also to workers, consumers, and the long-term health of the company. The Carrier and UTEC decisions demonstrate that corporate short-termism often results in the working- and middle-class paying the price.

IV. Manufacturing and Corporate Offshoring

In the 1800s and early 1900s, American productivity and ingenuity—from Eli Whitney to Henry Ford—resulted in major technological advances, and America unquestionably became the dominant global manufacturing power by the end of World War II. By the end of the 20th century, however, the rest of the world caught up, and American workers began losing jobs as offshoring began and factories closed. According to the U.S. Bureau of Labor Statistics (BLS), U.S. manufacturing peaked in 1979 at nearly 20 million workers.[9] Today, domestic manufacturing supports roughly 12 million workers.

Chart 2: MANUFACTURING EMPLOYMENT

Source: U.S. Bureau of Labor Statistics:
http://www.bls.gov/careeroutlook/2014/article/manufacturing.htm

United Technologies is not the only company to lay off American workers in favor of foreign workers. Recently, there was similar outcry in Chicago when Nabisco decided to ship 600 jobs to Mexico. In fact, a review of the U.S. Department of Labor's Trade Adjustment Assistance program shows as many as 100,000 workers claiming job losses in recent years due to production or services moving to a foreign country.[10]

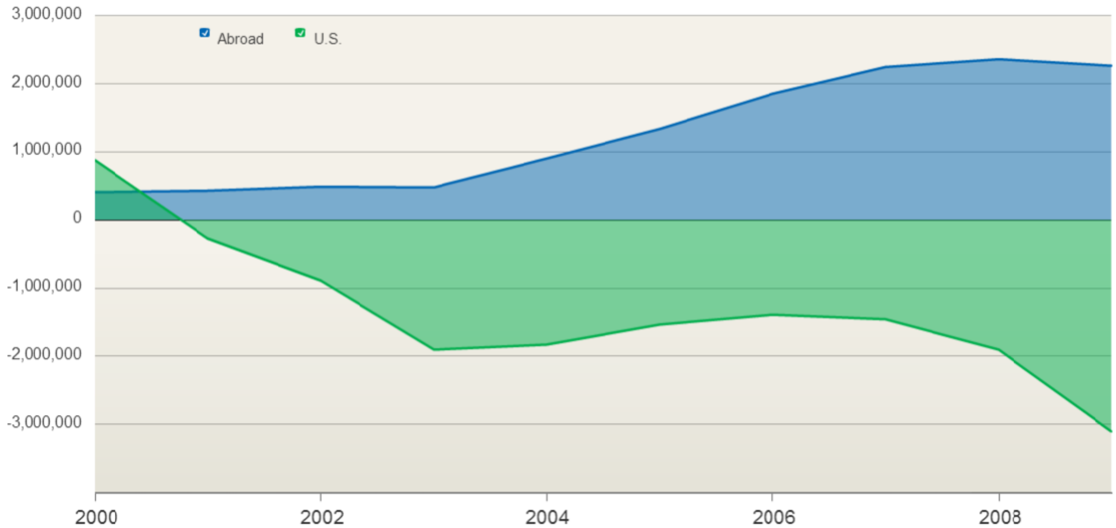
It is important to note that the flow of jobs is not entirely a one-way street. It is widely reported that some corporations have begun reshoring jobs, but, unfortunately, as a 2015 A.T. Kearney report argues, "the rate of reshoring actually lagged that of offshoring between 2009 and 2013, as the growth of overall domestic U.S. manufacturing activity

[9] http://www.bls.gov/careeroutlook/2014/article/manufacturing.htm
[10] https://www.doleta.gov/tradeact/docs/AnnualReport14.pdf

failed to keep pace with the import of offshore manufactured goods over the five-year period."

Similarly, U.S. Department of Commerce data provides further evidence of multi-national corporations cutting U.S. employment by two million during the 2000s, while increasing foreign employment by 2.4 million.[11]

Chart 3: JOB CREATION AT MULTI-NATIONAL CORPORATIONS



Source: Wall Street Journal: http://www.wsj.com/news/interactive/MULTINATL0419

It is reasonable to assume that corporations will continue to make decisions to advance both their short-term and long-term corporate objectives. It is also reasonable for U.S. policymakers to do the same through policies that support short- and long-term economic objectives by encouraging companies to locate and invest domestically.

V. Policy Recommendations to Stop Offshoring

There is no single solution to prevent major corporations from moving manufacturing to low-cost, low-wage countries. However, the federal government does have a responsibility to ensure that U.S. policies are designed to strengthen the American economy and support the American worker.

Congress can help retain and create good-paying jobs by investing in infrastructure, education, and workforce development; by developing tax policies that encourage long-term performance; and through the careful creation of smart regulatory policies that protect consumers while allowing business growth.

Similarly, smart trade agreements hold the potential to strengthen both the U.S. and global economies. Though past trade agreements have brought lower cost goods and services to consumers, it is often at the expense of American job losses and wage stagnation. Strong

[11] http://www.wsj.com/articles/SB10001424052702303990604577367881972648906

trade policies should benefit American workers and not result in devastated manufacturing communities.

In addition to these broad public policy challenges, policymakers have an obligation to ensure U.S. policies—including tax breaks, federal contracts, and other government incentives—are designed to benefit the U.S. economy. That includes closing loopholes exploited by corporations that often harm American workers and communities. To that end, below are a number of policy recommendations crafted to ensure federal policies support the American worker and domestic economy.

A. **Deny Expensing for Offshore Moving Costs:** When corporations fire American workers and send those jobs abroad, that corporation should not be permitted to write off moving costs. It is fundamentally unfair that when companies move operations overseas the taxpayer subsidizes its moving expenses.

B. **Claw-Back and Restrict Tax Incentives:** When corporations offshore jobs, taxpayers should be reimbursed for the recent grants and tax breaks received at those facilities. And going forward, taxpayers expect tax breaks to go to companies that invest here in America. Therefore, companies that offshore jobs should be restricted from claiming future tax breaks like Section 199, LIFO, and lower cost of market.

C. **Offshoring as a Factor in Federal Contracting:** As federal contracting officers decide which goods and services to purchase with U.S. tax dollars, they consider a host of factors including cost, past performance, and technical quality. They should also consider whether the bidding corporation has pursued cheaper foreign labor at the expense of American workers. This would allow offshoring to be considered a negative factor in contracting decisions, including as a potential negative price preference.

D. **Incentives to Invest in Rural and Low-Income Communities:** By offering tax breaks to companies that re-shore jobs from foreign countries to low-income and rural communities in the U.S., we can reward companies that choose to hire American workers, while encouraging economic growth.

VI. Conclusion

Just as corporations have an obligation to their shareholders, U.S. policymakers have an obligation to taxpayers to enact and maintain policies that support American workers, communities, and the economy. United Technologies is not the first company to offshore jobs in order to chase short-term profits, and it will not be the last. That is why federal policy must foster a culture that prioritizes investment in America in order to help the middle class grow and achieve sustained economic success.