February 26, 2019

CC:PA:LPD:PR
(REG-106089-18)
Internal Revenue Service
1111 Constitution Avenue, NW
Washington, DC  20224

Submitted via Regulations.gov

Re: Comments on REG-106089-18, Limitation on Deduction for Business Interest Expense

Dear Sir or Madam:

The American Supply Association (ASA) appreciates the opportunity to comment on REG-106089-18, Limitation on Deduction for Business Interest Notice of Proposed Rulemaking (83 Fed. Reg. 67490, Dec. 28, 2018). ASA believes that the IRS’s acceptance of comments and feedback is an important step toward implementing the various intricacies of IRC §163(j).

ASA is the national association serving the interests of Plumbing, Heating, Cooling and Piping, and Pipe, Valves and Fittings (PHCP-PVF) industry stakeholders which provide manufacturing and distribution services to residential, commercial and industrial customers. Members of ASA include the industry’s largest national wholesaler-distributors whose customers are often independent, family-owned companies. Members also include manufacturers and independent reps for some of the nation’s largest consumer brands and producers of the industry’s key commodities.

Background

ASA was pleased to see the Tax Cut and Jobs Act (TJCA) signed into law by President Trump. But ASA has concerns about TCJA’s substantial amending of §163(j) by placing additional limitations on the deduction of the business interest expense for taxpayers and expanding the group of taxpayers to which it applies.

The new §163(j) that applies through the end of 2021 is based on a revised formula to determine the amount that businesses can deduct. The amount cannot be more than 30% of earnings before interest, taxes, depreciation, and amortization (commonly known as EBITDA).

The IRS’s Proposed Rule would limit the formula to exclude depreciation and amortization. This would make the amount that businesses could deduct even smaller. This proposed IRS formula would essentially go beyond an EBITDA formula and would immensely affect ASA members’ tax liability in a negative manner.
Recommendation

Current interest expense regulations already negatively impact some ASA members and one supplier member informed ASA that the IRS’s proposed changes will make the impact even more significant. This company and other ASA members operate in an industry that requires a large investment in working capital items (such as inventory and accounts receivable). Based on their capital structure, they borrow to fund working capital needs. Even in today’s low interest rate economy, this company will already have to reduce their interest expense deduction by about $300,000 for their 2018 corporate tax return.

If these new §163(j) regulations are effective for the 2018 tax year, the deduction limit for this company and others will be further diminished. And company management believes this will occur even as interest rates continue to rise.

Also, in today’s business environment, this company and other ASA members must continually reinvest profits into fixed assets to grow and remain competitive. As they grow, their working capital needs will grow, too, and needed reinvestment will increase their future depreciation expenses. By limiting the ability to fully utilize the long-standing business interest deduction to facilitate this business activity, their growth will be hampered which translates to hiring fewer employees.

While the Proposed Rule’s definition of a taxpayer’s adjusted taxable income (ATI) for a taxable year would not go into effect until Jan. 1, 2022, ASA is concerned that the IRS’s administrative interpretation of TJCA language for §163(j) conflicts with what lawmakers intended. Thus, if it was Congress’s intent for the EBITDA test to be in current effect, it would have stated so in the TCJA legislation.

ASA is pleased to see that the proposed new IRS limitations on business interest do not apply to certain small businesses, which are defined using a gross-receipts test of $25 million or less, but ASA is concerned that a portion of its membership likely will not qualify for this exception. Also, this enlightened approach to small business does not negate ASA’s overall concerns with the IRS’s current interpretation of §163(j) and implementation of the entire Proposed Rule.

Therefore, ASA recommends that the IRS provide additional guidance related to the mechanics of determining the business interest expense limitation and clarify the application of §163(j) to align with the intent of Congress.

Sincerely,

Catherine Treadwell Perry, J.D.
Director of Government Relations