

Testimony of Richard Hampton
Chairman of the Board, Circuit Interruption Technology Inc.
Hearing before the Joint Economic Committee
“Unleashing America’s Economic Potential”

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Chairman Paulsen, Ranking Member Heinrich, and members of the Committee, thank you for this opportunity to testify on “Unleashing America’s Economic Potential” through the perspective of one small but growing family-owned business in Rogers, Minnesota.

Our Company

My name is Rick Hampton, and I am Chairman of the Board of Circuit Interruption Technology, Inc. CIT is truly a family business. It was started in 1999 by my son, Jeffrey, shortly after he graduated from Metropolitan State University business school. Jeff, who is here with me today, was an entrepreneur from an early age. In junior high he sold gum out of his locker. In high school, he started a very successful lawn and landscaping business. That financed his way through college and provided seed money to start CIT. CIT began in my home, staffed by Jeff and my wife Sharon. It moved from selling fuses and circuit breakers to a line of business I had experience with, electro-mechanical relays and switches. We now do business as CIT RELAY & SWITCH.

For a variety of reasons, there are virtually no manufacturers of our kind of products left in America, so we contract with manufacturing facilities in China and Korea. Our engineering staff creates the design in consultation with Asian engineering affiliates. CIT is committed to the highest quality possible. Our specifications frequently exceed those of our competition, making CIT often the first choice in critical or problem applications. Our employee base continues to grow in all sectors of our business. We also support other jobs, including 94 independent sales representatives, and sell through nearly 100 distributor locations throughout the United States.

Our customers are mostly North American original equipment manufacturers, many of which are household names. Our relays and switches are used in countless products you’ll find in your home, office, on the road, in restaurants or parking lots, or even on aircraft carriers. When you send your child off to school on a “Yellow Bus,” start your washer or dishwasher, drive on a golf course, or mix your favorite health drink, you may well be depending upon a quality CIT product.

Today, my son is President and CEO, I am Chairman of the Board, my wife Sharon is Chief Financial Officer, and my daughter Nicole—a successful businesswoman in her own right—handles International Distribution and Sales Management. Four years ago we moved from a smaller facility in Spring Lake Park to a larger facility in Rogers, and since then we have expanded from 12 to 22 employees. We invest in our employees, paying them well, helping them advance professionally, and even helping them through rough patches in their lives.

Pre December 2017 Tax Consequence:

The long-term drag of a burdensome tax system likely played a role in the migration of relay and switch manufacturing from North America to Asia and mostly China. Other factors involved cheap labor and low regulatory burdens. The migration accelerated as China aggressively sought manufacturing facilities and technology transfers. Fewer component part suppliers remained in America, driving up costs. Inevitably, this was followed by fewer technical personnel skilled in production.

Manufacturing and the transfer of technical know-how enabled China to become skilled in metallurgy, magnetics, polymers, and other elements of sophisticated manufacturing.

All the while, the high average tax on CIT profits resulted in a less-than-desirable business approach from an accounting standpoint. Essentially, the tax system punished us for keeping profits in the company.

As a family-owned business it was clear that \$1.00 in profit would be subject to an initial corporate tax of 37%; followed by roughly another 37% Federal personal tax when it was taken out as income, and another 8% in Minnesota State tax, leaving us with less than 35 cents of the original \$1.00. To avoid this double taxation professional accountants agreed the best approach would be to take out 100% of the profit, subject it to a one-time Federal and State personal tax, which would retain more than 50% of the original dollar. Those net dollars could then be re-invested in the company. The negative impact of this approach was highlighted recently when CIT applied for an expansion of its credit card line of credit. Due to what appeared to be low income on sales of \$10,000,000, the credit company denied our request. The re-invested dollars were clearly shown on our balance sheet but were seen as a CIT liability, not retained earnings.

December 22, 2017, Tax Reform Changed our Business Model

CIT made a plan in the event tax reform actually became law. We determined that we would:

- Provide a bonus of one extra week pay to all employees;
- Fund our employee 401K program with no matching required at 5% of employee 2017 W-2 income, including the bonus;
- Launch a lab and facilities construction program estimated between \$140,000~\$200,000;
- Increase our employee base by 10%;
- Extend a \$1000 bonus to employees achieving their 10-year milestone of employment;
- Establish a fund to evaluate the possibility of bringing manufacturing back to America; and
- Changing our budgeted forecast from 5% growth to 15% in 2018

All of the above have been implemented. We are now projecting additional changes in the near term:

- We will retain 2018 profit in the business, meaning that after tax we will be able to keep 79% of the profit as retained earnings in the company.
- We anticipate expanding hiring by another 10% by year's end.
- We anticipate repeating the 5% 401K contribution and extra one-week year-end bonus.
- We are projecting 30% growth 2019.

Additional Thoughts on Manufacturing Our Products in America

While tax reform was great news, the remaining barriers to manufacturing our products in America are two-fold:

- CIT would need to compete with companies receiving direct assistance and subsidies from the China government.
- We would have to navigate the plethora of regulations from various domestic County, State and Federal agencies.

We think that CIT specialization and quality can meet the first challenge. The second, however, is more daunting as the unknowns become known only through the process of re-introducing manufacturing in America. The ultimate cost may be unknowable until far along in the process, making this barrier the most frightening of all; for a small business such as ours taking such a risk could even lead to the very extinction of the Company.

Tariffs

Since tariffs are in the news and have a direct effect on CIT let me say a word about the proposed tariff on relays in particular. As there are virtually no general-line relay manufacturers remaining in the United States, here is how I assess the potential impact:

1. The affected products are broad. The average automobile uses over 20 relays. In addition to all vehicle types they are used in computers, security, thermostats, furnaces, humidifiers, appliances such as washers and dryers, industrial and restaurant ovens, heating and air conditioning, as well as medical and military uses. There are simply too many product applications to mention.
2. An exclusive China tariff will provide a corresponding competitive edge to relay manufacturers currently located in Canada, Mexico, and Europe, providing them a 25% price advantage and potentially damaging CIT's ability to survive.
3. A specific China manufacturer with a solid foothold in the United States is State-Owned and thus any tariff may be potentially reimbursed to this China manufacturer, allowing them to maintain price while CIT must increase theirs 25%, resulting in an unintended consequence of increasing the growing dominance of China over this critical component.

Conclusion

While companies like CIT Relay & Switch continue to face a host of regulatory and other challenges, tax reform has been and will continue to be a tremendous help to our business and employees. We are in the process of developing a longer term approach to expanding our business model from private-label manufacturing outside the United States to re-shoring manufacturing in America. In conjunction with this approach CIT will be hiring added technical staff to help explore this process. We'll hire additional staff to expand new products, some of which will meet the demand for relays to support electric automobile charging stations and specialty relays used to reduce energy used for office lighting. CIT will take the necessary steps to position itself to meet the growing desire by our customers for US-made quality and improved logistics that ultimately result from domestic US manufacturing.

I believe the lower tax will allow CIT Relay & Switch to position itself for continued growth for the coming decade. More might be done, but this historical change alone is energizing and exciting to all our team, employees and management alike.

Thank you again for this opportunity to testify, and I look forward to any questions you may have.