taxnotes® state

Volume 95, Number 1 ■ January 6, 2020

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Reprinted from *Tax Notes State*, January 6, 2020, p. 53

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In this article, the authors discuss state, county, and local-level credits and incentives that a company should consider in evaluating investment into the U.S.

Companies that are seeking to expand and invest into the United States have myriad tax considerations to evaluate. These considerations can include not only federally imposed taxes, but also state, county, and city taxes based on the locations where the company intends to do business. While understanding the tax requirements associated with these jurisdictions can be complex, there are numerous state, county, and local credits and incentives that a company should consider in evaluating investment into the United States.

Introduction to U.S. Taxes

Evaluation of a foreign direct investment into the United States requires understanding that state and local tax regimes independently impose compliance and payment requirements in addition to a company's federal tax obligations. More than 40 states, the District of Columbia, and many localities (such as cities or counties) impose some type of income-based tax on corporations and other businesses, and many states also impose franchise taxes for the privilege of doing business in their state. Franchise taxes are generally based on net income, net worth, or gross receipts of the business. Additionally, 45 states and the District of Columbia, and nearly 10,000 local jurisdictions, impose transaction-based sales and use taxes on qualifying retail sales of tangible personal property and various services. Sales and use taxes apply to all entity types in every industry, and in virtually every state, resulting in a highly fragmented and complex indirect tax regime requiring careful diligence to navigate.

Applicable to all state and local taxes, there is a minimum threshold of business activity that must be present before a taxing jurisdiction has the right to tax a company. This concept is called nexus, and for state tax purposes, the analysis is completely independent of whether the company has a permanent establishment in the United States. Additionally, companies operating under treaty protection for federal purposes may still face state and local tax obligations. Nexus thresholds vary by state and have been changing rapidly following the 2018 seminal decision of *South Dakota v. Wayfair Inc.*[1]

[1] 585 U.S. ___, 138 S. Ct. 2080 (2018).

There are a handful of other tax types that a company should consider, from property tax (generally at the county or city level) to state and local gross receipts taxes. Any entity doing business in the United States should review the laws for each state and locality where it does business to ensure compliance with the myriad potential subnational taxes, particularly entities with employees, physical locations, stored inventory, or sales to locations in the United States. These companies are likely subject to one or more of these tax types. Companies investing into the United States need to remember that state income tax is a completely different regime than federal income tax, so a company may owe $0 of federal income tax but still have state and local tax liabilities.

Credits and Incentives in the United States

States and localities use a slew of tax credits and incentives to encourage companies to engage in economic activity that aligns with the jurisdictions' goals. These goals include geographic targeting that will target economic growth in specific communities, focusing on industries perceived to be high-value, or focusing on the attraction or retention on high-paying jobs.

The economic activities that are most often encouraged through state and local tax credits and incentives are job creation or retention, capital investment, and new technology development. These programs can influence a business location decision by making a location relatively more cost effective for the business to locate there. The form of these benefits can vary by jurisdiction, but generally can include cash grants, property tax abatements, sales tax exemptions, utility rate reductions, infrastructure grants, fee waivers, state income tax credits, building reuse or redevelopment grants, and much more.

While state and local jurisdictions have discretion in awarding a number of these benefits, the programs tend to be long-standing and generally available to any company that meets program criteria. Credits and incentives programs are just one component of a jurisdiction's economic development framework. On the business side, a tax incentive will offset business costs; on the government side, a tax incentive will stimulate investment and provide new jobs in the area and therefore increase the tax base.

Securing Credits and Incentives

State and local tax incentives are generally secured through some interaction with the relevant economic development agency. In addition, there are benefits that are secured through a company's tax return and are administered by the jurisdiction's taxing authority. These incentives can be based on the company meeting quantitative metrics, such as several jobs created, amount of capital investment, or other criteria as negotiated with the relevant agency.

Although the nature of the program and the exact process needed to secure the benefit varies by jurisdiction, there are several common items that companies need to keep in mind. The timing on when a company should begin discussions with an economic development agent and apply for these benefits is critical. As compared to credits and incentives in several non-U.S. jurisdictions where funding can be secured well after initiation of a company expansion, U.S.-based programs almost always require that a company secure program funding before initiation of an expansion project. Baked into all these programs is the concept that the credit or incentive is an inducement for the company to undertake the project and that without the inducement, the project would likely not occur. As such, many companies that are undergoing foreign investment in the United States frequently fail to consider incentives before a project commences, thus increasing the risk that the incentives will not be received.

Another element that companies should consider is timing of the benefit. Frequently, state- or local-level credits and incentives provide benefits over a multiyear basis. By spreading out benefits over a multiyear period, jurisdictions can better tie the receipt of the benefit to the project's performance. By contrast, many non-U.S. programs are front-loaded one-time payments that occur on approval. Understanding when a company can expect to receive the benefits can be critical to properly understanding and measuring the company's financial economics around the expansion.

In addition to the timing, companies need to be aware of how any credit or incentive they secure is monetized. Depending on the nature of the underlying program, the benefit may be in the form of — but not limited to — a cash grant, an income tax credit, a reduction or abatement in sales tax, a similar reduction or abatement of property taxes, low-cost or interest-free financing, and nonfinancial items such as infrastructure improvements and expedited permitting. Companies need to make sure that the credit or incentive being offered is in the form that a company can use. A tax credit, for example, for a company that will pay little to no income tax may ultimately be of little value to that company.

Finally, companies that are seeking credits and incentives from state or local jurisdictions need to be aware that the process of receiving the benefit does not end with the award. In almost all instances, companies must go through an application process, which varies in difficulty by jurisdiction, once the benefit is awarded. In addition, there is frequently multiyear reporting that must be done for companies to maintain any benefits that were awarded. Again, this contrasts with many programs that operate outside the United States.

Typical State and Local Tax Incentives

Most of the credits and incentives programs are triggered by job creation or retention, capital investment, and technology development and deployment. The nature of these programs and the benefit amounts can vary widely by jurisdiction. As foreign companies evaluate potential credits and incentives that may be available to support their U.S. investment strategy, they must understand the mechanics of these programs. Doing so will allow these companies to target jurisdictions that have programs that can support the investment objectives of their expansion.

Job Creation or Retention Programs

Nearly every state has some variation of a jobs-based credits and incentives program, which rewards companies that either add new jobs or can verify that they retained jobs that otherwise would have been lost. Some states use jobs as the unit of measurement while others use the dollar value of payroll. Under these programs participating companies will receive — depending on the program — either a credit against, or reduction of, a state or local tax that may be otherwise due, or a cash grant based on the number of jobs created or retained. In each of these instances, companies must satisfy qualifications regarding the amount, type, or pay of the jobs created. Finally, it is not uncommon for a jurisdiction to limit these benefits to industries that align with that jurisdiction's overall economic strategy.

For example, Delaware provides for a credit of $500 against a corporation's income tax liability for each new job created in the state.[2] The company must have hired five or more qualified employees, make an investment of at least $200,000 in a qualified facility, and be engaged in a qualified activity. To claim the credit — and as an example of the compliance burden that can be associated with some of these credits — the taxpayer must complete an application and receive written notice of approval from the Division of Revenue before the credit can be claimed on a tax return.

Mississippi, however, which provides a similar benefit based on the number of newly created jobs, ties the benefit to the payroll of the qualifying employees. Qualifying companies can claim a corporate income tax credit equal to 2.5 percent of the employees' pay,[3] rather than a fixed amount per employee as in Delaware.

Additionally, some states have job-creation credits for hiring from some populations. Arizona, for example, provides for a corporate income tax credit for a portion of an employee's wages if the employee is an Arizona resident receiving state assistance for needy families.[4] The credit can be taken only during the employee's first three years of employment.

All these programs provide companies with a benefit related to creating jobs, even though the basis of the credit or benefit amount varies

[2] Del. Code Ann. title 30, section 2011 et seq.

[3] Miss. Admin. Code 35.X.01.

[4] Ariz. Rev. Stat. section 43-1175.

dramatically. As companies evaluate U.S. expansion, they should be cognizant of the various job-related credits and incentives programs so that they can align expansion plans with jurisdictions that provide programs to support their activity.

Capital Investment

In addition to providing some type of jobs-related credits and incentives program, most jurisdictions provide benefits to support capital investment. Many states seek to encourage manufacturers to invest in their states through a series of credits and incentives programs tied to capital investment. Kentucky, for example, offers a sales tax exemption for manufacturers that purchase personal property to be used directly in the manufacturing or industrial process for new and expanded operations in Kentucky.[5] New York similarly uses credits and incentives to encourage manufacturers to invest in the state. However, New York provides companies with a refundable tax credit equal to 2 percent of qualified investment, which must be negotiated with the state's economic development agency.[6] Programs like these seek to encourage companies to invest in manufacturing locations in their states.

Technology

The last main area that drives credits and incentives is when jurisdictions seek to attract high-technology companies through a variety of credits and incentives. As with jobs and capital investment-based programs, there is a tremendous amount of variance between the states. This can include everything from a sales tax exemption for e-commerce in West Virginia[7] to a comprehensive set of tax incentives for high-technology companies in the District of Columbia.[8] Programs like these are designed to attract high-paying jobs and highly educated employees to the region, which would diversify the area's economy and expand its tax base.

Finally, many states offer research and development tax credits to encourage companies to perform research in their respective jurisdictions. In New York, for example, a firm that meets minimum established job and investment thresholds may qualify for a credit against its corporate income tax for up to 50 percent of its federal R&D credit.[9] For Virginia's local business, professional, and occupational license tax, a company that designs, develops, or creates computer software at a Virginia location may qualify to exclude these receipts from its tax base.[10]

As with jobs and investment-based credits and incentives programs, companies need to fully understand the technology components of their expansion projects to fully match their activity with available programs.

Targeted Geographic Considerations

The final consideration for companies that are evaluating credits and incentives to support their investment into the United States, is that these programs are frequently location-specific. States and localities often target specific geographic areas for economic development purposes. The goal behind these target programs is that significant credits and incentives will lead companies to expand in targeted areas, leading to more jobs and more economic activity.

Many states have specially designated economic development zones, sometimes called enterprise zones, which are designated areas of high unemployment or declining property values that jurisdictions set aside for favorable treatment. Louisiana, for example, provides enterprise zone credits and incentives providing either a rebate on sales tax paid for qualifying materials, machinery, furniture, and equipment, or a refundable investment tax credit of 1.5 percent of the capital investment in the project.[11] The business must create a minimum number of jobs and a minimum

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[5]Ky. Rev. Stat. Ann. section 139.480(10).

[6]N.Y. Tax Law section 31(a)(2).

[7]W. Va. Code section 11-15-9h(a)(7).

[8]D.C. Office of Tax & Revenue, Qualified High Technology Companies. The QHTC program for qualified entities includes a reduced corporate income tax rate, a credit for wages paid to qualified employees, an exemption from sales tax for certain sales made by QHTCs, and partial reduction in the personal property tax, among other benefits.

[9]N.Y. Tax Law section 31(a)(3).

[10]*See, e.g.*, Loudoun County, Virginia Code section 840.11(a).

[11]La. Stat. Ann. section 51:1787.

number must be individuals from targeted groups.

Cities such as Chicago have also created tax increment financing (TIF) districts for incentives to develop in even more localized areas.[12] In these programs, the TIF district's tax revenue does not go into the city's general fund but remains in the district to fund redevelopment or more investment.

In both situations, as well as with location-targeted programs in other jurisdictions, the exact street address matters. Frequently, these economic development zones are drawn so that they encompass highly defined areas in a state or locality. As such, companies cannot rely on merely locating in a jurisdiction that contains one of the economic development zones. Companies must analyze this potential benefit based on the actual physical location of their perspective project.

Ongoing Considerations

This article merely scratches the surface of the credits and incentives that are available to companies making inbound investments into the United States, but aims to serve as a brief overview of the programs that might be available as well as some considerations in securing these benefits. It is imperative that companies seeking to expand their presence in the United States fully understand the nature of their expansion to fully match those factors with a host of available credits and incentives. ■

[12] City of Chicago Planning and Development, Tax Increment Financing (TIF).