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Make the case

Navigating the tax credit challenges of COVID-19

From bankable revenue to benefits in doubt.

The stay-at-home orders and economic impacts of COVID-19 put tax credits and incentives programs for many organizations in jeopardy. Ongoing requirements previously agreed to as part of federal, state, or local programs about a certain number of new hires or a sustainable construction project were suddenly unachievable. The financial perks organizations would get in exchange for their investment in the respective jurisdiction were suddenly inaccessible.

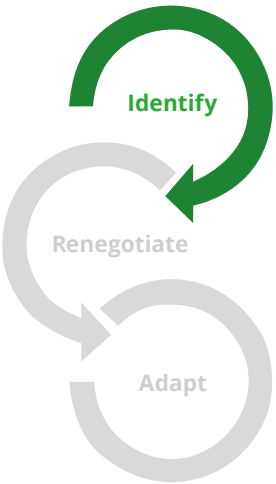
Their tax teams didn't see it coming. Or was it their real estate teams? Talent, maybe?

Yes, just determining who in the organization has responsibility for credits and incentives was one of the first challenges faced by many organizations in response to the impact of COVID-19. In many cases, oversight was distributed based on the nature of the programs, which were siloed and managed in different ways. Once the question of oversight is untangled, there's that whole matter of "What do we do now?" and then "Let's make sure this never happens again."

These challenges are particularly applicable to state and local programs. While federal programs are typically available to organizations that achieve certain statutory requirements, state and local incentives are often individually negotiated programs. In many, benefits are received when the company meets the milestones. In others, benefits are offered on the front end in anticipation of the company meeting the requirements. Force majeure or other similar clauses may have been included in the agreement between the company and the jurisdiction; however, the company's legal counsel should be consulted to vet whether the pandemic is considered among the "act of God" events covered by such terms.

Organizations need to understand the impact of not meeting agreed-upon milestones in their state and local programs, then act proactively today and in the future to avoid being penalized for unforeseen crises such as COVID-19.

It can be a lot to manage. And there's a lot at stake. So let's take it step by step.



Identify your problem areas

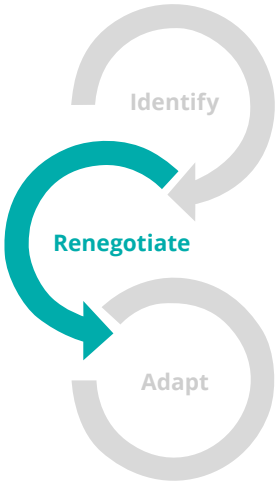
Large organizations that operate in multiple states and cities can have a thick portfolio of incentive programs. Keeping them on track depends on cross-functional communication and collaboration.

The nature of tax credits and incentives programs varies. So do organizational approaches to managing them. As a result, these programs may be overseen by anyone from tax to facilities to talent. Combine this decentralization with the individualized nature of state and local programs—with their differing timelines, percentage-of-completion clauses, and clawback provisions—and you have a potentially challenging management situation.

One of the first steps to making sure your overall incentives program remains good for your bottom line is to identify parts that might not be breaking even. It is critical to set up a cross-functional team tasked with centralizing management of all your programs. This dedicated task force can help you more efficiently flag COVID-19–affected tax credits and incentives programs featuring milestones you may struggle to meet. For one program, it could be that a hiring freeze didn't allow you to add the number of new employees required under the terms of the incentive. For another, revenue shortfalls and stay-at-home mandates might have made efficiency improvements at your facility untenable.

Who needs a seat at the table?
A cross-functional task force focused on centralizing and managing your credits and incentives should include representatives from numerous teams.

Prioritizing problem areas requires an understanding of their potential business impact. By centralizing oversight of your incentives program, you can effectively calculate what not meeting them might mean. Have you already received dollars that will be clawed back, or is it solely future benefits that are at stake? How have those benefits been accounted for in future budgets, and what would not receiving them mean? Being able to answer questions like these lays the groundwork for the actions you may take next.



Renegotiation considerations

After you identify your COVID-19–affected tax credits and incentives, you can try to address them through renegotiation. Prepare your case by examining the factors beyond your control that explain your inability to meet the required milestones. If you're a retailer, your state's or city's indoor shopping limits might have made the growth necessary for meeting the terms of the incentive agreement unrealistic. Or maybe you're a manufacturer, and a key part of your supply chain suffered as a result of a particularly bad COVID-19 outbreak that significantly reduced revenue.

Once your case is prepared, make it. Identify and get in touch with the key individuals at the state or local authority where your problem programs reside. As you seek changes to the program's terms, keep in mind that the original arrangement was likely mutually beneficial. You may have been getting incentives, while the local community was getting its citizens new job opportunities or improved infrastructure. The investments made in local communities often provide more value to the community than having the community claw back, or not pay, the incentive dollars. It will most likely be in the community's best interest to renegotiate the program's terms.

It may be in the authority's interest to continue the program, even if it now has a longer timeline (like extending a three-year window to five years) or revised expectations (like dropping the required number of new hires by 20%).

Timing is critical to fruitful renegotiation. Have the foresight to initiate these conversations well before tkey milestone dates in your program. Doing so can provide the time needed to work out key details comfortably.

Renegotiating problematic incentive programs today is akin to patching a leak. It needs to be done, and it might hold for a while, but it's no guarantee the same problem won't turn up in the future.

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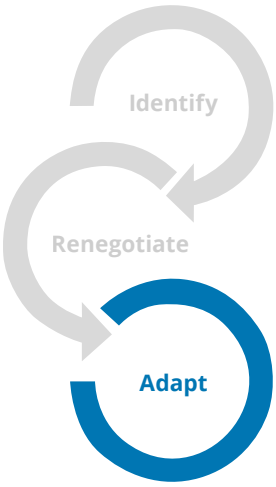

Adapt your program going forward

After renegotiating problematic programs, it's important to document key takeaways that could support more efficient incentives processes down the road. Here are some actions you can take to future-proof your credits and incentives organization:

Keep a cross-functional team to identify problem programs in place. It will be critical to centralizing tax credits and incentives from various departments and monitoring potentially hard-to-meet milestones going forward.

Track potential negative business impacts of not meeting milestones. Those impacts should be accounted for in future budgets and capital plans to avoid being pushed into panic mode by clawbacks or unconveyed dollars.

Discuss with counsel the potential to incorporate language addressing unforeseen events (like the COVID-19 pandemic) into program language in the future, perhaps including language that would trigger renegotiation or timeline extension in the event of a massive, economy-disrupting event. Your new cross-functional tax credits and incentives team can keep track of best practices and standardize them across your organization.

So what's the state of federal tax credits and incentives?

Unlike many state and local programs, federal tax credits and incentives are generally statutory by nature and widely available to businesses who meet certain criteria when tax time rolls around.

The federal government has enacted initiatives to address the pandemic's impact, such as the Employee Retention Credit under the CARES Act. The Employee Retention Credit is a fully refundable tax credit for eligible employers equal to 50% of qualified wages ("Qualified Wages") in 2020 and 70% of qualified wages in 2021 that eligible employers ("Eligible Employers") pay their employees after March 12, 2020, and before December 31, 2021. Each employee could have $10,000 in qualified wages in 2020 and $10,000 per quarter in qualified wages in 2021. That means employers could potentially obtain $5,000 per employee in credits in 2020 and $28,000 per employee in credits in 2021.

As the economy recovers and more companies hire new employees, the long-standing federal Work Opportunity Tax Credit (WOTC) program is another initiative companies can pursue. WOTC can help companies benefit from income tax credits based on the hiring of veterans, individuals who have been unemployed for a specific amount of time, and individuals who have received qualifying public assistance that meets specific criteria.

Because they're administered differently than state and local programs, previously obtained federal tax credits and incentives may not have similar risk. Giving them a fresh look is critical to enhancing your benefits today and into the future.

Unexpected shouldn't mean unprepared

COVID-19 derailed many organizations' state and local tax credits and incentives programs. But keeping them on track shouldn't end with the end of the pandemic. Unforeseen events will likely continue to surprise companies. Even relatively small events may put at risk vital benefits that organizations considered part of current or future revenue.

Coming through the pandemic with a centralized and efficient tax credits and incentives program can put your organization on strong footing. By identifying your COVID-19–affected agreements, renegotiating them when possible, and improving oversight going forward, your incentives program can better handle whatever the future brings.

Keeping those benefits bankable is a process. Are you ready to take the first step?

Contact us to discuss more

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