SIFM

Credits and Incentives Overview: Generating and Monetizing tax credits

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Incentives overview/triggers

- Governments around the world use tax and non-tax incentives to encourage capital expenditure, job creation, and certain business activities (e.g., R&D, employee training, sustainability initiatives).
- Many business activities can trigger incentives opportunities:
  - Capital expenditures and routine spend (real and/or personal property)
  - Job creation, reduction or relocation
  - Facility expansion, modernization, remodeling or acquisition
  - Greenfield
  - Joint ventures / mergers and acquisitions
  - Equipment replacement / retooling
  - Research and development
  - Training expenditures
  - Lease expiration or renewal
  - Sustainability / green initiatives
- Certain incentives are available if the company meets defined statutory requirements while others require advanced approval or must be negotiated with the government prior to the company publicly announcing the project, acquiring land, etc.

Types of statutory and discretionary business incentives

Statutory: Automatic ("as of right")	*Statutory: Pre-approval or Prior Certification Required*	*Discretionary ("but for")*
‣ Statutory tax credits & incentives that are provided to companies "as of right" if meet defined statutory requirements ‣ Pre-certification or prior approval not required	‣ Statutory tax credits & incentives that require companies to meet additional approval qualifications within state and local regulations	‣ Customized financial incentive packages that are negotiated with state and local government agencies

Sample incentives by region/country

Canada
- Training reimbursements
- R&D credit
- Sustainability incentives

USA
- Cash grants
- Tax credits, exemptions, abatements, and rebates
- R&D incentives
- Infrastructure funding
- Sustainability incentives
- Training benefits

Europe
- Cash grants
- Training subsidies
- Tax incentives
- Patent boxes and R&D incentives

Japan
- Cash grants
- Tax credits
- Local rent and hiring subsidies
- R&D tax credit

ASEAN
- Tax incentives for regional hub/HQ
- R&D incentives

Potential Federal Tax Credit Opportunities

Jurisdiction	Benefit Type	Description	Benefit	Retrospective vs. Prospective
Federal FMLA credit	Federal Income Tax Credit	Credit for a percentage of wages paid to qualified employees while on qualified family or medical leave	Up to 25% of wages paid to a qualified employee while on an eligible FMLA.	Retrospective Prospective
Federal Empowerment zone credit	Federal Income Tax Credit	Credit for wages paid to employees who work and reside within a designated federal empowerment zone	Credit is 20% of wages paid capped at $3,000/employee annually	Retrospective Prospective
Federal WOTC	Federal Income Tax Credit	Credit for wages paid to employees hired from underserved communities	40% of qualified wages paid to each employee up to $2,400 per employee (or more in some cases)	Prospective

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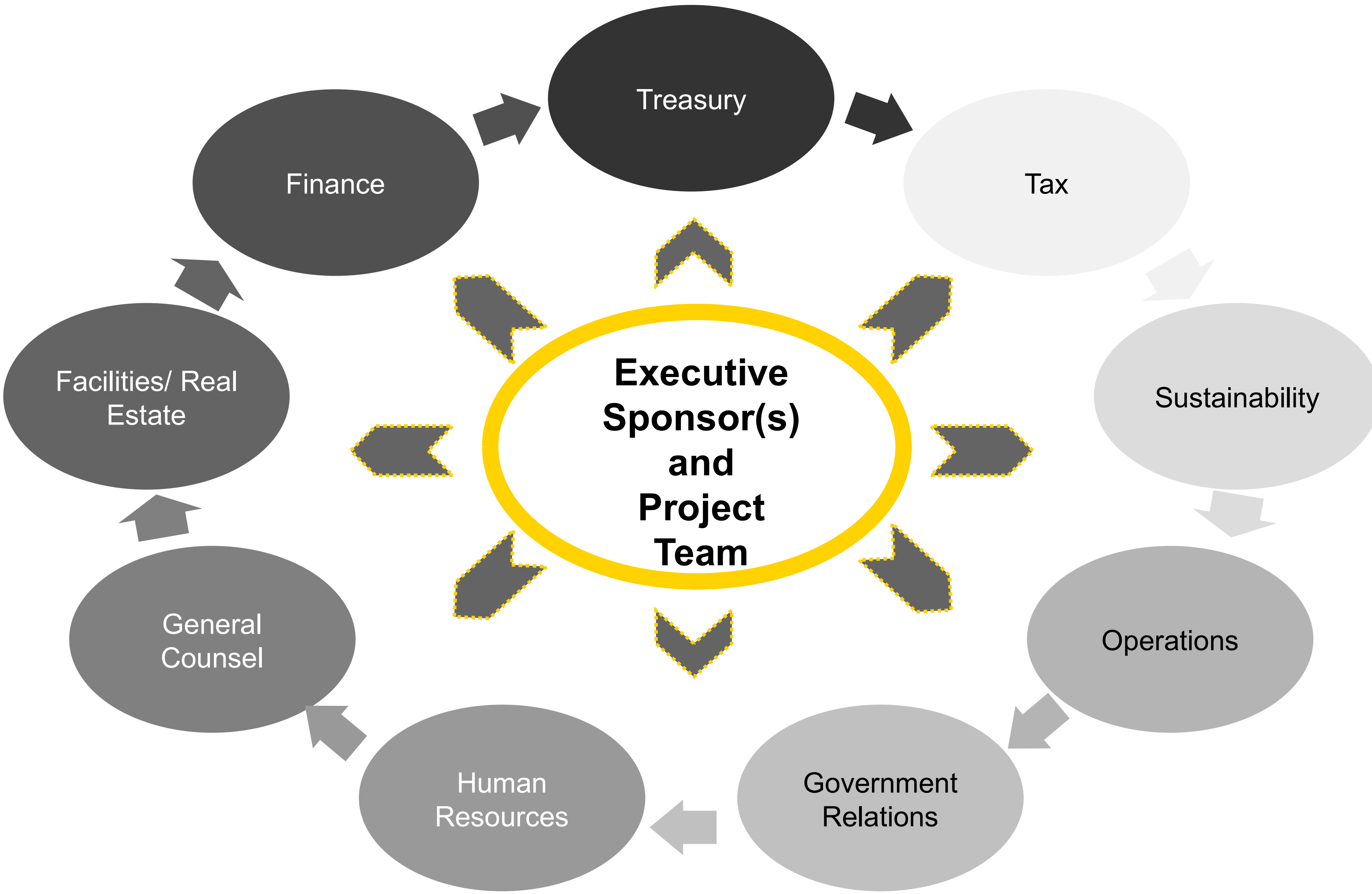
Potential State Refund Opportunities

Jurisdiction	Benefit Type	Description	Benefit	Retrospective vs. Prospective
Georgia Jobs Tax Credit	Premium Tax Credit (non-refundable)	Premium tax credit for historic and prospective job creation in Georgia. Eligible employers must create at least 15 net new jobs in order to qualify for the credit	Credit of between $6,250 and $8,750 per job over 5 years	Retrospective and Prospective
South Carolina Jobs Tax Credit	Premium Tax Credit (non-refundable)	Credit for eligible companies that create at least 10 net new jobs in one year	Credit is equal to $7,500 per job over 5 years.	Retrospective and Prospective
New York Youth Works Jobs Tax Credit	Income tax credit (refundable)	Credit for employing qualified youths between the ages of 16 – 24	Credit is up to $5,000 per qualifying individual for the tax year	Retrospective and Prospective
New York Investment tax credit & SUT exemption for R&D equipment	Income tax credit (refundable)	Credit/exemption for equipment used in R&D	ITC is 9% of qualified property	Retrospective and Prospective

Potential State Prospective Opportunities

Jurisdiction	Opportunity	Benefit Type	Description	Benefit	Retrospective vs. Prospective
Kansas Promoting Employment Across Kansas	Discretionary	Payroll Withholding Tax Refund (refundable)	Company must commit to creating 10 new jobs that pay at least county average and provide benefits within a two-year period	Up to 95% of the payroll withholding tax of PEAK-eligible employees/jobs for a period up to 10 years	Prospective
Missouri Missouri Works Business Incentives	Discretionary	Payroll Withholding Tax Refund (refundable)	Company must create at least 2 net new jobs in an Enhanced Enterprise Zone or 5 jobs outside of an EEZ	Tiered percentages of payroll withholding tax (80% - 50%) refunded to qualifying taxpayers for 6 years	Prospective
New York Excelsior Jobs Program	Discretionary	Premium Tax Credit (Refundable)	Refundable credits for approved projects involving job creation and investment. Must be pre-approved	Credits equal to 6.85% of new payroll, 2% of investment, R&D credits and Real Property Tax Credits	Prospective
Rhode Island Job Training Credit	As of right pending compiance	Income Tax / Premium Tax Credit (Non-refundable)	Credit for training costs incurred for RI employees. Must be pre-approved	50% of actual training expense, up to $5,000 per employee, over three years	Prospective
Florida (IWT)/ (QRT)	As of right pending compliance	Cash grants	Provides for a percentage of dollars spent on qualified training back as a cash grant. IWT for existing workers. QRT is for net new employees.	Requires pre-approval. IWT is up to $200,000 per entity. QRT is up to $500,000 per entity	Prospective

Best practices: Identify a core team of stakeholders



IRC 6418 - Transferability

- **Section 6418 general rule:** an irrevocable election to transfer all or any portion of the following credits to an unrelated taxpayer in exchange for cash:

30C (certain portions)	45 (PTC)	45Q (CCUS)
45U (nuclear)	45V (hydrogen)	48 (ITC)
45X (advanced manufacturing)	45Y (technology-neutral PTC)	48E (technology-neutral ITC)
45Z (clean fuel production)	48C (advanced energy)	

- One-time only transfer
- Election must be made prior to filing the return in the year the credit is eligible
- Not included in the income of the transferor or deductible by the transferee
- “Applicable entities” that can elect direct pay cannot transfer the credits
- Penalty for “excessive payments”

What are we seeing?

- General transaction framework
  - Seller guarantees delivery of “good” tax credits and agrees to make the buyer whole if there is an issue with the delivered tax credits. Insurance is sometimes taken out if the guarantor is less creditworthy.
  - Payment schedules vary, but tying them to remaining quarterly estimated payment dates is becoming the norm.
  - Rules don’t allow for payment in a tax year before the tax credit is generated.
  - Pricing ranges from $0.92 to $0.96, with timing and size being the biggest factors.
- Why do taxpayers sell?
  - Tax inefficiencies (federal tax, BEAT, Pillar 2, etc.) make the tax credit worth less than $1
  - More flexibility relative to tax equity
  - Payment timing better than direct pay option on 45X credits
- Why do taxpayers buy?
  - Reduce cash taxes
  - Provides safe yield relative to equivalent corporate paper — largely a treasury function

Process

Bilateral negotiation
- *Higher risk*
- *Less efficient*

Auction process
- Lower risk
- More efficient

- Executing tax credit transactions via an auction process de-risks transaction and provides benefits for both buyers and sellers
  - Market-based pricing and terms
  - Ready access to a variety of tax credit types, amounts and timing (supply and demand)
  - Structured process/standardized documentation for maximum efficiency

State tax credits

- U.S. States provide credits for a diverse series of fiscally, economically or socially positive activities, such as job creation, desirable investment (e.g., manufacturing machinery and equipment, renewable energy technologies, research and development), employee training, etc.

- The types of state tax credits which may be transferred can generally be divided into three market segments.
  - Certificatable Credits
  - Bifurcatable Credits
  - Allocable Credits

Types of monetizable credits: Certificated credits

- **Certificated credits:** *Tax credits that can be converted to certificates which can be bought and sold much like bearer bonds with the party attaching the certificates to its tax return in lieu of payment*
  - Examples of Certificated Credits:
    - Low Income Housing Tax Credits – Massachusetts
    - Historic Rehabilitation Tax Credits – Arkansas, Connecticut, Delaware, Iowa, Kansas, Kentucky, Louisiana, Massachusetts, Minnesota, Missouri, Oklahoma, and West Virginia
    - Film – Alaska, Arizona, Connecticut, California, Florida, Georgia, Illinois, Iowa, Louisiana, Massachusetts, Missouri, New Jersey, Pennsylvania, Puerto Rico, Rhode Island, and West Virginia

Types of monetizable credits: Bifurcatable Credits

- **Bifurcatable :** *Tax credits that can be specially allocated amongst partners*
  - Ownership Example:
    - Partner A holds a 1% ownership interest while being allocated a 100% of the state tax credit while receiving 1% (or less) of depreciation, cash flow, federal credits, and residual proceeds

  - Examples of Bifurcatable Credits:
    - LIHTC– Arkansas, California, Connecticut, Georgia, Illinois, and Puerto Rico
    - HRTC – Georgia, Maine, Mississippi, Ohio, South Carolina, and Virginia

Investment considerations

- Tax liability
  - Most deals that go wrong, go wrong because the credit purchaser didn't have the taxable income to use the credits
  - Not just income tax but BEAT, Pillar 2, etc
- What is the alternative use of cash?
- Is the juice worth the squeeze?
  - Benefit versus transaction costs
- Counterparty risk
- Delivery risk/Opportunity cost
- Financial statement considerations

Questions