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Tax Intelligence - Clawback or Recapture Provisions Related to Incentives

Situation

Clawback or recapture provisions are tools state and local governments use to ensure companies deliver on their negotiated promises for economic incentives. These provisions are usually clauses that simply say a company must uphold its end of the deal when claiming statutory or discretionary incentives. If the company fails to achieve certain performance benchmarks, the provisions can require that the tax payer repay tax incentives earned or received.

In the past, jurisdictions were sometimes reluctant to enact clawback or recapture provisions since they may be viewed as unfriendly to business. Clawbacks or recaptures should not be viewed as a threat to businesses, but rather as a set of clear expectations for everyone involved. However, newly enforced clawback and recapture provisions by states now have companies paying specific attention should their facility be downsized or closed, if jobs are transferred or cut, and/or if machinery or other property is moved.

Solution

Taxpayers should be aware of the clawback provisions associated with the tax incentive benefits they are receiving, and a specific strategy should be developed and communicated quickly if a taxpayer forecasts they will not meet the requirements. It is possible that the taxpayer can negotiate with the jurisdiction on opportunities to reduce or erase the impact of the clawback provisions. The following credits currently have clawback or recapture provisions in place:

- Maryland Job Creation Tax Credit – If the taxpayer decreases the number of qualified positions during the three years after the credit begins, a percentage of the credit is recaptured. If the taxpayer's positions fall below the threshold (usually 60%), the credits used must be repaid in full. If the number of jobs for which the credit is taken falls more than 5% but remains above the threshold, then the amount of the tax credit to be repaid is in proportion to the decline in certified employees.
- Michigan Tax Credit Claimed Under the Former Single Business Tax or the Michigan Business Tax – If a taxpayer fails to comply with credit conditions, then the taxpayer may have a percentage of the credit or the entire credit amount added back to the taxpayer's corporate income tax liability.
- North Carolina Job Development Investment Grant - If a taxpayer fails to meet the terms of the agreement, the grant will be reduced proportionately (at minimum), and may be terminated. If the taxpayer fails to meet employment or other goals for two consecutive years, the agreement will be terminated. If the taxpayer attempts to manipulate employee withholdings to increase the benefit, the benefit will be recaptured or terminated.
- South Carolina Economic Impact Zone Investment Tax Credit – If the taxpayer removes equipment from the zone before the end of the applicant period, the taxpayer must pay an increased tax during that year, recapturing any unearned portion of the credit.

Value

The concept of clawbacks or recaptures may seem straightforward, but the provisions vary significantly by state and by programs within the state. If you would like to learn more on clawback or recapture provisions, please contact Pete Krieshok at 314-214-7325 or by e-mail at pkrieshok@talx.com.