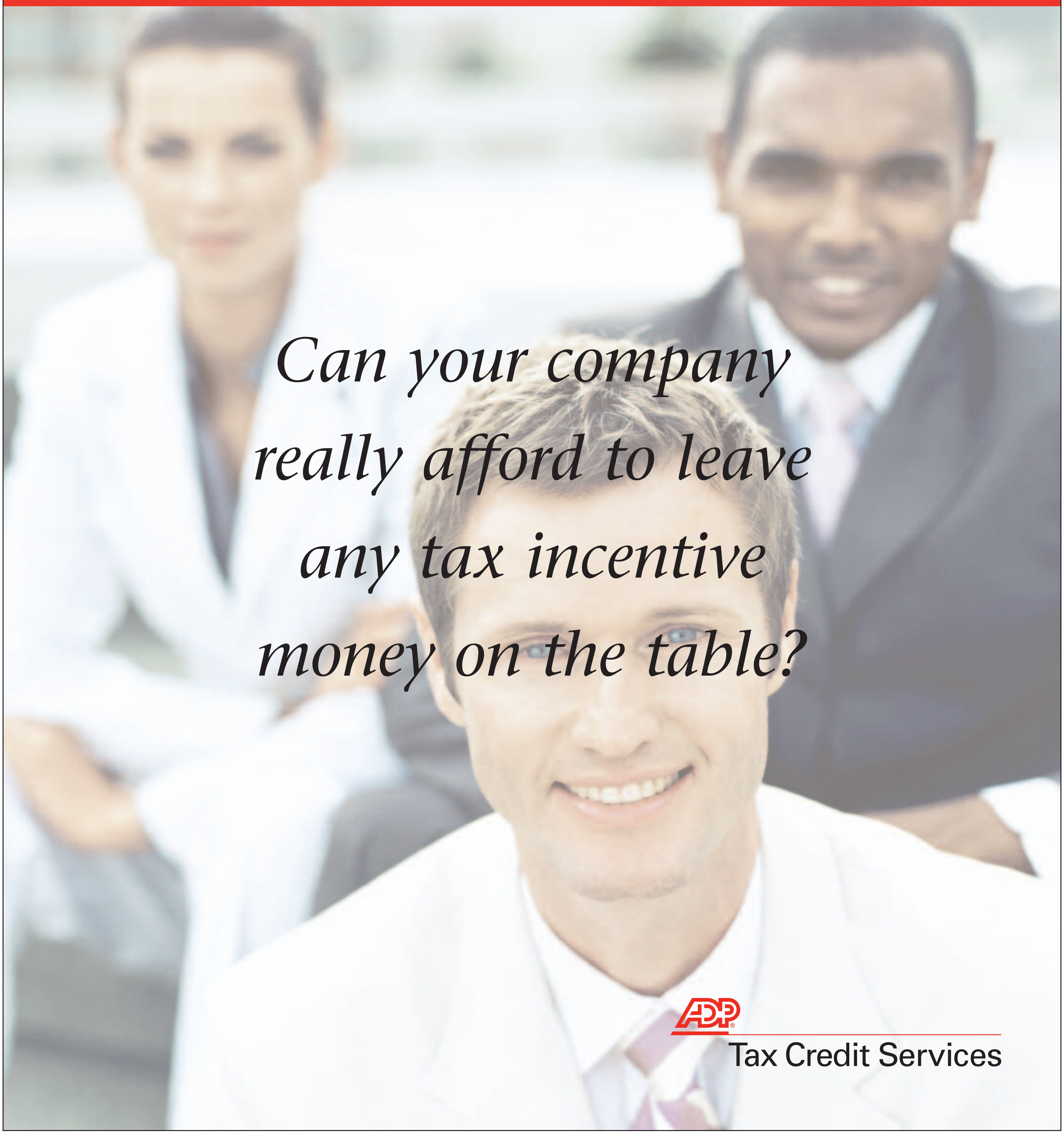
Matching Companies, Communities, and Incentives



Can your company really afford to leave any tax incentive money on the table?

Tax Credit Services

TABLE OF CONTENTS

I. INTRODUCTION

There is an old saying, "A penny saved is a penny earned." When applying that fabled economic principle to the constantly evolving world of tax credits and incentives, there is a corollary that each company must answer for itself: *How much incentive money must be on the table to make administering tax credits and incentives a worthwhile blip on the radar screen?*

This white paper explores why many companies typically do not view tax and incentive administration as a worthwhile opportunity. It also provides reasons why companies should take a fresh look at the profit potential of an efficient administrative solution. The fact is no company should walk away from any tax credit and incentive money that can be "mined" cost-effectively. While some people will never stop and bend over to pick up a coin on the sidewalk, a rational business person should never leave significant amounts of free money unclaimed.

Two key questions emerge:
1) How much in tax credits and economic incentives are available? and 2) Why do so many companies seem to not have a strategy to administer and earn those credits and incentives?

- ***How much tax credit and incentive money is currently available?*** There are more than 2,000 federal, state, and local tax credits that annually have a total value in the billions of dollars. However, the critical statistic here is what is *not* happening regarding these economic opportunities – that is, a significant amount of all tax credits and economic incentives in the United States are either unclaimed or uncollected.

- ***Why aren't more companies pursuing their credit and incentive opportunities in a more comprehensive way?*** Identifying tax credits and economic incentives requires: 1) a commitment of people with specialized skills, 2) a database that must be constantly fed with fresh information, and 3) a coordinated effort to meet all of the requirements of each incentive.

Because many tax credit efforts result in a dead end with no payback, financial executives are, at the very least, reluctant to commit limited corporate resources to search for dollars that may or may not be there.

II. AN INTERNAL DILEMMA

Some corporate departments may be actively pursuing certain categories of incentives; however, other departments that could do the same have other priorities. The net result – company-wide – is actually one of *under-performance*.

There are two reasons for this. First, many opportunities go unrecognized because organizations simply fail to determine all of the incentives that are available. Second, even when an organization identifies an incentive, it requires a coordinated effort by several departments to collect all of the information to successfully apply for the incentive.

When even just one department (or individual) fails to perform their portion of the effort, the end result is to miss out on an opportunity. A classic example of this is when one group within an organization negotiates an incentive package, but no one else in the company is aware of the incentive, and it is never claimed.

Clearly, companies should designate an individual or team to take the lead to manage the tax credit and incentive function. In addition, when there is appropriate internal (or external) control to assure performance, then there is a greater likelihood that the effort will be performed – and performed effectively.

Since this results in a financial benefit, it generally falls within the purview of the finance organization. This leads to the obvious question: who in the finance and accounting hierarchy of a company is obligated to identify, review, and maximize tax credit and economic incentives? In addition, who is responsible for evaluating the performance of the company with regard to incentive compliance?

II. LIMITED CORPORATE RESOURCES TO IDENTIFY, PURSUE, AND CAPTURE INCENTIVES

Many companies have no formal structure in place to verify if all tax credits and economic incentives are being managed correctly, let alone anyone being assigned to champion the effort to address and administer incentives.

According to a KPMG LLP survey of senior corporate tax and real estate professionals, the responsibility for tax credits and incentives at best is "fragmented" within the companies surveyed.[1] While 55% of respondents said that incentives and tax credits play a significant role in decisions concerning corporate expansion among other things, 79% of the surveyed firms assigned the responsibility to multiple people within their organizations.

Unless a tax credit and economic incentive management system is in place and requires fiscal oversight, chances are internal as well as external financial resources will not proactively identify tax credit and incentive opportunities.

- *External auditors* have no obligation to deal with tax incentives because the attestation function that certified public accountants perform only involves items that rarely would include tax incentives.

- *Internal auditors* only review tax credit opportunities when they audit operations that involve incentives or tax operations for entities that are already claiming credits; typically there is no audit of incentives.

- *The internal accounting function* will help maximize incentives if they are "material" not just "significant" in total value.

Tax incentive management can easily be a source of frustration for a company. With fresh streams of revenue as the optimum goal for a corporation, why apply resources to ferret out incentives that may not be a cost-effective use of talent and other resources?

Continued on the next page.

1. "Economic Incentives, Tax Credits Go Unused," Laurie Brannen, *Business Finance*, January 2004.

II. LIMITED CORPORATE RESOURCES TO IDENTIFY, PURSUE, AND CAPTURE INCENTIVES (CONTINUED)

In the end, for many financial professionals, tax credits and incentives must clearly be material in size and scope to gain their attention. If the anticipated reward does not meet that threshold, there is little reason to commit internal resources to the chase.

One of the driving reasons why half of all credits and incentives administered internally by corporations are never realized is not because the money is not there. To the contrary, the real driving reasons include: unclear or decentralized responsibility for identifying, pursuing, and administering credits and incentives; failure by internal corporate staff assigned to administer these projects to fully understand the government's requirements; and/or the lack of an *incentive management process.*

Companies can overcome these obstacles by retaining one of the many excellent consulting firms that have the resources and experience to perform all of these functions. In most instances, this is the lower cost/risk option. Yet, in spite of the lack of significant success generated by internal corporate staffs in managing the tax incentives and credits process, many companies will still choose to build and keep that function in-house.

IV. FINDING A SUCCESSFUL MANAGEMENT SOLUTION

The pressure to consistently improve profitability is the primary force driving companies – public and private – to revisit opportunities that can improve bottom-line performance, including the value that can be derived from a tax and incentive management solution.

Once a company conceptually commits itself to adopt a tax credit and incentive management process, then comes the big question: *How?*

V. SHOULD A CORPORATION "CREATE" OR "BUY" A MANAGEMENT SOLUTION?

During the course of any given year, companies face strategic "make or buy" decisions… *"Should we process our own payroll or outsource to an ADP?" "Should we hire our own security guards or obtain those services from Brinks or Pinkerton?" "Should we hire our own cafeteria staff or pay a Marriott or an Aramark to run the facility on a soup-to-nuts basis?"*

To "build or buy" basically involves determining the best way for you to achieve a goal or objective. Because identifying and administering tax credits and incentives requires technical knowledge, access to proprietary databases, and specialized skill levels by those who are handling the administration, a company needs to consider several critical expense items before making a decision to manage credits and incentives with internal resources or through outsourcing.

- **Implementation Expense** – The cost of designing the process, gathering available data about incentives, creating checks and balances, and recruiting and training system users.

- **Ongoing Support Costs –** Updating the database, assuring compliance with the latest legislative updates, and recurrent training expenses as a result of employee turnover and other changes.

Once you have developed an accurate assessment of implementation and ongoing support costs for a tax credit and incentive management solution, then comes the selection of the strategy that will best work for your company. Do you "build" or "buy" the solution? Because your company has the data needed to calculate the incentives, you can never completely turn the effort over to an outside organization. However, by introducing outside expertise into the process, you can confidently avoid much of the administrative burden and associated expense.

VI. THE "CREATE IT" OPTION

Companies that prefer control over every aspect of the solution – from hardware and software purchases and upgrades to internal staffing – are more likely to create their own tax credit and incentive management process. In return, they also end up owning the "perception" of convenience and control.

With convenience and control of an internally staffed solution come relentless responsibilities, not the least of which involves constantly keeping the tax credit and incentive management database updated to reflect changes in incentive rules and regulations. Compliance with current regulations is a never-ending chore.

Every task at every stage of implementation and operation belongs to the in-house owner. In addition, the cost per employee to staff a comprehensive in-house management system is also considerable. The professional talent required ranges from attorneys and accountants to tax and financial experts.

VII. THE "OUTSOURCING" OPTION

Companies looking for a solution with maximum return but minimal overhead and low risk tend to outsource. The focus is on purchasing a solution from a provider and realizing the benefits in return for a fee – preferably a contingency fee. The outsourcing option, in principle and practice, lets a business focus on tax credits and incentives without the burden of operating a fixed-cost, high-overhead operation that needs justification.

Through an outsourcing arrangement, the risk of solution ownership is not with the company using a service, but rather with the provider. It is the provider that builds the process, manages the database, and performs upgrades to maintain compliance, accounting for changes in laws and regulations as well as technology. A qualified service provider may also offer limited legal immunity from some risks.

If outsourcing is a viable option for your company, what about using *public accounting firms* to manage your tax credit and incentive management system?

VIII. THE SARBANES-OXLEY "SOX" FACTOR

One option that had been used by companies to realize tax credits and economic incentives – engaging public accounting firms on a contingent fee basis – has virtually evaporated with the implementation of a federal law in 2002 that was primarily designed to respond to corporate scandals. This law also had an unintentional result. It caused a strategic shift in the way publicly owned businesses can do business with CPA firms.

Perhaps no group has been more greatly impacted by SOX regulations than public accounting firms, which have found themselves under an unprecedented microscope of compliance. Due to the increasing demands on public accounting firms to comply with SOX rules, companies that choose to use these firms have often ended up paying high "time and material" costs with little to no incentive on the part of the accounting firm to maximize credits for their clients.

SOX rules have also limited the ability of public accounting firms to provide services on a contingency fee basis, which is often desirable in situations where the outcome of a search for credits and incentives is uncertain. Although public accounting firms have performed incentive work in the past and may still offer the service, a company – particularly publicly held corporations – must be extremely careful in hiring accounting firms to ensure all of the Sarbanes-Oxley requirements are met and the arrangement won't result in problems with the SEC.[2]

SOX compliance has given rise to service providers as a solid source for tax credit and incentive solutions. ADP[3] is one of the leading providers of tax credit and economic incentive services in the United States. The company's staff of more than 330 professionals – attorneys, certified public accountants, tax and financial experts, and economic developers – serves clients throughout the country. ADP has a proprietary database that includes more than 2,000 incentives, and a geographic information system that maps 1,800 individual incentive zones.

Because ADP's tax credit and economic incentive solutions are typically based on contingency fee pricing, clients position themselves to realize benefits without a significant commitment of people, hardware, software, and related resources. Clients can also reach out easily for answers when questions arise by contacting ADP's call center which operates 24x7x365.

2 Letter from SEC Chief Accountant to Chair of AICPA Professional Ethics Executive Committee, May 21, 2004.
3 ADP provides market-leading payroll, HR, benefit administration and other services to employers in the United States and globally.

IX. IS YOUR BUSINESS A GOOD CANDIDATE FOR TAX INCENTIVE OUTSOURCING?

Can I improve my business with a tax credit and economic incentive management service solution? If after reading this white paper you are still not sure how to answer this question, consider asking yourself these specific questions:

1) Am I sure about the number and types of credits and incentives that my business is eligible for?

2) Do I have a system in place to help me identify, track, and capture tax credits and incentives (federal, state, and local) that my business can qualify for?

3) Does a member of our management team have the responsibility for identifying and administering all credits and incentives for our company?

4) Has my business captured every opportunity to earn a tax credit or economic incentive?

5) Do I have someone with whom I can regularly consult concerning legislative and regulatory changes that can impact my company's tax credits and incentives?

6) Can the solution we now have in place definitely help us improve our profitability (regarding tax credits and economic incentives) better than an *outsourced* management solution?

If you responded "no" to just one of these questions, your business is likely a candidate for a tax credit and economic incentive management solution. If you responded in the negative more than once, the indications are that much greater.

X. CONCLUSION AND TAKE-HOME POINTS

Here is a recap of key take-home points from this white paper:

A) There are more than 2,000 tax credits and economic incentives, worth billions of dollars, currently available from federal, state, and local government agencies.

B) A high percentage of tax credits and economic incentives that are available to eligible companies go unclaimed or uncollected.

C) Many companies have chosen not to pursue tax incentives – and "leave money on the table" – because they do not want to commit resources to search for dollars that may not be there.

D) Many companies do not have a formal, centralized structure to identify, administer, and capture tax credits and incentives. If you assume that your current efforts are satisfactory, you are likely to ignore the potential for additional earnings.

E) The Sarbanes-Oxley Act of 2002 has placed significant restrictions on public accounting firms to accept contingent fees for pursuing unearthed tax credits for clients.

F) Companies that choose to pursue tax credits and incentives have a "create it" or "buy it" decision. Internal administration solutions carry high overhead and support costs.

G) Outsourcing to a service provider enables companies in pursuit of tax credits and incentives to secure what they are entitled to without the cost of "owning" an administrative solution.

H) An outsourced tax credit and economic incentive management solution enables companies to efficiently identify, track, and capture credits and incentives, usually on a contingent fee basis.

The amount of money needed to excite a company will vary, so companies will have different levels of enthusiasm with regard to incentives. What you need to remember is that there may be many incentives that you are not even aware of and which can be earned (albeit with some effort) if you only knew they were available. You can assume that your current efforts are satisfactory and ignore the potential for additional earnings or you can initiate a process to thoroughly explore all opportunities on an ongoing basis and achieve additional savings.

ADP Tax Credit Services
2205 Enterprise Drive, Suite C
Florence, SC 29501
800-868-1836
www.adp.com
www.taxcredits.adp.com

The ADP Logo is a registered trademark of ADP of North America, Inc.
Printed in USA © 2007 ADP, Inc.