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From Handshake to Ribbon Cutting: Lessons in Implementing Economic Development Incentives that Avoid Clawbacks

Article By:

Tax Practice Group McDermott Will Emery

Once an incentive agreement is in place, it is time for the company to get to work building and staffing the new or expanded facility. While the economics of a deal are typically still on track, the initial buildout/expansion can raise issues that may not have been anticipated during the negotiation process, such as construction delays, interim hiring or how to calculate average salaries of new employees. As these questions arise, it is critical to work collaboratively with the development agency to ensure maximum value to the recipient business.

An all-too-typical problem is construction delays. An incentive proposal or application will usually include a construction schedule. The planned construction benchmarks included in the proposal then become performance requirements in the incentive award agreement. After the agreement is signed, unforeseen delays arise such that the business cannot meet the specified timeline. Economic development agencies are typically understanding about delays and will be open to renegotiation as long as the project is still on track. Still, it is best to address these issues proactively before the target is missed. In many instances an agency can provide more relief if the issue is addressed before the deadline passes and a technical breach may have occurred.

One silver lining of addressing construction delays with a development agency is that the agency may help solve the problem causing the delay. Particularly if the delays are being driven by a governmental inspection or permitting process, the development agency will often have contacts with political leadership and management at the agency causing the delay. Using these contacts can be very effective in facilitating resolution of any regulatory or permitting hold-up.

Another issue that comes up is the question of counting interim job growth. Once a company commits to a location, it typically is enthused to begin hiring employees, even if the expanded or new facility is not yet ready. New job qualification criteria for purposes of the incentive, however, often include location and start date requirements that can unduly restrict qualification of new jobs. That is particularly the case where jobs transferred intrastate do not count toward performance. For example, new jobs initially housed in a temporary off-site office while construction is pending could face a risk of being considered transferred jobs (i.e., not “new” jobs) that do not qualify. Additionally, start dates can be an issue: A company may be eager to begin hiring after an initial letter of intent or government offer, but an incentive agreement often only counts jobs created after it is signed and in effect. Where the demands of the business world require quick execution, it is problematic to have a delay of months for an agreement to be signed and approved before a business can begin counting new jobs.

A corollary issue to consider is how to define what compensation types are available to use to meet negotiated average salary targets, particularly for mid-year hires. For example, consider that a salaried employee may not have a full year of wages in the first year of a project so payroll records won't support a business' compliance reporting. More frightening is deferred compensation or bonuses earned in year one but paid in a later year that might not count toward calculating average compensation. If these issues are not addressed during negotiation, it is important to deal with them prior to the filing deadline on any compliance reporting.

The negotiation dynamic resolving these types of technical issues is typically collaborative: With the ink still wet on the agreement, the economic development agency is enthused about the project and wants to see it succeed. The individuals involved in the original negotiation are probably still available and willing to help. However, with the agreement concluded and amidst heightened scrutiny of incentives, there can also be a sense that any accommodation made by the government must be something that they could defend if the negotiations were made public. Proactively resolving issues with the economic development agency is critical. If a problem is ignored, it may be uncovered by an agency tasked with enforcement (often a state department of revenue). This enforcement agency is often less understanding and accommodating than the economic development agency granting the incentive.

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