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Tax Incentives Help Firms Harness Cost Reduction Opportunities

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Companies should strategize identifying and understanding the appropriate tax incentives established under The Inflation Reduction Act, CHIPS Act, and the US Foreign-Trade Zones Program in order to promote their financial goals, say KPMG practitioners.

With the dynamic market and competitive business landscape, many trade and tax professionals are examining the federal regulatory framework to identify incentives, credits and customs duty management programs that may be leveraged to help companies compete more effectively in their US manufacturing and distribution operations. Depending on the type of operation the company has or is developing in the United States, companies may achieve cost savings measures through the use of the Inflation Reduction Act, CHIPS Act and / or Free Trade Zone program, as long as the eligibility and regulatory compliance requirements are met. Importantly, because these opportunities are not mutually exclusive, it may be valuable to evaluate the applicability and opportunity under each incentive program for current and future US operations.

The Inflation Reduction Act

On August 16, 2022, the Inflation Reduction Act was enacted to promote clean energy technology manufacturing and boost the production of these products in the United States. The Act includes new and expanded energy and climate-related tax incentives, including investment and production tax credits (such as incentives provided under §45, §45X, §45V, §45Z, §45Q, §45Y, §48, §48C, and §48E). As

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a result, taxpayers with a US footprint are taking these incentives into consideration as they plan the location of, and invest in, new projects.

For instance, the Inflation Reduction Act provides a new production tax credit under §45X for each eligible component that is produced in the US and sold to unrelated third parties as part of the taxpayer's business. Eligible components include solar, wind and electric vehicle (EV) parts, including solar polysilicon, wafers, cells, and modules, nacelles, towers, and offshore foundations, wind blades, battery cells, battery modules, and certain critical minerals. Many clients who have previously built manufacturing plants internationally are planning to bring these facilities and operations to the US to take advantage of this lucrative production tax credit.

By capitalizing on these incentives, businesses can significantly reduce their tax liabilities, freeing up capital for reinvestment into growth initiatives and innovation. These incentives often target renewable energy projects, energy efficiency improvements, and other environmentally friendly practices, aligning financial benefits with corporate social responsibility. As a result, companies not only achieve cost savings but also position themselves as leaders in the transition to a greener economy, thus attracting environmentally conscious investors and customers.

CHIPS Act

The Creating Helpful Incentives to Produce Semiconductors and Science (CHIPS) Act was enacted on August 9, 2022, to promote domestic semiconductor manufacturing. The CHIPS Act includes a 25% advanced investment tax credit (ITC) for certain investments in semiconductor manufacturing in the US that are placed in service after 2022.The CHIPS Act also includes opportunities to apply for and receive government grants for semiconductor manufacturing investments in the US.

These incentives are designed to stimulate domestic production of semiconductors, addressing supply chain vulnerabilities and reducing dependency on foreign manufacturers. By incorporating these tax incentives into the financial plan, companies can lower their operational costs, enabling them to allocate more resources towards research and development, expanding manufacturing capabilities, and enhancing technological advancements. This not only helps firms achieve immediate financial benefits but also positions them for long-term growth and competitiveness in a critical sector.

As taxpayers navigate, generate, and monetize these new or expanded credits, it is important for organizations to identify, understand, and prioritize the appropriate incentives given financial and strategic goals. Such an undertaking is oftentimes consuming and complex but can result in significant benefits.

FTZ Program

The US Foreign-Trade Zones (FTZ) program is a widely used program today that provides several benefits to companies importing materials into the US, such as deferral and possible elimination of certain customs duties and fees. Although the programs mentioned above may provide added incentives to domestically source the materials used to construct a facility, taxpayers are generally not required to do so. Based on supply chain and market needs, companies often end up having a mix of domestically source and imported materials. Therefore, many companies exploring the above Inflation Reduction Act incentives are also navigating establishing a US footprint for importing production equipment used within their manufacturing facilities as well as the subsequent importation of raw materials that may be used in the production of their finished goods. There are several factors related to establishing an importer of record and trade compliance responsibilities that a company must consider as part of establishing US manufacturing operations. Today's current trade landscape has become increasingly complex with the implementation of punitive tariffs, increased enforcement of forced labor for imports from certain regions, and overall supply chain complexity related to moving goods across borders. Companies should also consider strategic trade opportunities that may help them mitigate import costs such as tariffs and fees. There are many programs that are available to importers that can help importers accomplish this, however they take careful review, consideration, and execution to ensure successful implementation.

The FTZ program was established in 1934 to encourage US economic activity, promote US labor, and increase capital investment within the United States. The FTZ program is widely used today by importers in different industries. According to the 2022 Annual Report of the Foreign-Trade Zones Board to the Congress of the US, there were 1,200 active FTZ operations and over $1,011 billion of merchandise received into Zones. Some of the top foreign-status products that were received into production US FTZs during 2022 include oil/petroleum, vehicle and vehicle parts and consumer electronics, machinery/equipment and iron/steel.

The FTZ program provides importers with several benefits to help offset specific costs related to setting up US production operations. FTZs are geographically in the US but are considered outside of US Customs and Border Protection (CBP) territory, and thus foreign merchandise may be admitted into an FTZ duty free and undergo various activities such as inspection, manufacturing, testing, and packing while in the facility for an unlimited amount of time. When merchandise is ready to be shipped to domestic locations, duties and fees are paid to CBP upon withdrawal from the facility. Further, if the merchandise is exported outside of the US, duties and fees can be eliminated from using bonded procedures. By deferring duties and fees for goods that are eventually imported into the United States, companies can benefit from cash flow savings. The concept of "weekly entry" also allows companies to file one customs entry for goods leaving their facility and entering US commerce per week, which reduces merchandise processing and brokerage fees that non-FTZ importers pay sometimes multiple times per day for each importation.

Companies establishing new manufacturing facilities within the US, may also consider whether the production equipment clause of the FTZ Act may be beneficial for them. This allows Zone operators to admit production equipment that is intended for use in FTZ activity under FTZ procedures, and duty payment may be deferred until the equipment goes into use as part of production equipment as part of FTZ activity. At that time, the equipment is entered for consumption and duties are paid. This may provide companies an increase in cash flow while setting up US operations over several years, and potentially even a benefit from inverted tariff on the completed equipment. The inverted tariff benefit also allows FTZ operators with production authority to enter and pay duty on the condition of the finished products manufactured in the Zone if it has a lower duty rate than the rates on the foreign raw materials. It is important to note that there are certain restrictions around imported materials that are subject to trade remedies (such as antidumping/countervailing, §301, §232) that require that the merchandise be admitted under privileged foreign status (which locks in the applicable duty rates at time of zone admission) and are not eligible for the inverted tariff benefit.

Companies that are interested in exploring whether an FTZ is right for their company, should work with an adviser to conduct a return on investment to understand the financial benefits, followed by an operational feasibility study to explore transitioning their current or future operations under the FTZ environment.

If the financial and operational assessments are favorable, a company must seek approval for FTZ designation from the US Foreign-Trade Zones Board under the FTZ Board and Grantee in which their facility is located. Following FTZ designation, an importer must work with their local CBP office to seek activation of the facility to operate under FTZ procedures. The activation process includes two major steps (1) working to meet CBP's activation requirements under CBP regulations, and (2) implementation of an FTZ Inventory Control and Recordkeeping System (ICRS), which allows companies to track FTZ inventory under the customs-approved methods for FTZs and facilitate customs filings and recordkeeping. The FTZ software is a critical piece of the project implementation and ongoing program management, as it facilitates inventory control, duty liability, and customs filings related to the admission and withdrawal of merchandise within the FTZ.Building and maintaining a strong FTZ program internally is dependent on solid operational procedures coupled with strong automation that allows for visibility and flexibility to handle and maintain complex trade and FTZ processes.

FTZ implementation timelines may vary based on each company's operations and complexity. Engaging a trade consultant to advise through the FTZ process is an essential part of FTZ project planning, to help avoid pitfalls that may be encountered throughout the implementation. In conclusion, these tax and trade incentives may be valuable tools to encourage and enable re encouraging and enabling companies to achieve tax and trade incentives while operating in the US Companies should review their long-term supply chain and strategic goals alongside these incentives to understand the full scope of benefits that may be realized from utilizing one or more of the programs described herein.