

MANUFACTURING

in Lehman's Terms

Incentives 101: Automation Tax Credit Overview

Tis the season....tax season. A time to dig a little deeper into our pockets and pay Uncle Sam. Fortunately for some, this year's tax hit will be alleviated a bit due to the inclusion of the automation tax credit. Put into place during the 2019 legislative session (following a one-year hiatus), this credit is meant to help companies automate their factory processes to alleviate the ongoing challenges resulting from the labor-constrained world our manufacturers are operating in today.



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So, what is the automation tax credit? This North Dakota tax credit incentivizes primary sector businesses to increase automation. It does so by giving approved applicants up to 20% of their automation equipment purchase price (or lease) back as a tax credit. The legislature set aside \$1 million per year for the next four years for the program. Approved applicants receive a prorated portion if demand exceeds the \$1 million set aside. Such is the case for this year's applicants. Let's break down the numbers:

With a tax credit of 20%, it takes \$5 million worth of automation equipment statewide to fully allocate the \$1 million set aside by the legislature. This year, we received applications totaling nearly \$21 million. Some of the application expenses didn't qualify for various reasons, so we ended up with just over \$14 million of equipment approved. If we prorate that, we find that instead of a 20% credit, approved applicants will receive a credit just shy of 7%. In the past, various amounts had been set aside, but typically the balance had been around \$2 million per year.

I had mentioned "qualified" equipment or application in our discussion above. What are some of the reasons for the disqualifications?

- **Not primary sector:** Company must be primary sector at the time they take ownership of the equipment.
- **Title not transferred during the appropriate tax year:** Ownership of the automation equipment must have been transferred to the company in 2019. If a robot was shipped from Japan and showed up on the dock in 2019, but had freight on board port of entry in

2018, this would not qualify. Please note the program DOES NOT go by the date the equipment is placed into service as is the case in some tax related situations.

- **Replacing current automation equipment:** Simply replacing an automated process with another automated process does not apply. To be considered, the equipment must automate an existing manual process or tangibly advance automation of a previously automated process. Simply being faster isn't enough to qualify.
- **Not submitting the application on time:** Applications MUST be submitted by Jan. 31 of the year following the purchase. Applications cannot be accepted if it is not postmarked by Jan. 31.
- **Installing automation equipment for a new process:** To qualify, the equipment must replace an existing manual or substantially more archaic automation process.

Whether your equipment qualified for the Automation Tax Credit or not, be sure to also look into the manufacturing, agriculture, or recycling equipment sales tax exemption.

If your equipment did not qualify for the Automation Tax Credit, you may still qualify for the New/Expanding Business Income Tax Exemption. This is an exemption on incremental income resulting from new or expanding business activity for up to 5 years. This is only available if you did not qualify for the credit.

All applications have been vetted by the North Dakota Department of Commerce and the Office of the Tax Commissioner, and all applicants have received a letter outlining qualified expenditures. So, what's next? With tax deadlines fast approaching, the final determination on the tax formula will be made. Letters outlining the actual credit amount specific to that application will then be sent to the approved applicants so they can file their taxes. Although everything is not finalized yet, it appears applicants will receive a credit for approximately 7% of the cost of the approved equipment. Please keep in mind, applicants will be required to file a report with the Office of State Tax Commissioner documenting the improved job quality or increased productivity within one year of claiming the tax credit.

I would encourage you to look into the automation tax credit, if you are on the fence regarding whether or not you should integrate additional automation into your operation as a result of a challenging labor situation or if the breakeven point is less than optimal. A link to the automation tax credit form can be found on the North Dakota Department of Commerce's website at <https://www.business.nd.gov/finance/TaxIncentives/>.

For additional information regarding this or other incentives applicable to your manufacturing operation, please feel free to reach out and I will point you in the right direction. Also, if you are considering an expansion or relocating to North Dakota, I would be happy to work with you to make that a reality!

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