Workshop on Tax Incentives and Base Protection
New York, 23-24 April 2015

Tax Incentives: Objectives, Challenges and Alternatives for Governments and Investors

CASE STUDY 1

Acme Medical Equipment Co., Inc.

1. Description of Company

Acme is a US Corporation with its principal place of business in New York. The company was formed in 1950 in Buffalo, NY. The headquarters are still in Buffalo, where the company owns and operates a significant manufacturing facility.

Acme manufactures a wide range of medical diagnostic imaging equipment. The company started with X-ray machines (which it still makes) and expanded its product lines through the years to include many newer forms of diagnostic equipment, such as CT and MRI machines.

Originally, Acme manufactured equipment and spare parts, but did not provide services to customers. Since the 1970s, the company has offered installation service and repairs. Beginning in 2000, Acme broadened its product offerings further. Today, in addition to selling and leasing equipment, Acme offers customers the option to have a machine (owned and serviced by Acme) installed on site; the customer pays a fee each time the machine is used.

2. Overseas Activity

Acme exported its equipment to customers outside the United States soon after the company began operation. Sales were made through third-party distributors. Since Acme provided no services to customers, the only activity of Acme outside the United States was to identify distributors and manage relationships with those distributors.

Acme manufactured all of its equipment in the United States until 1980, when it opened a factory in Japan. In 1990, Acme opened a factory in Spain. The three factories (US, Japan and Spain) generally manufactured the full range of products offered by Acme. Although each factory generally served customers in its region of the world, products could be exported from each factory to customers located anywhere.

As services became an important component of Acme's business, Acme established subsidiaries in several countries. Trained personnel would travel widely to talk with customers (and sell products directly to the largest customers.) Acme staff also provided installation and repair services, although some work was contracted out to local, unrelated companies.

All of Acme's intellectual property was owned by its parent company, resident in the United States. Most of the IP was developed in the US. All research was funded by the US parent, whether the R&D was performed by an Acme entity or a third-party company.

3. 2015 Expansion

In 2012, Acme recognized that it needed to invest:

- Plant and equipment for a new factory, or a substantial expansion of the existing facilities in the US, Japan and Spain.
- Capital for a software center, to build an in-house team that could develop new and improved software to be embedded in its equipment.
- A monitoring center, to provide 24/7 monitoring for equipment located anywhere in the world. Most Acme equipment is built with sensors that are connected to the internet, so that the equipment can be monitored for potential break-downs. In many cases, diagnostics and repairs can be made remotely, through the internet, without the need for a technician on site.

Acme initiated a global review of potential locations for each of these three investments. The company was willing to consider any country that could provide an attractive combination of resources.

Tax considerations are important in this global review, but not the only factor, of course. Acme needs to be sure the new facilities are located in countries with reasonable safety, good transportation, a skilled and available workforce, reasonable costs for facilities and labor, and other business factors.

Questions:

1. Should your country seek to attract Acme's investments through a tax incentive?

   i. What are the arguments for and against?
   ii. Are the arguments different for the three different proposed new investments (a new factory; a software center; a monitoring center)?

2. How do you weigh tax incentives against other, non-tax incentives (such as providing infrastructure, training grants, or other benefits)?

3. If you offer tax incentives, should the incentives be determined by a fixed list of benefits your country offers, or should there be a negotiation? If there is a negotiation, how is that negotiation structured?

4. For how many years should incentives be offered? Why? What are the considerations?

   i. What requirements would you impose on Acme in order to secure the tax incentives?
   ii. What penalty would you impose if Acme fails to meet its commitment?

5. Would your approach to providing tax incentives to Acme change if you knew that Acme was involved in similar negotiations with other countries?