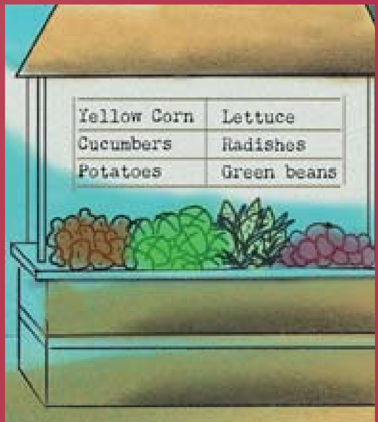
Tax Incentives + Businesses = JOBS

A Marketing Primer on How to Entice Businesses to Renewal Communities, Empowerment Zones, & Enterprise Communities



U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

The strength of our economy lies in the unmatched enterprise, creativity, and hard work of the American people. That is why President George W. Bush believes that the Federal Government should create an environment that encourages and rewards these qualities. HUD is helping create that environment across the nation, but we are especially focused on the communities that have fallen behind. In addition, we are paying special attention to America's small businesses—which consistently create more new jobs than any other sector of our economy.

In his first year in office, Congress passed and President Bush signed the Renewal Communities program into law. HUD moved quickly to support this encouraging program: in January 2002 we made 40 communities eligible for its special benefits, and also created Empowerment Zones in eight additional communities. In that one month alone, we brought more potential for economic growth in distressed communities than the nation had seen in the previous ten years.

In the past, Empowerment Zone programs offered some tax incentives, but experience showed that they were not widely used. In many cases, businesses were completely unaware of these tax incentives, while others did not understand the impact they could have on their "bottom line." To make the most of economic renewal programs and spur economic growth, it is critical for chambers of commerce, local elected officials, and especially the business community to understand all of the available incentives.

That is why we created this tax incentives marketing tool. And, the muscle behind this tool is the $22 billion in available tax relief that can create jobs, grow businesses, clean brownfields, and build homes. It is a guide created expressly for the men and women who want to use their local Community Renewal Initiative to bring success to areas that once had little reason for hope.

Our new marketing guide is filled with examples of successful strategies that will help you communicate the value of tax incentives available through your local Community Renewal Initiative. Even more, with your designation as a Renewal Community or an Empowerment Zone, it may be the single most valuable tool you can have to help businesses clearly understand the benefits of expanding in or moving to your community.

We hope you will take advantage of this valuable marketing guide. Along with the lessons you have learned in your first year of operation, it can help you create a brighter future—for your potential business partners, and every family in your community.

Sincerely

Mel Martinez

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Introduction

High unemployment, crumbling infrastructure, minimal access to business capital, and loss of hope represent some of the most notable challenges to confront inner cities and distressed rural areas during the past few decades. HUD's initiatives for Renewal Communities (RCs), Empowerment Zones (EZs), and Enterprise Communities (ECs) offer a number of tax incentives to businesses and workers to help overcome these problems. The tax incentives reduce the Federal tax liability of businesses, increase the expensing limits of business assets, permit the issuance of tax-exempt bonds, and provide for exemptions from capital gains taxation for properties that are sold. For example, in the area of business tax liability, a business located in an EZ could receive up to $3,000, and a business in an RC, up to $1,500, for every existing employee and new hire living and working in the area. More details on the incentives are provided later in this publication.

Under the banner of "Partnering for Community Renewal," HUD's Community Renewal Initiative supports alliances among State and local governments, businesses, and community-based organizations as a means of expanding economic development in our Nation's most distressed communities. Currently, 30 urban areas are designated as EZs and 40 urban and rural areas are designated as RCs. (See the appendix for a complete listing of RCs, EZs, and ECs.)

The success of each designee depends on the ability of its local officials to educate companies about the advantages of doing business within the designated area. Officials in EZs have confronted several challenges while luring businesses and they have adopted strategies to overcome them. Local EZ officials need to understand which businesses are eligible for the tax incentives and what makes a business ineligible. The final decision regarding whether or not a business is eligible for certain tax incentives should be made only by the business's tax professionals or by the Internal Revenue Service (IRS). These challenges and their solutions are described in more detail later in this publication.

Please note that EZ requirements prohibit the carte blanche relocation of businesses from a location outside the Zone to one inside the Zone because this would violate the anti-pirating proscription set forth in both the Omnibus Budget Reconciliation Act of 1993 and the regulations at 24 CFR 598.215. Although this legislation does not apply to RCs or to relocation motivated by tax incentives, local leaders who promote the use of the RC and EZ tax incentives should be aware of the underlying public policy concern.

Because RCs have existed only since December 2001, these communities have limited experience—compared with EZs—in the use of tax incentives. Subsequent to HUD's review of the RCs' Tax Incentive Utilization Plans (TIUPs), challenges surfaced that RCs will face. These are discussed in part 1. Fortunately, some of the incentives available to EZs are also available to RCs and many EZ successes can be replicated in RCs.

The successful marketing of the tax incentives should be a committed team effort that includes three primary groups: State and local officials and EZ/RC administrators; community-based and business organizations; and Federal agencies such as HUD, the IRS, AmeriCorps, and others who have pledged their support to RC/EZ/EC-designated areas. HUD's Office of Community Renewal has produced this publication to help administrators, as well as State, local, and Federal officials, communicate to businesses the advantages of locating and expanding in the RCs and EZs. This publication is organized as follows:

Part 1: Challenges and Strategies for Marketing RC and EZ Tax Incentives

This part describes the challenges local officials have faced in helping businesses use the appropriate RC/EZ tax incentives and the strategies used in response to these challenges. Many of the challenges are based on the actual experiences of EZs in implementing the tax incentives and have been highlighted in reports commissioned by the Inspector General and HUD.

Part 2: Case Studies

This part highlights 11 case studies on successfully using RC and EZ business tax incentives including wage credits, tax-exempt bonds, and deductions.

Part 3: WorkPads and Fast Formulas

This section has been developed as a quick and easy first step to determine whether a business is eligible for one or more of the available tax incentives and the related tax savings. RC/EZ directors can use this section as a teaching and marketing tool as well as a tool for data gathering and tracking. Although these tools are very useful, IRS and business tax accountants need to make the final determination of eligibility.

Appendix: Current Renewal Communities, Empowerment Zones, and Enterprise Communities as Designated by HUD and USDA

This section lists by location the RCs, EZs, and Enterprise Communities that HUD and the U.S. Department of Agriculture have designated.

A major goal of the Community Renewal Office at HUD is to help local RCs/EZs to achieve full use of tax incentives by the business community and other interested parties. To realize this goal, promoters need a working knowledge of the $22 billion package of tax incentives. They also should have a strategy to inform all businesses within RCs/EZs about the incentives available.

Before starting your marketing efforts, you should review and be familiar with the material in the *Tax Incentive Guide for Businesses in the Renewal Communities, Empowerment Zones, and Enterprise Communities.* This guide and *Market Primer on How to Entice Businesses to Renewal Communities, Empowerment Zones, and Enterprise Communities* are available free from HUD's Community Connections at 1–800–998–9999. TTY users should call 1–800–483–2209.

The following pages provide updated summaries of excerpts from the HUD publication *Tax Incentive Guide for Businesses* as well as brief descriptions of how the tax incentives work.

Overview of Tax Incentives

The RC and EZ initiatives provide a variety of tax incentives: some that work well for labor intensive businesses; some that benefit businesses with capital needs; some for large companies; and others for small companies.

Tax incentives are only one part of this Federal effort to reinvigorate economically distressed communities. Contributions from other Federal programs, local and State governments, businesses, financial institutions, nonprofit organizations, and residents are integral parts of the EZ Strategic Plan and the RC Course of Action. The tax incentives are intended to be used to complement Federal grant, monetary, and in-kind contributions from partners as detailed in the Strategic Plan and Course of Action.

Tables 1 through 4 provide brief descriptions of tax incentives available to qualified businesses in EZs and RCs.

How Wage Credits Work

Wage credits reduce the amount of Federal income tax that a business has to pay. Once a business has determined its income, it subtracts its business and other allowable deductions to arrive at its *taxable income.* The amount of taxes owed is then calculated against the taxable income. A tax credit is a direct subtraction from the amount of taxes owed. So, if a business calculated that it owed $50,000 in taxes and had $20,000 in tax credits, it would owe only $30,000 in taxes. In some cases, wage credits can be carried forward or backward under the IRS's general business credit rules. If the business owed $50,000 in taxes and had tax credits equal to $53,000, it would owe $0 taxes this year and could carry the additional $3,000 in tax credits forward to upcoming years or, in some cases, carry it back to prior years to reduce taxes owed in those years.

Refer to Part 3: WorkPads and Fast Formulas for tools to determine, through a simple calculation, whether a business may be eligible for one or more of these wage credit incentives, and to help a business determine the potential financial benefits of using these incentives.

Table 1. Summary of Wage Credits

Wage Credit Incentives	Description	Availability
Empowerment Zone Employment Credit (EZ Wage Credit)	Credit against Federal taxes of up to $3,000 for businesses for each year of EZ designation for every existing employee and new hire who both lives and works within the EZ.	Available for all EZs from January 1, 2002, to December 31, 2009. Cannot count wages for both the WOTC or WtW credits and the EZ Wage Credit.
Renewal Community Employment Credit (RC Wage Credit)	Credit against Federal taxes of up to $1,500 for businesses for each year of RC designation for every existing employee and new hire who both lives and works within the RC.	Available from January 1, 2002, to December 31, 2009. Cannot count wages for both the WOTC or WtW credits and the RC Wage Credit.
Work Opportunity Tax Credit (WOTC)	Credit of up to $2,400 against Federal taxes to businesses for each new hire from groups that have high unemployment rates or other special employment needs, including youth ages 18 to 24 who live within an EZ, EC, or RC and summer hires ages 16 to 17 who live within an EZ, EC, or RC.	State employment services agency must certify employee is in targeted group. Business does not have to be located in an EZ or RC to qualify. Cannot be combined with the WtW Credit. Expires for individuals who begin work after December 31, 2003, although this credit may be extended.
Welfare to Work Credit (WtW Credit)	Two-year credit against Federal taxes for businesses that hire long-term family assistance recipients. Credits up to $3,500 for the first year and up to $5,000 for the second year for each new hire.	State employment services agency must certify employee is in targeted group. Business does not have to be in an EZ, EC, or RC to qualify. Cannot be combined with WOTC. Expires for individuals who begin work after December 31, 2003, although this credit may be extended.

How Deductions/Accelerated Depreciation Work

Expensing or accelerated depreciation increases the deductions a business can claim when calculating its taxable income. Generally a business has to account for its equipment and buildings for tax purposes by depreciating the cost over the economic life of the equipment or building. That means, for example, that if a business pays $30,000 for a printing machine that is expected to perform for 10 years, the business cannot subtract $30,000 from its income when it pays for the printing machinery, but can subtract only a prescribed percentage of the $30,000 each year for the next 10 years. However, an EZ/RC tax incentive that permits increased expensing would allow the business to subtract the full $30,000 from its income in the year purchased. Also, deduction of qualified commercial revitalization expenditures (available only in the RCs) will let the business increase the amount of the deduction for a new or rehabilitated building by reducing the time period over which the cost must be spread.



Table 2. Summary of Deductions/Accelerated Depreciation

Deductions/Accelerated Depreciation Incentives	Description	Availability
Increased Section 179 Expensing	Allows businesses to claim an increased Section 179 deduction if they qualify as an EZ Business or RC Business (up to $35,000 for property acquired after December 31, 2001). Can be claimed on certain depreciable property such as equipment and machinery.	Can be used only in EZs and RCs. Could not be used in EZ developable sites until after December 31, 2001. Business must meet the eligibility test. See the chart "What it takes to be an RC or EZ Business" in part 3.
Commercial Revitalization Deduction (available only in RCs)	Deduction of either one-half of qualified revitalization expenditures (QREs) in the first year a building is placed into service or all of QREs on ratable basis over 10 years if QREs have been allocated to revitalization of a commercial building located in an RC.	Available in RCs for buildings placed into service after December 31, 2001, and before January 1, 2010. State may allocate up to $12 million in deductions (not more than $10 million per project) for each year from 2002 to 2009 for each RC in the State.
Environmental Cleanup Cost Deduction (brownfields)	Businesses can elect to deduct qualified cleanup costs of hazardous substances in certain areas (brownfields) in the tax year the business pays or incurs the costs.	Property is not required to be located in an EZ, EC, or RC. Need certification from State environmental agency that at or on the site there has been a release (or a threat of release) of a hazardous substance or substances. Includes costs paid or incurred prior to January 1, 2004.

Refer to Part 3: WorkPads and Fast Formulas for tools to determine, through a simple calculation, whether a business may be eligible for one or more deductions or accelerated depreciation incentives and to help a business determine the potential financial benefits of using these incentives.

How Bond Financing Works

Tax-exempt bond financing is a tax incentive that increases a business's cash flow because it allows businesses to receive low-interest loans. For this incentive to work, a State or local government issues a bond and sells it to investors. The State or local government then uses the money it receives from investors to make a loan to the business. The investors will accept a lower interest rate on the bond from the State or local government because they do not have to pay income tax on the interest income. The lower interest rate is passed on to the business. The investor expects to receive the payments of interest and the principal of the loan from the business. The State or local government can pay back the investor only with funds received from the business. The interest rate savings may be up to 2 percent, which increases cash flows each year and may result in substantial interest savings over the term of the loan.

Table 3. Summary of Bond Financing

Bond Financing Incentives	Description	Availability
Enterprise Zone Facility Bonds (available only in EZs)	State and local governments can issue Enterprise Zone Facility Bonds (a type of tax-exempt bond) to make loans at lower interest rates to EZ businesses to finance Qualified Zone Property.	$130 million or $230 million is available in urban Round II EZs ($60 million in rural Round II EZs) over the designation period and for all EZs after December 31, 2001, including developable sites (no per-borrower limit and bonds are not subject to State volume cap) for EZ-based commercial, retail, or industrial property. Thirty-five percent of employees must be EZ residents. Businesses must meet eligibility criteria. See the chart "What it takes to be an RC or EZ Business" in part 3.
Qualified Zone Academy Bonds (QZABs)	State or local governments can issue bonds at zero percent interest cost to them to finance public school programs with private business partnerships. Private businesses must contribute money, equipment, or services equal to 10 percent of bond proceeds, which may qualify as a charitable contribution. The Federal Government pays interest in the form of tax credit to banks, insurance companies, and certain lending corporations that hold QZABs.	Federal allocation to States annually from 1998 through 2003. State education agency allocates credit to a QZA to finance materials, teacher training, building renovation, or equipment for programs that prepare students for jobs or college. Schools must be located within an EZ or 35 percent of students must be eligible for the free or reduced-cost lunch program. QZABs are available to be purchased by banks, insurance companies, and lending corporations.

Refer to Part 3: WorkPads and Fast Formulas for tools to determine, through a simple calculation, whether a business may be eligible for one or more of the bond financing incentives, and to help a business determine the potential financial benefits of using these incentives.

How Capital Gains Work

Capital gains tax incentives reduce or postpone the amount of income a business or investor has to pay on the appreciation of stock, partnership interests, or business property. If an investor buys stock in a company for $100 and sells it later for $200, the investor would normally have to pay tax on the $100 gain. Along the same lines, if a developer constructs a building for $1 million and sells it a few years later for $1.5 million, the developer would normally have to pay tax on the $500,000 gain from the sale. The tax code requires separate ways of calculating taxes on capital gains and losses. Capital gains calculations take into account capital losses when figuring the amount of income subject to tax. For this reason the tax year in which

Table 4. Summary of Capital Gains

Capital Gains	Description	Availability
Zero Percent Capital Gains Rate for RC Assets and District of Columbia Zone (DC Zone) Assets (Not available in EZs other than DC Zone)	The holder, for more than 5 years, of a DC Zone asset acquired between January 1, 1998, and December 31, 2003, or an RC asset acquired between January 1, 2002, and December 31, 2009, will not have to include in its gross income any qualified capital gain from the sale or exchange of the asset.	Exclusion applies only to an interest in or property of certain businesses operating in the District of Columbia or in an RC. The following qualify as DC Zone or RC assets: DC Zone or RC business stock, DC Zone or RC partnership interests, and DC Zone or RC business properties. Only gain attributable to the period from January 1, 1998, through December 31, 2008, for the DC incentive and from January 1, 2002, through December 31, 2014, for RCs may be excluded.
Nonrecognition of Gain on Sale of Empowerment Zone Assets (EZAs) (Not available in DC Zone or RCs)	Capitol gain on EZAs (stock, partnership interests, and business property) of an EZ Business held for more than 1 year is not recognized and is rolled over if a replacement EZA is acquired within 60 days.	Election by taxpayer for EZA acquired after December 21, 2000, and before January 1, 2010, for all EZs.
Partial Exclusion of Gain From Sale of EZ Stock (Available only in EZs)	Exclusion of 60 percent of the gain on sale of small business stock of a C Corporation that is an EZ Business located in an EZ if the stock is held for more than 5 years.	Stock must be acquired after December 21, 2000, and before January 1, 2010, at original issuance in exchange for cash. Sixty percent exclusion does not apply to gain after December 31, 2014. Business must be an Enterprise Zone Business in an EZ (other than the DC Zone.)

a capital gain has to be taken can be important. A further tax incentive allows a business to postpone capital gains by rolling them over into a newly purchased asset.

For each of these incentives, a business must meet the eligibility test. See the chart "What it takes to be an RC or EZ Business" in part 3.

Refer to Part 3: WorkPads and Fast Formulas for tools to determine, through a simple calculation, if a business qualifies for the tax incentives, and to help a business calculate the potential financial benefits of using these incentives.

How the Incentives May Impact Businesses

Local officials from RCs, EZs, and ECs need to know how a business or a group of businesses would use these incentives to effectively market and attract new businesses to their communities. Most EZ program staff are not tax professionals and do not give specific advice about the extent to which a business qualifies for a particular incentive.

EZ businesses' tax professionals and the IRS are the only entities that can make a determination of eligibility for tax incentives. The role of EZ program staff is to educate tax professionals about the incentives and to be accessible to businesses to handle issues. This is discussed in greater detail in Part 1: Challenges and Strategies for Marketing RC and EZ Tax Incentives.

The following is a hypothetical example of how a business benefits from locating in an EZ.

A Look at ABC Internet Service Company. ABC Internet service company approaches a real estate broker about purchasing an abandoned building in an industrial site in a city with colleges and technical programs that should help provide the workforce the company will need. In particular, it will need staffing around-the-clock and expects many of the employees to work part-time. ABC is a startup operation that has begun the process of raising venture capital to acquire the building and the equipment. ABC's real estate broker has attended a seminar sponsored by the local chamber of commerce on tax incentives in the EZ and puts the company in touch with EZ program staff. The staff and ABC work together, using the workpads and fast formulas in part 3 of this publication, to help determine whether the business qualifies for individual tax incentives and to help the business calculate potential financial benefits for fully using the available tax incentives.

ABC and Wage Credits. ABC is both labor- and capital-intensive. To run 24 hours per day/7 days per week, it will need many employees, including part-time workers. Many jobs will require specialized computer skills, yet the company will also need many general business employees for billing, custodial work, administrative services, accounting, and human resources. EZ program staff suggest the WOTC, which may be useful in ABC's first year, particularly since it is likely to hire many younger employees. EZ staff also suggest the company take advantage of the EZ Wage Credit for the employees retained beyond the first year of operations. Because ABC is a startup, it may not have a Federal tax liability during the first several years of operation, so the effect of the wage credits on its bottom line may be delayed by carrying the credits forward to future tax years. ABC's tax professional would perform income and expense projections to determine how wage credits could be of benefit in the future.

ABC and Bond Financing. ABC Internet Services could also use tax-exempt bond financing through Enterprise Zone Facility Bonds to purchase the building and equipment. Since it is a startup company, EZ program staff or a bond issuer and the company's financial adviser may need to identify sources to strengthen the credit so that the bonds can be sold. This might include a guarantee of the debt service payments or grant money that can serve as a source of equity or debt service reserve. The bond issuer may also be able to assist in finding investors that seek out this type of debt and can evaluate the associated risk. ABC must be a qualified EZ Business for at least 3 years after a startup period to maintain tax-exemption on the bonds. Therefore, EZ program staff will need to facilitate hiring, training, and retaining of employees to help ABC meet the eligibility requirement of having 35 percent of its workforce living within the

Zone. Bond financing will reduce the interest rate on the borrowing by about 2 percent compared to a conventional taxable loan. This reduced interest cost will save the company money each year.

ABC and Partial Exclusion of Capital Gains. EZ program staff should suggest the company increase equity by attracting investors through the incentive that provides a partial exclusion of gain from the sale of EZ stock. The company will have to qualify as an EZ Business, which again includes meeting the 35-percent-resident-employee test, and investors must hold stock in the company for more than 5 years. If an investor sees a great potential for gain on the purchase of stock in this Internet service company, the ability to exclude gain on the sale of the stock after 5 years may be very attractive and subsequently help raise the equity the company needs.

ABC and Section 179. ABC will have large equipment needs at the beginning and, given the nature of the computer industry, the equipment will need to be replaced and upgraded regularly. If the company qualifies as an EZ Business, the EZ program staff should suggest the increased Section 179 expensing incentive, which would permit the company to deduct an additional $35,000 of the cost of the equipment in the year purchased. If the company's equipment needs are more than $200,000 in a year, the incentive begins to phase out and be less valuable.

To summarize, the incentives that could benefit ABC include the following:

- WOTC for first-year wages.
- EZ Wage Credit for the entire EZ designation period.
- Tax-exempt bond financing for the purchase and renovation of a building located in the Zone.
- Increased Section 179 expensing for equipment purchases, including future replacement purchases.
- Partial exclusion of gain on the sale of stock in the company.

The local EZ program staff can assist ABC in the following ways:

- Identifying sources of strengthening the credit so that tax-exempt bonds can be sold.
- Guiding the business on which tax incentives may be available.
- Facilitating the hiring, training, and retaining of employees.
- Providing technical assistance on attracting investors.

ABC and State and Local Incentives. The local government may also provide some property tax relief or the State may give sales tax relief to help the company increase its cash flow in its early years. Local government may also have special programs for new businesses such as reductions in business license taxes, which will encourage the business to locate within the EZ.

Part 1: Challenges and Strategies for Marketing RC and EZ Tax Incentives

Renewal Community and Empowerment Zone officials have faced many challenges in helping businesses fully use appropriate tax incentives. A discussion of typical challenges and the strategies that can be used to address them follows. These challenges are grouped into six basic categories:

1. Qualifying for tax incentives.
2. Marketing tax incentives.
3. Optimizing the commercial revitalization deduction.
4. Assisting RCs/EZs through the New Markets Tax Credit.
5. Raising awareness of tax incentives.
6. Evaluating the effectiveness of tax incentives.

Qualifying for Tax Incentives

Challenge 1: Providing opportunities to businesses outside the RC/EZ

Boundaries of an RC/EZ are based on census tracts, and these boundaries may be difficult to explain. Some businesses will not be eligible for incentives because they are located outside the boundaries. However, they are important to the economic development of the RC/EZ.

By statute, an RC/EZ must meet very specific population, poverty rate, and size requirements and use census tract boundaries. The RC/EZ boundaries inevitably put some businesses in the RC/EZ but others located across the street or next door may not be within the RC/EZ. General marketing brochures will often include a broad description of boundaries because precise maps might be too complicated. Initial news stories may identify neighborhoods that do not coincide exactly with census tract lines.

This may contribute to confusion about which businesses, property, and residents are located in the RC/EZ and may also cause some resentment by businesses that are near but not within the RC/EZ. In some instances, a business on the outside may believe that the RC/EZ-based tax incentives provide unfair advantages to its competitors on the inside.

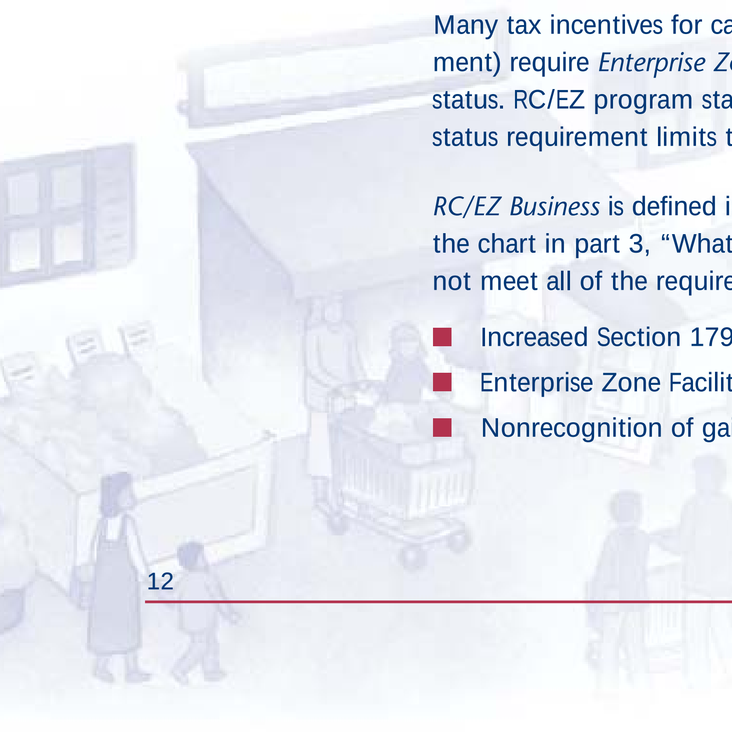
Recommended strategy. RC/EZ offices must be prepared to identify tax and other incentives available to businesses outside the RC/EZ.

At least two of the Federal tax incentives, Work Opportunity Tax Credit (WOTC) and Welfare to Work Credit (WtW Credit) are directly available to businesses outside an RC/EZ. In the case of WOTC, the credit applies when a business hires individuals who live in the RC/EZ. WOTC is the first credit that should be marketed to a business outside the RC/EZ.

RC/EZ program staff can also identify ways in which individuals and businesses on the outside may *indirectly* benefit from Federal tax incentives available to businesses within the RC/EZ. For example, a company that sells equipment may be able to expand its market inside the RC/EZ by knowing which RC/EZ Businesses are able to use increased Section 179 expensing. RC/EZ training programs that assist businesses with meeting the RC/EZ Business definition may also provide skilled workers for businesses outside of the RC/EZ. An investor who lives outside of the RC/EZ can still receive capital gains tax benefits from owning stock in a business located within the RC/EZ.

The RC/EZ program staff can look at the boundary challenge as an opportunity to identify and market other forms of assistance to businesses and residents on the outside. In many cases, the programs may be able to refer businesses that are outside the RC/EZ to well-established State low-interest loan programs, venture capital groups, or business incubators. For example, a State-level *enterprise zone* may overlap with the Federal RC/EZ but include areas outside its boundaries because the State initiative is not census tract dependent. The State enterprise zone may have sales, transfer, property, or income tax incentives available to these businesses.

Challenge 2: Understanding the RC/EZ business requirement



Many tax incentives for capital projects (such as construction, renovations, and equipment) require *Enterprise Zone Business* or *Renewal Community Business (RC/EZ Business)* status. RC/EZ program staff must be familiar with the criteria and recognize that this status requirement limits the number of businesses that may qualify.

RC/EZ Business is defined in the Internal Revenue Code in a very detailed way. Reference the chart in part 3, "What it takes to be an RC or EZ Business." A business that does not meet all of the requirements will not be eligible for the following tax incentives:

- Increased Section 179 expensing.
- Enterprise Zone Facility Bond financing.
- Nonrecognition of gain on sale of Empowerment Zone Assets (EZAs).

- Partial exclusion of gain from sale of EZ stock.
- Zero percent capital gains rate for RC assets and District of Columbia Zone (DC Zone) assets.

Refer to the discussion in the Introduction for a complete list of incentives and brief descriptions. The operational requirements for any corporation, partnership, or sole proprietorship to be an RC/EZ Business are as follows:

- Except with respect to a sole proprietorship, every trade or business of the entity is actively conducted in the RC or EZ.
- At least 50 percent of business income is derived from the active conduct of trade or business within the RC or EZ.
- A substantial portion of the use of the tangible property (owned or leased) of the business is within the RC or EZ.
- A substantial portion of the intangible property of the business is used in the active conduct of business within the RC or EZ.
- A substantial portion of services performed for the business by its employees is performed within the RC or EZ.
- At least 35 percent of the employees are residents of the RC or EZ.

Recommended strategy. This program should focus on the types of businesses that, because of the nature of their operations, are likely to qualify as an RC/EZ Business.

Types of businesses that have been able to meet the operational tests for designation as an RC/EZ Business include:

- Retail establishments, such as grocery stores, clothing stores, department stores, and hardware stores.
- Local service providers, such as bakeries, dry cleaners, small appliance repair, picture framing shops, local accountants or lawyers, physician or dental offices, for-profit daycare, auto sales or repair, print shops, pharmacies, and drugstores.
- Hotels and restaurants.
- Manufacturing and food processing plants.
- Small farming and nursery operations.
- Movie theaters.
- Office buildings that are owner-occupied or occupied by only a few tenants under long-term leases. Commercial real estate qualifies only if at least 50 percent of gross rental income is from an RC/EZ Business.
- Rental of tangible personal property (such as car rental or tool rental) if at least 50 percent of gross rental income is from an RC/EZ Business or resident of the RC/EZ.
- Farming operations if at the close of the preceding taxable year the aggregate basis of the assets used in the farming operation (owned or leased) does not exceed $500,000.

Some of the business types listed above will not qualify if they are part of national chain operations, businesses with multiple locations, or businesses with outside sales offices unless the facility and operations within the RC/EZ are owned by a legally separate entity. For example, a local movie house that is part of a national chain could qualify if it is a separate corporation or partnership from the national chain—even if the national corporation owns a majority of the stock in the local company.

The definition of RC/EZ Business looks at legally separate entities and ignores related companies. Because this is unusual among Federal tax incentives, an RC/EZ program should communicate this special feature when marketing to national companies.

Local business listings may be useful for identifying some of these businesses, but a local chamber of commerce, real estate agencies, or local bankers are also potential resources.

Challenge 3: Identifying eligible RC/EZ businesses

The statute eliminates certain businesses from eligibility as an RC/EZ Business even if all of their operations are within the RC/EZ and regardless of how many RC/EZ residents they hire. None of the tax incentives directed to purchases of equipment, capital gains incentives, or tax-exempt bond financing are available to these businesses. The following types of businesses are not eligible to be an RC/EZ Business:

- Residential rental property.
- Companies primarily in the business of developing or holding intangibles for sale or licensure (such as a movie production company, software development company, or drug development company).
- Companies in which 5 percent or more of the average of the aggregate unadjusted basis of the assets used in the business is attributable to collectibles (such as antiques, wine, or oriental rugs) unless the collectibles are held for sale to customers in the ordinary course of business.
- Banks, insurance companies, investment banking firms, and other similar businesses in which 5 percent or more of the average of the aggregate unadjusted basis of the property used in the business is "nonqualified financial property," including debt, stock, partnership interests, options, futures contracts, forward contracts, warrants, notional principal contracts, annuities, or other similar property other than short-term debt held for reasonable working capital needs.
- Massage parlors.
- Stores the principal business of which is the sale of alcoholic beverages for consumption off premises (such as a liquor store but probably not a grocery store where beer or wine are among the items sold).
- Country clubs.
- Private or commercial golf courses.

- Hot tub or suntan facilities.
- Race tracks or other facilities used for gambling.

However, the first four types of businesses are eligible for EZ and RC wage credits although they do not meet the definition of an RC/EZ Business for purposes of eligibility.

Recommended strategy. An RC/EZ office should market wage credits and develop a list of other incentives that can be offered to businesses not meeting the statutory definition of an eligible RC/EZ Business.

Generally, RC/EZ wage credits, WOTC, and the WtW Credit are available to businesses within the RC/EZ for employees who live within the RC/EZ, even if the business itself does not qualify as an RC/EZ Business. The RC/EZ wage credits are available for the first four categories (residential rental property through banks, etc.) mentioned above. Local or State incentives such as grants or low-cost loans may be available to help with equipment, construction, and renovation of buildings for those businesses that cannot qualify as an RC/EZ Business. If the business site is contaminated, the environmental cleanup deduction would also be available even though the business is not an RC/EZ Business. For RCs, the commercial revitalization deduction can be used by a business that does not qualify as a RC Business to construct or renovate commercial property within the RC.

Challenge 4: Meeting the 35-percent resident employee test

Some businesses may not qualify as an RC/EZ Business solely because they fail to meet the requirement that 35 percent of the employees must be residents of the RC/EZ.

The employment of residents within the RC/EZ is a key goal of the RC/EZ programs. Many of the tax incentives depend on businesses employing RC/EZ residents. An RC/EZ will be more successful in marketing capital incentives that require a business to be an RC/EZ Business if it can demonstrate in-place programs to help the business meet the 35-percent test.

The RC/EZ office may face a variety of challenges to providing this service. The population included in an RC/EZ-designated area varies and so does the number of residents of employment age. For example, WOTC is available for youth employed in the summer, but the summer youth must be at least 16 years old. An RC/EZ with a large population of youth under age 16 may find it difficult to provide seasonal businesses with enough youth qualified employees for the WOTC summer youth tax credit. Likewise, an aging population in the RC/EZ may limit the number and type of employees that it could provide to a business seeking to meet the 35-percent test.

Recommended strategy 1. The RC/EZ office should identify trainers to help businesses hire and retain RC/EZ-resident employees and thereby contribute to the business's efforts to qualify for the tax incentives.

WOTC and the WtW Credit are very important in helping RC/EZ residents obtain a job. Both credits are incentives to hire individuals who have traditionally found getting into the job market difficult. Youth and summer youth who live in an RC/EZ as well as veterans, ex-felons, vocational rehabilitation referrals, and recipients of supplemental security income (SSI), food stamps, and Temporary Assistance for Needy Families are among the targeted groups. These tax credits are available only if a business obtains certification from the State employment services agency (SESA) that the individual is a member of an eligible targeted group. This tax credit program or its variations have been available for many years and SESA personnel are knowledgeable about the process of qualifying for the credit and certification.

Some States have centralized the certification process, although others have delegated it to local offices. The RC/EZ office should begin by identifying the person or persons responsible for issuing SESA certifications. Businesses are more likely to do the paperwork necessary for these incentives if they have a contact person to ask questions about the specific documents they must submit and a timetable for submission. That SESA employee can also be a resource to RC/EZ staff when questions arise in the daily efforts of marketing these credits.

Recommended strategy 2. Develop a precertification process for the RC/EZ wage credits.

Unlike WOTC and the WtW Credit, RC/EZ wage credits do not require that the employer obtain certification from SESA. RC/EZ wage credits are not limited to new hires or to a specific age group. Because of this, an RC/EZ office could set up its own informal precertification process to help advertise the credit availability. That process could take place at a job fair or a community meeting, which are ideal forums to impart information and promote not only the RC/EZ wage credits but other tax incentives as well.

As part of the promotion efforts, RC/EZ staff could set up and host information tables for each of the incentives that include forms and other information pertaining to a particular tax incentive. The Internal Revenue Service (IRS) has not provided a certification form for a business to use for the RC/EZ wage credits to verify that an employee is a resident of the designated area (similar to the certificate required for WOTC). The RC/EZ office in conjunction with a tax professional could prepare a form for any resident who is seeking or already has a job with a business located in the RC/EZ. The business does not need to submit the form to SESA, so the RC/EZ office could incorporate a fact sheet on the wage credits along with certification that the individual lives in the RC/EZ.

Because the RC/EZ wage credits require that an individual both live and work in the RC/EZ, the number of businesses that can claim these credits is smaller than the number that can claim WOTC. However, the RC/EZ office can work with all job placement groups to identify employers that might be able to use the wage credits. Billboards and informational flyers can be placed in prominent RC/EZ locations to communicate the availability of the credit.

Challenge 5: Meeting precertification requirements for WOTC and WtW

The IRS mandates specific time requirements for obtaining information from a potential employee and submitting requests for certifications before businesses can claim WOTC or the WtW Credit. Some businesses view this as burdensome.

A business must obtain information from a potential employee during the hiring process before a job is offered. This information can be gathered on a form provided by the IRS and the U.S. Department of Labor or the potential employee can provide what is known as a precertification form. If a business does not obtain the information before hiring the employee, the credit may be denied. A business is also required to submit a request for certification from SESA within 21 days of the employee's start date.

To take the tax credit, both of these deadlines must be met. A business may think that the paperwork burden is greater than the value of the credit. Additionally, a business may be unaware of the time deadlines. If the credit is taken but time deadlines are not met, a business could face penalties that include having to pay back taxes and possibly related interest and fines.

Recommended strategy 1. RC/EZ offices should target workplaces that employ many entry-level workers for education about WOTC and wage credits.

The limited age range (youth 18 to 24) for WOTC suggests targeting specific businesses (such as restaurants, fast food establishments, hotels, summer camps, farming, and retail establishments) in an RC/EZ and nearby areas that have a strong demand for entry-level employees or that have high turnover rates. Job and training program placement offices and schools can assist an RC/EZ office with identifying that business population. A focus on businesses that are likely to hire RC/EZ residents in this age group but that may not be aware of WOTC will reinforce an effort to precertify youth coming out of these programs. An RC/EZ office can arrange meetings in which these businesses learn from SESA how the process works. SESA brochures can be mailed or handed out to these businesses.

Recommended strategy 2. Tap into existing intermediary companies for WOTC and the WtW Credit or consider establishing one in the RC/EZ.

Many entities can serve as intermediaries for companies that want to use WOTC and the WtW Credit. These entities typically deal with prospective employees over the phone to obtain information for the forms that must be completed before an individual can be offered a job. They will also work with the company to obtain its SESA certification. The intermediary's compensation is usually based on a percentage of the credit. Major corporations (such as national retail stores, hotels, and convenience stores) that use the wage credits extensively often use intermediaries.

RC/EZ offices may want to contact intermediaries about ways in which they can be included as part of the marketing of incentives. SESA may also be able to provide a list of intermediaries with which it has experience. The RC/EZ office may want to set up its own intermediary or work with a local community group or business to fulfill this function within the RC/EZ.

Recommended strategy 3. RC/EZ offices can link up with human resources groups.

Human resource personnel often belong to State and local organizations that can be tapped as a resource to gain additional skills and knowledge. RC/EZ offices can also contact these organizations as additional ways in which to market wage credit information to the businesses. By providing specific information on the boundaries of the RC/EZ and the characteristics of the workforce, RC/EZs can stimulate hiring from within the RC/EZ while also providing general information on tax credits. This can be accomplished through press releases to newspapers and organizations or through presentations at local and State organization meetings.

Challenge 6: Identifying tax incentives for family-run businesses

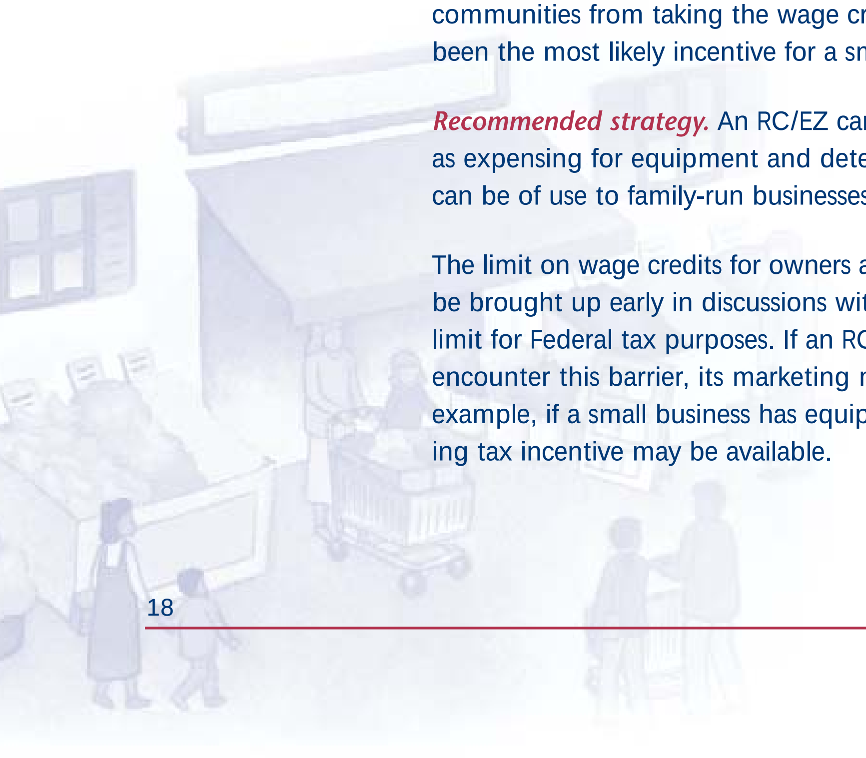
Many RC/EZ businesses may be family run. If the owner and employees are related, this will limit the use of the RC/EZ wage credits, WOTC, and the WtW Credit.

The tax code does not permit a business to take the RC/EZ wage credits, WOTC, or the WtW Credit for any person who owns 5 percent or more of the stock or partnership interests of the business even if that person is providing services to the business as an employee. For example, if a small RC/EZ firm is a partnership with four related partners with equal shares in the business, the firm would not be able to take an RC/EZ wage credit for any of the partners. Also, a small business owned by one person who hires her two sons will not be able to take an RC/EZ wage credit, WOTC, or the WtW Credit for either of them.

This requirement will prevent many small communities or small businesses in larger communities from taking the wage credits even though the wage credits may have been the most likely incentive for a small business to locate within an RC/EZ.

Recommended strategy. An RC/EZ can focus on ways to use capital incentives such as expensing for equipment and determine whether other State or local incentives can be of use to family-run businesses.

The limit on wage credits for owners and relatives is not common knowledge. It should be brought up early in discussions with small businesses. There are no waivers to this limit for Federal tax purposes. If an RC/EZ has several businesses with the potential to encounter this barrier, its marketing materials should identify some alternatives. For example, if a small business has equipment needs, the increased Section 179 expensing tax incentive may be available.



If a business is labor intensive with few equipment needs, the RC/EZ offices may be able to identify State and local incentives to help it. For example, training programs in the RC/EZ that update computer skills or sales techniques may be available free or at a reduced cost to these small businesses.

Challenge 7: Working with State and local governments on bond issuances

The EZ itself cannot issue tax-exempt bonds for capital projects. Only a State or local governmental unit can issue these bonds. If an EZ hopes to have projects financed with tax-exempt bonds, it must work with a State or local government to have the bonds issued. Tax-exempt bonds for capital projects cannot be issued for projects in an RC.

This financing technique is more specialized than a conventional bank loan and EZ staff may not be familiar with the steps in the process. EZ staff may be able to assist a business in the evaluation of the credit aspects of a loan but professionals with specialized knowledge of tax-exempt bonds must be involved.

Recommended strategy 1. Survey possible issuers of tax-exempt bonds and develop informational materials and meetings.

Tax-exempt bonds available to businesses located in the EZ must be issued by a State or local governmental unit such as the city, county, State, or economic or redevelopment authority. Once an issuer has been identified, that entity can provide the EZ office and potential business borrowers with an overview of tax-exempt financing, including a discussion of tax rules and the practical aspects of selling tax-exempt debt to investors. The issuer of the tax-exempt bonds will also have access to an attorney from a bond counsel firm and an investment banker who can help explain this incentive and can evaluate potential projects.

Recommended strategy 2. EZ office staff can meet with local bankers and investment bankers to assist with the tax-exempt bond financing and capital gains incentives.

Many tax-exempt bonds are sold through investment bankers with credit support, such as a letter of credit, from a bank. Financial institutions are an important source of economic development and often play a role in developing the EZ Strategic Plan. They can assist the EZ program with the identification and evaluation of projects that can be financed with tax-exempt bonds.

Investment bankers and advisers may also assist by identifying potential investors and offering stock in companies that qualify for the partial exclusion of gain. An EZ Business that meets the definition of a *small business* can obtain an infusion of equity while providing investors with a partial exclusion of potential gain on the sale of the investment. Generally, a small business is a C corporation with gross assets of up to $50 million. Businesses should consult their tax advisers for more specific requirements.

Challenge 8: Overcoming impediments to bond financing

Tax-exempt bond financing may be difficult to implement if businesses in the EZ need to borrow relatively small amounts or if the businesses do not have the necessary credit rating or cash flow to borrow the amount needed to make capital improvements.

Tax-exempt bond financing will involve larger upfront costs than a conventional taxable loan and, in some cases, these costs will outweigh any interest savings expected from tax-exempt financing. This is particularly true if the amount to be borrowed is a small amount or the loan term is short because the financed property has a short economic life.

Tax-exempt bonds are often sold in the public market where investors will be looking for a good credit. Even though a State or local government issues a bond, investors are told that repayment will come only from installments made by the recipient business. Investors may not be familiar with the credit of a small EZ Business or may have concerns about whether there will be sufficient revenues to pay back the debt over a period of years.

Recommended strategy. An EZ office can work with local and regional banks to establish pooled loan or letter of credit programs to reduce the costs of tax-exempt bond financing.

The costs of tax-exempt bond financing can be reduced on a per-borrower basis when several small loans are pooled. The tax-exempt bond rules permit a State or local government to issue bonds to make a loan to a bank that agrees to reloan the money to EZ Businesses. A community bank is in a better position to evaluate the credit of an EZ Business than the purchaser of a tax-exempt bond. The bank can loan the money to the EZ Businesses at a lower cost because its source of capital comes from tax-exempt bond proceeds. Tax-exempt bond investors look to the credit of the bank for the repayment of the bonds. The bank, in turn, expects to repay the bonds with loan repayments it receives from the EZ Businesses.

If five businesses want to borrow less than $1 million each, some of the legal and bank costs can be reduced if the loans are pooled into a bond covering the total of all the borrowers. Pooling may also be possible if a State issuer of bonds and several EZs in the State have requests for several small loans that can be pooled together. In other cases, the tax-exempt bonds can be sold to a local or regional bank that provides a letter of credit guaranteeing payment of principal and interest. A bank enters into a reimbursement agreement with EZ Businesses to pay for the draws on a letter of credit, and then the bank pays principal and interest to the investors. The bank uses its credit rating to get investors to buy the bonds, but relies on EZ Businesses to pay their debt service.

In some cases, an EZ office or a State or local agency may be able to provide a direct letter of credit or guarantee of repayment of the debt by an EZ Business. In all cases, the pooling of loans or the pooling of credits through guarantees by banks may reduce



the costs of borrowing enough to make tax-exempt bond financing work for smaller borrowers. Many local and regional banks have a division or related entity that sells tax-exempt bonds (often called the *Capital Markets* group) that can work with an EZ office to evaluate the feasibility of setting up this type of program.

Challenge 9: Balancing Federal tax incentives with State and local tax liability

Federal tax incentives may not be coordinated with State or local taxes. Taking the Federal incentive may increase State or local tax liability.

The Federal tax system is the “800-pound gorilla” in the taxing system, and many States base their individual and corporate tax systems on Federal taxable income. Many entities make business decisions based on the State and local tax consequences of moving or expanding operations into a particular location.

Taking a Federal tax benefit by being in the RC/EZ results in that benefit not being taken into account in the State tax calculation. For decisionmaking purposes, a business will want to know about that impact. For example, RC/EZ wage credit rules require that a business reduce its employee wages deduction by the amount of the credit. This will increase the amount of income that is subject to tax, but for Federal purposes, the business will be subtracting a credit from the taxes calculated off this income.

However, a business may not be allowed to take a similar credit against State tax liability and also may not be able to alter the taxable income amount calculated for Federal tax purposes because of a possible State tax law that requires it to use the Federal taxable income figure. This increases the amount of income subject to State tax because not all of the wages could be deducted at the Federal level.

Recommended strategy. RC/EZ offices should contact State tax officials to identify conflicts or areas of confusion between Federal and State taxes and develop solutions to the conflicts.

RC/EZ offices can work with State tax officials to identify the overlap and conflict between Federal tax incentives and State tax calculations. In some cases, State tax officials may be able to interpret current law and regulations to clarify how the State tax calculation takes Federal incentives into account. In other cases, these discussions may identify legislative changes that need to be made at the State or local level. If a State tax professional advisory committee exists, it can be an important resource in this process.

A comparison of Federal, State, and local tax incentives may also lead to changes in State or local laws to provide incremental incentives that enhance the Federal tax incentives. For example, if an RC/EZ office identifies businesses that either cannot qualify for Federal incentives or finds them to be not quite enough to attract it into the RC/EZ, the RC/EZ office can work with State and local tax officials to find ways to enact additional incentives to fill the gap. In some cases, short-term tax relief or a grant can succeed in attracting the business.

Marketing Tax Incentives

Challenge 1: Developing the expertise to promote tax incentives

Offering RC/EZ Federal tax incentives to stimulate economic development is different from the traditional approach of offering Federal grant money.

The RC/EZ staff must develop new marketing expertise to promote these benefits to the business community, and the office may not have enough of a budget to begin the process.

Recommended strategy 1. The RC/EZ office should bring together a marketing team to devise ways to market the use of tax incentives.

Marketing the tax incentives can be enhanced by assembling a team of professionals, each of whom has a unique contribution to make to the overall marketing effort. This team should include:

- **Tax attorneys and accountants.** Requirements for the tax incentives tend to be very specific and detailed. Because they affect a business' tax liability, the marketing details should be handled by an attorney or an accountant. Although RC/EZ staff may be able to obtain general information about businesses and tax liability for marketing purposes, such as the ranking of businesses by gross revenues, that information will not tell the extent to which a tax provision may serve as an incentive to a business with large gross revenues. Accountants and tax attorneys, who have a more intimate knowledge of a business's tax status, have a role: to identify tax provisions that reduce their clients' tax liability. Additionally, they can apply the provisions to the individual facts and circumstances of a client. Finally, they will have established an allocation of liability if the application of the facts on the tax return is challenged by an IRS audit.
- **Real estate agencies and developers.** Real estate agencies and developers know what property is available within the RC/EZ, whether a property is environmentally sound, and which businesses may want to locate or relocate in or near it. Real estate agencies will need general information about the incentives to use as part of their marketing to businesses. Developers may be able to use tax-exempt financing for their projects if they are able to obtain qualifying tenants. Advertising in a trade journal or newsletter for local real estate agencies and developers may also be a good way for an RC/EZ office to market the RC/EZ and its incentives. Real estate agencies and local planners can generate block-by-block maps to provide more specific information to businesses so that they can make better informed business

location decisions. Developable sites in the EZ are fertile areas for real estate agencies and developers that are looking for new financial and market opportunities.

- **State and local job placement personnel.** State and local employment services staff should be involved early in the development process. Both WOTC and the WtW Credit require certification by SESA or its designee. Many States have centralized this certification process, and it is important to determine the responsible entity who handles this task for your area. Businesses will be more likely to complete the paperwork necessary for these incentives if a specific contact person is available to answer questions about the certification process. Accountants and attorneys may also want to know how the process works locally and they may want to have access to a local contact person.
- **Independent job placement personnel.** Private recruiters may be able to place RC/EZ residents using WOTC and RC/EZ wage credits. They may also be able to assist businesses in meeting the RC/EZ Business definition, which requires that 35 percent of its employees be residents. School and college placement offices should also be viewed as sources of employees because they educate youth in the age range needed by an employer seeking to use WOTC.
- **Bankers, investment bankers, and tax-exempt bond issuers.** The important role that investment bankers play in identifying and evaluating projects that can be financed with tax-exempt bonds cannot be understated. That role also extends to their ability to offer stock in companies that qualify for the partial exclusion of gain on the sale of EZ stock or the zero percent capital gains incentive for an RC Business. Bond issuers are also critical in the promotion of tax-exempt bonds for an EZ project. It is critical that these issuers become active and involved members of any marketing team early on in the process because only a State or local governmental unit can issue such bonds.
- **Chamber of commerce and community or economic development organizations.** Organizations such as local chambers of commerce are consistently involved in marketing. They can add information on the RC/EZ to their promotional materials, sponsor meetings for local businesses, and use their publications to advertise businesses that have successfully used the incentives. They can also effectively market RC/EZs and RC/EZ residents as employees.

Recommended strategy 2. RC/EZ offices can schedule a series of meetings with the business community throughout the RC/EZ-designation period and prepare for followup meetings.

The business community, residents, and other stakeholders will need an introduction to the RC/EZ concept, tax incentives, and other available benefits. Several introductory sessions should be conducted over the full term of designation because the business community will evolve over that time. Meetings may be cosponsored by local business organizations, local bar or accountant associations, or individual local businesses. Meetings, which should be scheduled for a time most convenient for businesses, should include discussions about the RC/EZ itself, including the relevant Strategic Plan/Course of Action goals, Tax Incentive Utilization Plans (TIUPs), and RC/EZ boundaries.

To assist with the discussion of tax incentives, the meeting should include the SESA contact person, bond issuers, investment bankers, tax professionals, companies that have successfully used tax incentives, and officials who can give an overview of other loan and grant programs and State and local tax incentives available to complement the Federal tax incentives. Followup meetings should accommodate the probability that the business community is constantly evolving and changing numbers, types of business needed to meet market demands, and employee skill levels.

Challenge 2: Matching resident skills to business needs

The educational level and technical skill set of residents may not match the needs of businesses seeking to meet the RC/EZ Business requirement that 35 percent of the employees must live within the RC/EZ boundaries.

Attracting businesses to the RC/EZ will most likely involve both targeting businesses that require employees with the current pattern of education and skill sets and establishing training programs to develop education and skill sets to match the needs of businesses with higher requirements that want to move to the RC/EZ or expand a current location. Consequently, the designated area must have an ongoing grasp of the numbers and skill levels of its employable residents. The challenge is to target businesses that fit the designee's population skills, help businesses meet their turnover needs, and establish training programs to match businesses' employment needs.

For example, if an Internet servicing company wants to locate in the RC/EZ, the RC/EZ office may be expected to help that company identify potential employees for computer repair and operation, computer programming and troubleshooting, telemarketing, call center operations, billing and accounting, office management and human resources, custodial services, and executive positions. Conversely, a business that seeks to locate a grocery store in the RC/EZ might require a different workforce yet still expect the RC/EZ to help them find employees.

In the case of the capital incentives, the business will have to meet the 35-percent test for a period of time. The length of time will depend on the specific incentive. For example, if a printing business is using the increased Section 179 expensing incentive for a piece of equipment it would otherwise have depreciated over 10 years, it must meet the RC/EZ Business test for 80 percent of that time (8 years). Many businesses expect turnover in employees, so the RC/EZ office must assure the business that it can assist in identifying future RC/EZ-resident employees. Some businesses may hesitate to use the tax incentives because they fear losing the benefit if they cannot meet the 35-percent test. To effectively market the incentives, RC/EZ offices must know the number and qualifications of RC/EZ residents available for employment.

Recommended strategy. RC/EZ offices should set up job placement advisory committees to survey needs and available workers.

RC/EZ offices will want to hold informational meetings and perhaps develop an advisory committee composed of job and school placement practitioners to assist them in identifying the RC/EZ residents needed to meet the 35-percent test. These practitioners can provide information on the current educational level and skill set of residents to assist the RC/EZ office in evaluating strengths and gaps in employees as a marketing strategy for tax incentives. The marketing efforts may result in the identification of educational and training needs that are not being met by current programs.

Challenge 3: Addressing obstacles to outreach

Small business owners may not be able to attend meetings on the RC/EZ tax incentives but are likely to hire residents. They also may not engage a tax professional to complete their tax returns. Outreach to these businesses may prove more difficult.

Recommended strategy 1. An RC/EZ office can use local government tax mailings to send informational brochures to these small businesses.

One way to market information to businesses about the credits is to include information about them in business tax mailings made by the local government. For example, a local government may send invoices for business license taxes or forms for submitting business franchise tax payments. One-page fact sheets on WOTC and the RC/EZ wage credits can easily be enclosed with wage or business license tax mailings and may provide broader coverage than other mailing lists available to the RC/EZ.

Recommended strategy 2. An RC/EZ may use HUD's electronic file to track RC/EZ businesses' use of the tax incentives.

HUD provides each RC/EZ with an electronic file containing information from Dunn and Bradstreet that identifies businesses located within each designated area. From that list, RC/EZs can establish goals in each of the four categories of tax incentives: wage credits, deductions, bonds, and capital gains. Staff can then identify those businesses that are best suited for one or more of the tax incentives. The RC/EZ can develop a plan for contacting the business that includes the resources that will be used for notifying businesses of the various tax incentives that may be available to them.

Challenge 4: Providing wage credit outreach to RC/EZ residents

The RC/EZ office must reach out to residents and ensure that they know their worth as a tax credit to the business that hires them.

RC/EZ residents do not get the actual benefit of the tax credit on their personal tax returns. Their employer gets the credit. Residents seeking jobs or hoping to change jobs may not be aware of their added value to a business because of RC/EZ wage credits.

Recommended strategy 1. An RC/EZ can establish precertification programs for WOTC and the WtW Credit that reinforce how employees help a business' bottom line.

WOTC and the WtW Credit require precertification of targeted-group members. For example, youth living in the RC/EZ could obtain certificates from SESA (or its permitted designee) in the spring identifying them as eligible for the WOTC summer youth category. That essentially means SESA has established that the youth are the right age and live in the RC/EZ. A company could get a tax credit for employing the youth between May 1 and September 15.

In the interview process, a youth would present the precertification, which the employer could attach to the form it sends to SESA for final certification. Local schools should be involved in this effort. If employers are unaware of WOTC, arming residents with precertification forms and informational pamphlets could greatly increase employers' awareness of this wage credit.

For the summer youth category, an RC/EZ office should identify any high-profile summer job programs, such as the mayor's summer youth initiative or a local high school outreach program, that the RC/EZ program could pair up with to market this tax incentive. Seasonal employment opportunities, such as daycare programs, summer camps, hotels, tourist attractions, and farming operations should be a focus for any RC/EZ. The WOTC summer youth category (ages 18 to 24) has direct relevance to these types of jobs, particularly since the employer does not have to be located in the RC/EZ to take the credit; the employee just has to be a resident.

Precertification efforts for WOTC should be directed toward high schools, junior colleges, colleges and universities, technical schools, and computer training programs that serve this age group. Linking the SESA contact to these training programs will expand the marketing of this incentive. WOTC is available for first-year wages so youth in these programs might be eligible if they work part-time or full time on completion of their studies.

Recommended strategy 2. An RC/EZ office should brainstorm to identify places it can reach residents living in the RC/EZ.

Efforts to disseminate information should extend to any housing or apartment complexes within the RC/EZ. This is a way to reach residents to let them know that they are valuable to an employer and to increase precertification efforts. RC/EZs should consider placing public service announcements on buses, other forms of public transit, and any other places where people have a chance to focus and read information.

Challenge 5: Marketing State and local tax incentives

The RC/EZ offices must identify and market State and local tax incentives. In some cases, they may need to advocate for new legislation or programs.

The State or local tax system may include income tax incentives similar to Federal tax incentives that can be used to increase the overall benefits a business receives by locating in the RC/EZ. For example, a State tax code may provide a tax credit to businesses that hire residents living in a State enterprise zone. A business may qualify for reduced property taxes for locating in an area that is also within an RC/EZ, or its local tax entity may waive recording or transfer taxes for property purchased within an RC/EZ, reducing the cost of acquiring land or buildings.

In high tax jurisdictions especially, RC/EZ offices can enhance their marketing efforts if they can identify State and local tax benefits that can be taken in addition to the Federal incentives for businesses located in the RC/EZ. However, rules for Federal and State incentives may conflict, and RC/EZ offices must know the differences to portray the scenario accurately.

Recommended strategy 1. Develop a working relationship with State tax officials who are familiar with State economic development incentives.

Historically, State governments have used tax incentives to stimulate economic development and attract new businesses. State officials or, in some cases, former State officials can provide important practical information on how to market incentives and identify the types of businesses that have taken advantage of similar incentives. State and local contact people can also provide the RC/EZ offices with a catalog of incentives available to businesses that can supplement the Federal RC/EZ incentives. These incentives can be used by businesses that would not otherwise qualify for the Federal incentives because they are located outside an RC/EZ or because the nature of the business does not allow it to qualify as an RC/EZ Business.

For example, a software company that cannot qualify as an RC/EZ Business because it develops an intangible for sale or license may qualify for State incentives directed toward attracting technology businesses. A business that cannot obtain tax-exempt bond financing because its sales offices are located outside the EZ may qualify for State low-interest loans for rehabilitating buildings in economically distressed areas.

Recommended strategy 2. An RC/EZ office can set up links with State tax officials to jointly develop materials and show the interactive effect of Federal, State, and local incentives.

State economic development offices have developed Web sites and printed materials to market their incentives and various programs to businesses. RC/EZ offices should explore ways to link their Web sites with the State's and ways to market materials that can be disseminated through State resources. RC/EZ offices can work with their tax professionals to develop materials to show how a business can reduce its overall tax burden by taking both Federal and State or local tax incentives. They can create charts to lay out the similarities and differences in the incentives and provide important information to both businesses that qualify for the Federal tax incentives and those that might qualify only for State incentives or programs.

Optimizing the Commercial Revitalization Deduction

Challenge 1: Optimizing the Commercial Revitalization Deduction

The Commercial Revitalization Deduction (CRD) cannot be carried over to future years if the full $12 million is not used in its entirety in 1 year. To receive the maximum benefit of this incentive, an RC must carefully devise a way to monitor allocations and the progress of potential qualifying projects.

Recommended strategy 1. Identify sources of information regarding future and completed projects so that some flexibility exists in allocating the CRD.

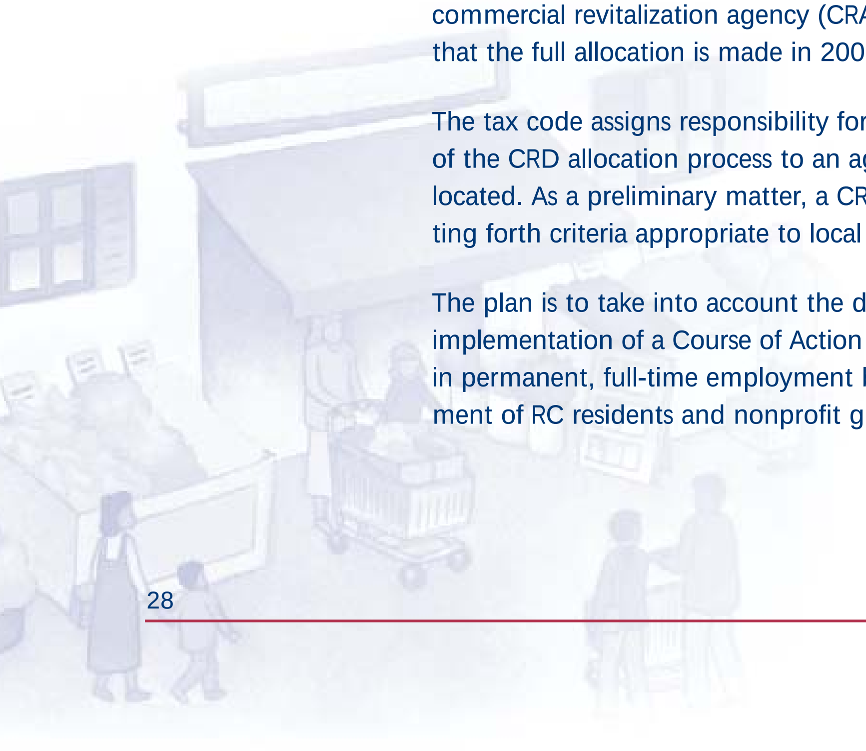
In general, an allocation for any calendar year can be made for a project that will be placed in service in that calendar year. However, there is a limited exception for an allocation in year 1 for a project placed in service in a subsequent year. For example, an allocation for calendar year 2002 could be made for a project placed in service by the end of 2004 if the project owner has made expenditures equal to 10 percent of the expected project cost in 2002. The tax rules also permit the State allocating agency to enter into a binding commitment to allocate from future year allocations.

These various timeframes suggest that an RC should develop an ongoing list of construction, renovation, and expansion projects. With respect to immediate and upcoming projects, this information might come from real estate brokers, developers, construction contractors, or bankers. The local business licensing department or agency can also provide information. For upcoming projects, the local permitting agency or department could provide information by street address to determine which projects are in the RC. The governmental office issuing certificates of occupancy could alert the RC to projects that are ready to be placed in service and thus in a more immediate position to receive a CRD allocation. For new businesses, requests for electrical service or water may indicate that a new project is coming on line.

Recommended strategy 2. The RC office should establish a procedure with the State commercial revitalization agency (CRA) responsible for allocating the CRD to ensure that the full allocation is made in 2002 and each subsequent year.

The tax code assigns responsibility for carrying out several initial and ongoing steps of the CRD allocation process to an agency authorized by the State in which an RC is located. As a preliminary matter, a CRA must develop a qualified allocation plan, setting forth criteria appropriate to local conditions to be used to determine its priorities.

The plan is to take into account the degree to which a project contributes to the implementation of a Course of Action devised by the RC, the amount of any increase in permanent, full-time employment by reason of any project, and the active involvement of RC residents and nonprofit groups. The RC, through its application process



and development of its TIUP and in partnership with its CRA, should develop the allocation plan. The plan must be the subject of a public hearing and must be approved by the Governor or State legislative body before any allocations can be made.

Although the tax rules provide that the CRA must notify the local government when an allocation is to be made within its jurisdiction and must provide for comment from the local government, the RC's active continued involvement in each step of the process will ensure more efficient and effective use of the CRD. For example, in conjunction with the CRA, the RC could analyze prospective projects and make recommendations. Each project must have an allocation before the tax incentive is available, which creates an ongoing opportunity for an RC to work with the CRA. The RC may also play a role in determining whether job projections are met and in monitoring ongoing compliance with requirements placed on the building receiving the CRD.

Assisting RCs/EZs Through the New Markets Tax Credit

Challenge 1: Marketing NMTC as a new source of capital

Businesses and investors in the RC/EZ may be unaware of the New Markets Tax Credit (NMTC) as a source of capital for loans and equity investment or as a tax credit for investors. The NMTC program started in late 2002 with $2.5 billion in credits to be allocated, building up to a full $15 billion in accumulated credits by 2007. For further information regarding NMTC, please see page 89 of the HUD publication *Tax Incentive Guide for Businesses in the Renewal Communities, Empowerment Zones, and Enterprise Communities.*

Recommended strategy 1. The RC/EZ can go through the process of obtaining an NMTC allocation itself.

NMTC, which can only be allocated to a for-profit credit community development entity (Credit CDE), must be allocated to an organization through an application process conducted by the Community Development Financial Institution (CDFI) Fund of the U.S. Treasury Department. The main requirements are that the organization has a primary mission of serving low-income communities and is accountable to these communities. The RC/EZ is likely to be a nonprofit organization that can meet the other requirements, but nonprofit entities cannot receive an allocation except as a partner or member of a for-profit entity that receives an allocation. A nonprofit may contribute its expertise and historic mission to a for-profit Credit CDE to help it obtain an allocation.

Once the for-profit receives an allocation from the U.S. Treasury as a Credit CDE, the RC/EZ can assist it in identifying businesses and projects that will qualify as investments.

Within a year of receipt of funds from an investor, a Credit CDE must invest at least 85 percent of the funds in equity investments or loans to businesses in low-income communities (including the RC/EZ). The requirements for a qualified business are similar to those for an RC/EZ business but less restrictive.

The RC/EZ can serve a key role by setting up a pipeline for investments by the Credit CDE, and the NMTC funds from investors may allow the RC/EZ to provide assistance to businesses that otherwise might not qualify for the RC/EZ incentives. For example, for the NMTC loan or equity investment, a commercial real estate project's qualification does not depend on whether the tenants themselves are qualified businesses and the qualifying business does not need to meet the requirement that a minimum percentage of its employees be RC/EZ residents.

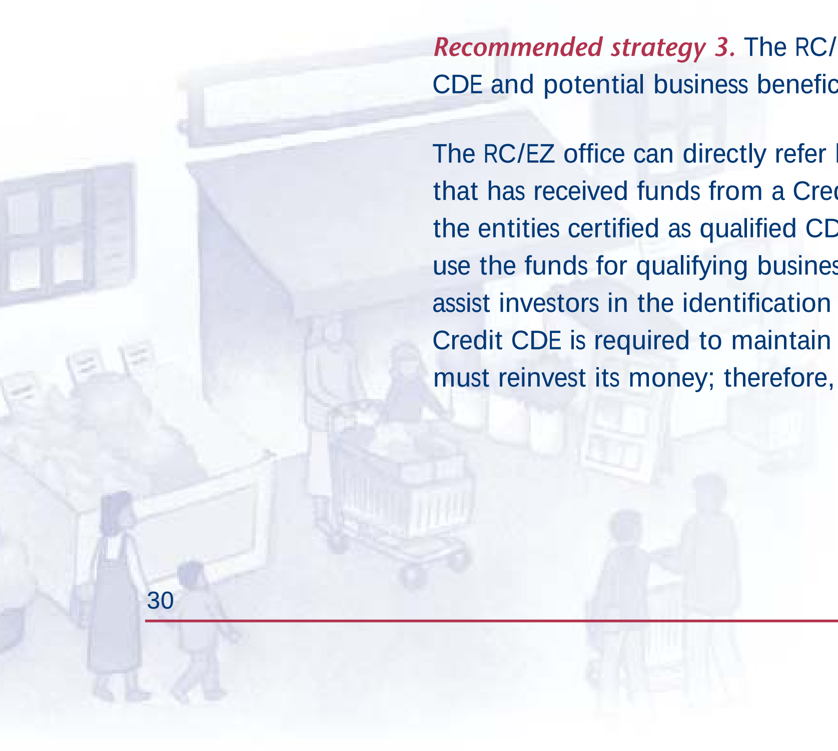
Recommended strategy 2. The RC/EZ can become certified as a CDE and sell its loan portfolio (consisting of loans made to qualified businesses) to a Credit CDE, or it can obtain a loan or equity investment from a Credit CDE to provide capital to the RC/EZ to make loans to, or equity investments in, qualifying businesses.

The tax rules encourage investors to purchase loans of, or make loans to, other CDEs that do not themselves receive an NMTC allocation. The RC/EZ can go through the process of becoming certified by the CDFI Fund based on its primary mission of serving low-income communities and being accountable to these communities. This certification will allow the RC/EZ to seek funds of the Credit CDE, which will generate a source of cash that the RC/EZ can use to make equity investments or business loans in the RC/EZ.

The cost of the capital will vary based on many factors. Although the investor in the Credit CDE receives a tax credit, no Federal tax rules exist regarding the extent to which the benefit of that credit gets passed on to the investments made by the Credit CDE. The tax rules do not require that a loan to a CDE or qualified business be below market, for example. The main benefit of NMTC to the RC/EZ will be the potential capital available to invest in the RC/EZ.

Recommended strategy 3. The RC/EZ can serve as an intermediary between the Credit CDE and potential business beneficiaries in the RC/EZ.

The RC/EZ office can directly refer businesses to a Credit CDE or to a qualified CDE that has received funds from a Credit CDE. The list of entities receiving allocations and the entities certified as qualified CDEs are available from the CDFI Fund. Investors must use the funds for qualifying businesses in areas such as an RC/EZ, and an RC/EZ can assist investors in the identification of projects and businesses that would qualify. The Credit CDE is required to maintain an 85-percent level of qualified investments and must reinvest its money; therefore, the RC/EZ can be an important pipeline.



Recommended strategy 4. An RC/EZ office can market NMTC to potential investors in a Credit CDE as another tax incentive available through the RC/EZ.

Like many of the tax credits available for employing RC/EZ residents, NMTC provides a credit against Federal tax liability. The investor in a Credit CDE can receive a credit ranging from 5 to 6 percent over a 7-year period. The credit is in addition to any return an investor might receive from a stock or partnership interest. Individuals and businesses within an RC/EZ or having an interest in it can benefit and the RC/EZ office should market NMTC.

Raising Awareness of Tax Incentives

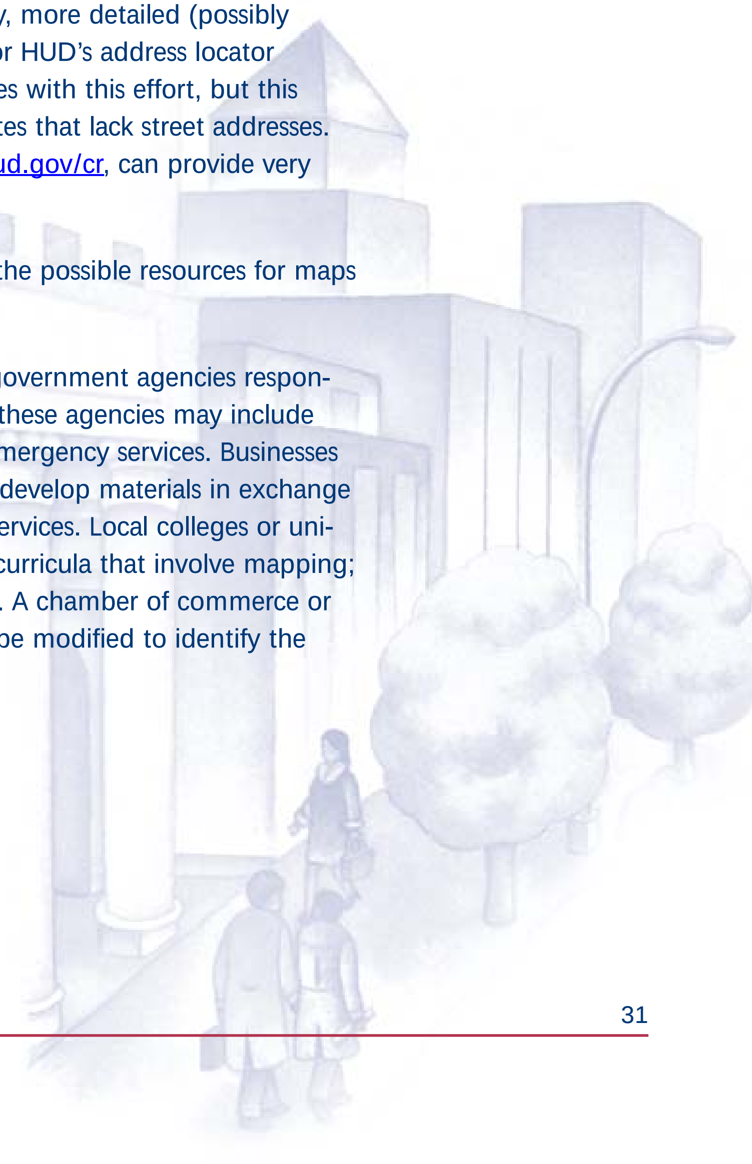
Challenge 1: Making boundary maps for RC/EZ

Maps for RCs/EZs must be very detailed to ensure that businesses and residents know the boundaries.

Written materials, such as marketing packets, should include a map of the overall qualifying area, but detailed maps will also need to be produced in a size that is legible and portable for businesses to study. The maps used in meetings or available onsite at the RC/EZ program office are likely to be large, sturdy, more detailed (possibly an aerial map) and designed for display. The Web site for HUD's address locator (http://hud.esri.com/locateservices/ezec) helps businesses with this effort, but this system may not be helpful for rural areas or industrial sites that lack street addresses. The Web site for the RC/EZ Initiative, located at www.hud.gov/cr, can provide very detailed maps.

Recommended strategy 1. An RC/EZ should identify all the possible resources for maps and mapping skills.

This strategy would include contacting local and State government agencies responsible for maps of the RC/EZ. Responsible entities within these agencies may include planning and development offices or fire and medical emergency services. Businesses that do surveys may contribute their time and talent to develop materials in exchange for acknowledgments that will help them market their services. Local colleges or universities do field studies for communities in a variety of curricula that involve mapping; an RC/EZ may provide a unique educational experience. A chamber of commerce or similar organization may also have materials that could be modified to identify the location of an RC/EZ.



Challenge 2: Compensating for lack of public tax information on individual businesses

Because tax information is not publicly available, it is difficult for an RC/EZ office to obtain sufficient information about a business's Federal tax position to really target incentives.

An RC/EZ office typically has a great deal of information about businesses existing in the RC/EZ and even about businesses that it may recruit or contact about locating in the area. This information may include company revenues, number of employees, location of business headquarters, outlets, and types of jobs available at the company. (For startup businesses, this information may not be available.) However useful the available information is to an RC/EZ's marketing efforts, it will not reveal much about the potential attractiveness of tax incentives to a potential RC/EZ business. Business Federal tax returns are privileged information that is not divulged in public reporting forms or business digests.

The Federal tax code is a complicated system. Over time there can be a wide variety of tax incentives and disincentives that can dramatically alter a business's tax liability. This means that an RC/EZ cannot assume that a company with a history of large gross revenues will have a tax liability large enough in the future to generate continued interest in wage tax credits. The company may find other deductions or tax credits to reduce its tax liability.

Although wage credits can be carried forward 20 years, it would be difficult for an RC/EZ program to predict whether carrying credits forward would be attractive to a business that has found other ways to reduce its liabilities or to a startup business that does not anticipate any Federal tax liability for several years. Also, a company may be in a better tax position if it can increase its deductions rather than use tax credits.

The RC/EZ office may have a company contact that is not familiar with the company's Federal tax position. An individual stockholder of a company may not benefit from a rollover of capital gains this year, but it may be beneficial a few years from now. The tax concerns of an individual stockholder, even a majority one, may not be known to the company representative.

Tax credits typically do not allow an amount taken as a credit to also be deducted from income in calculating taxable income. An inability to deduct otherwise common business deductions will increase taxable income in a way that affects other tax calculations or benefits and could increase a company's tax liability. Hence an RC/EZ marketing program must use caution when predicting that a company's taxes would be reduced with the RC/EZ incentives.

Ultimately, the IRS plays an important role in determining whether incentives are available for a particular business and is the final authority on whether that business

is eligible for one or more of the available tax incentives. Consequently, a business must work closely with its tax professional when deciding the value of the tax incentives.

Recommended strategy. An RC/EZ should set up an advisory committee of tax professionals to educate other professionals and businesses and to identify ways to track incentives.

For RC/EZ programs, tax professionals make important links to companies. Tax professionals have the information on a specific company's tax situation that an RC/EZ office may not be able to access. Not all companies hire accountants or tax lawyers to do their tax returns, but many do, and tax professionals welcome ways to obtain new clients through their expertise in finding tax benefits. Given the technical nature of the tax incentives, RC/EZ offices may want to establish an advisory committee made up of several tax professionals.

Some RC/EZs may have used the services of an accountant or tax attorney in the process of creating the EZ Strategic Plan or RC Course of Action and/or the TIUP. Because of this experience, a particular accountant/tax attorney may be willing to head up an advisory committee. If not, the RC/EZ office can contact a State or local organization of accountants and attorneys to identify potential members for an advisory committee. A faculty member or advanced student from a nearby law or accounting school may be willing to participate.

The advisory committee can serve to develop and review marketing materials, provide general advice to RC/EZ program staff, make presentations at community and business meetings, interact with State officials on any overlap of Federal and State incentives, and prepare materials for a Web site or for newsletters.

Challenge 3: Educating tax professionals about tax incentives

Most RC/EZ program staff are not tax professionals and should not assume the liability of giving specific advice about the extent to which a business will qualify. The challenge is to educate tax professionals about the incentives and ensure they will be available to handle issues.

Some tax incentives are more straightforward than others. In all cases, there are a number of very detailed rules. Despite the detail, there will always be some ambiguity as to whether a company meets a certain requirement. Absent a specific answer from the IRS, a company would have to evaluate its own particular facts and interpret those facts in light of the tax requirement.

If a company determines it meets a requirement, it will take such a position on its tax return. If the company is wrong and the IRS successfully challenges its position, the company could be liable for taxes, penalties, and interest. An RC/EZ office never wants to place itself in the position of giving advice on tax incentives that could result in any tax liability. The need to keep marketing materials and face-to-face discussion of the tax incentives general may sometimes appear in conflict with the desire for successful targeted marketing, however.

RC/EZ offices do not have the expertise to provide tax advice to businesses in their marketing efforts. Additionally, RC/EZ offices cannot advise businesses facing IRS challenges to use a particular incentive. If a business is ineligible for an incentive, it must bear the brunt of an IRS sanction. Tax lawyers and tax accountants can provide the type of service needed, and they can also be effective partners with an RC/EZ in the marketing of tax incentives. Tax incentives available in RC/EZs are all modifications to incentives that have been in the tax code for many years.

Tax professionals need to stay abreast of particular modifications to the existing incentives for the RC/EZs, and they are the ones expected to advise companies on the interpretation and application of the rules. RC/EZ offices will need to develop an aggressive marketing program to reach the tax professionals who have access to the privileged tax information of their clients. Although RC/EZ administrators cannot provide tax advice to businesses, it is important that they have an overall knowledge and understanding of the tax incentives.

Recommended strategy 1. An RC/EZ should establish ongoing training sessions for tax professionals, including courses that qualify for continuing education credits.

RC/EZ offices are strongly urged to work closely with their advisory committees to set up ongoing training programs for tax professionals. These training programs will give an RC/EZ office the opportunity to provide tax professionals with specific information about RC/EZ boundaries and the resources available for certifying which employees live in the RC/EZ. If an RC/EZ and its advisory committee consider how the training sessions could be structured to provide continuing education credits for the professionals, they will encourage broader participation. These training sessions will hopefully also encourage a continuing dialog between the professionals and the RC/EZ resulting in important feedback to RC/EZ program administrators.

Because tax professionals have intimate knowledge of clients' tax returns, they should be able to provide aggregate general information on the successful use of incentives and any factors that might be hindering their use. For example, tax professionals may be able to identify a specific type of business that is having difficulty meeting the 35-percent test.

Because income tax information is privileged, tax professionals may not provide specific information to RC/EZ offices with respect to an individual business. They can provide general information on the use of incentives. Tax professionals may also be willing to contact specific business people to serve as speakers at informational meetings or to act as mentors to other businesses considering the use of tax incentives.

Recommended strategy 2. RC/EZ offices may obtain pro bono assistance from tax professionals for specific tax questions.

An RC/EZ office may want to identify a tax professional to provide ongoing advice about the specific details and initial advice about the application of incentives to specific situations. In some situations, tax professionals commit to providing pro bono legal or accounting services and the RC/EZ office can make use of these opportunities. In other cases, the tax professional may offer services at a reduced rate to businesses referred by RC/EZ offices.

Challenge 4: Addressing circumstances particular to small retail operations

Small retail operations may represent a large part of the RC/EZ business community, particularly if the entities rent space rather than own their locations. They may have relatively small capital needs and annual cash flow, making the financing of equipment purchases or space renovations difficult.

Recommended strategy. An RC/EZ can focus marketing efforts on the increased Section 179 deduction and identify loan funds that might assist the business in purchasing equipment.

Retail businesses tend to be more labor intensive and have relatively few capital costs. They may pay for some capital improvements in the space they lease, and their equipment needs may be limited to computers, cash registers, and shelving or racks.

All businesses are able to use the increased Section 179 deduction to expense some equipment expenditures up to a certain amount (around $25,000), but a business that meets the RC/EZ definition can expense up to an additional $35,000. If loan funds are available for equipment purchases, a business may be able to upgrade or purchase its equipment sooner than expected. Having the ability to expense the equipment cost because it is used in the RC/EZ may allow a business to save taxes in the purchase year and put the money back into the business. The equipment purchase or upgrade may also allow the business to generate more income.

Challenge 5: Determining eligibility for environmental cleanup sites

Some areas included in the RC/EZ may be abandoned industrial sites that must be cleaned up before development can take place. The tax incentive targeted toward environmental cleanup is limited to certain types of contamination and the incentive rules require that the owner receive certifications about the site's eligibility.

The environmental cleanup tax incentive may not be widely used in a particular State. It requires a specialized knowledge of contaminants and the types of costs that must be incurred in cleaning up the site. For example, the tax incentive is only available if the owner capitalizes the costs (deducts over time). Because of the technical definition of contaminants contained in the tax rule, an RC/EZ may have difficulty identifying qualifying sites. In addition, an RC/EZ may not be familiar with the appropriate procedures for acquiring certification from the State.

Recommended strategy. An RC/EZ needs assistance to identify industrial and commercial sites in need of remediation that could qualify for the environmental cleanup deduction.

The environmental cleanup tax incentive will assist businesses that expect to incur capital expenditures to clean up property in the RC/EZ. The ability to deduct those expenditures may make the difference in a business's decision to purchase and develop a site. The eligibility requirements are very technical. An RC/EZ office should bring together local real estate agencies and brokers as well as State and local environmental officials to identify sites that qualify. The rules require that the State environmental agency certify that the site is eligible so it is important to establish contact with the appropriate State official.

Challenge 6: Marketing Qualified Zone Academy Bonds to public schools

Local public schools may be unaware that they are able to borrow funds at no interest by using Qualified Zone Academy Bonds (QZABs) to help set up programs to train RC/EZ students. The school system may need assistance with assembling all the participants required for a QZAB, including the State education department, the business community, and private investors.

Recommended strategy 1. The RC/EZ can put schools in touch with the local business community to develop an appropriate curriculum as required by the tax rules.

QZAB rules require that the proceeds of the bonds be used in a school, or in a program within a school, that has a curriculum designed in conjunction with private business to increase graduation and employment rates and better prepare students to participate in a complex workforce. To market these tax incentives, the RC/EZ office will identify specialized training needs of businesses currently in, relocating, or expanding to the RC/EZ.

Some of these training needs can be met through programs at the public school level. For example, a local healthcare office may need entry-level technicians to operate new equipment and could identify specific skill sets needed for this type of job. The RC/EZ office can facilitate dialogue between the school and businesses. This can be accomplished in a more permanent way by making sure that a representative of the school system is on the RC/EZ advisory group, or it may occur in a less formal manner through a series of meetings with a specific business or industry segment. The business partners

may also help to analyze how the proceeds of QZABs can be used to renovate buildings, acquire equipment or educational materials, train teachers, and provide students with mentorships or internships.

Recommended strategy 2. Identify businesses that can make the monetary or in-kind services commitments that the school is required to have in place before the QZABs are issued.

To qualify for zero-percent financing, the borrowing school system must demonstrate that its qualifying school or program has commitments from private businesses equal to 10 percent of the amount to be borrowed. These commitments can be in the form of equipment, materials, donated services for curriculum development, teacher training, mentorships, internships, or cash that will be used for any of these purposes. The contributions can be made at the time the QZAB is issued, or the business and school may set up a schedule of commitments over time. The RC/EZ office can help the school find donors to meet this requirement.

Recommended Strategy 3. The RC/EZ office can work with the school system to identify qualifying schools and obtain the volume cap from the State.

Schools located in an EZ automatically meet one of the requirements for QZAB financing, and the EZ can assist a school system in identifying EZ boundaries. Schools located in an RC do not automatically meet the requirement under the current tax rules, but schools in an RC will likely meet the alternate criterion that 35 percent of students receive free or reduced-price lunches. The RC office can analyze the schools within its boundaries.

In addition, a school must receive an allocation from the State department of education in the amount of the QZAB because tax laws limit the amount of QZABs that can be issued each year nationwide. An RC/EZ may be able to help the school system with obtaining an allocation through its State partners that participated in the RC or EZ application.

Recommended Strategy 4. Market the QZAB to banks and insurance companies as a tax incentive they can receive.

QZABs can be purchased only by banks, insurance companies, and lending corporations. The RC/EZ may be able to help the school identify potential purchasers from its contacts in the business community. QZABs can provide a bank or insurance company purchaser with a tax credit that reduces its Federal tax liability regardless of whether the investor is located in an RC/EZ. Although the school district pays zero-percent interest on a QZAB, the investor receives a tax credit against its Federal tax liability as a payment in lieu of receiving interest from the school system. Neither banks nor insurance companies can meet the definition of an RC/EZ Business because of limits on certain financial instrument holdings, so the QZAB is an incentive the RC/EZ can market to these groups.

Evaluating the Effectiveness of Tax Incentives

Challenge 1: Tracking the use of tax incentives

Tracking the use of incentives in an RC/EZ will be difficult. IRS data on use of the Federal tax incentives will not be sufficient to identify use of the incentives in any particular RC or EZ.

The IRS can track the use of the Federal tax incentives, but it takes time. There will be a time lag beginning with when a business qualifies for an incentive to the time it files a tax return and, finally, to the time the data on the incentives are analyzed and reported by the IRS. In addition, the information will be aggregated nationwide, so it is unlikely that any RC/EZ program will be able to evaluate its success in marketing an incentive or to determine the extent to which businesses in the RC/EZ were able to take advantage of the incentives.

Recommended strategy 1. An RC/EZ can collect data on use of incentives from local tax professionals.

Tax professionals may be able to provide data on an aggregate basis or with respect to specific types of business clients (small versus large, professional versus retail) that are able to use a tax incentive. They may also be willing to give a range of the dollar amount of specific tax incentives taken by clients. Equally important, tax professionals may be able to identify reasons why incentives could not be taken or had to be taken at a diminished level. This information can guide an RC/EZ's future marketing and educational efforts. RC/EZ offices can also measure success in their marketing efforts by cataloging the number of tax professionals who attend training sessions or make presentations at meetings or conferences.

Recommended strategy 2. An RC/EZ can track the use of wage incentives through job placement and training partners.

Given the limitations of IRS data, RC/EZ offices may be more successful in tracking the use of the incentives by working through some of their partners in the process or by gathering information through a survey approach. Partners such as job placement and training programs or the RC/EZ programs themselves may be able to track the number of precertifications of employees for the RC/EZ wage credits. Job training and placement partners may track how many participants in their programs obtain jobs and, in some cases, how long they retain these jobs. They may also be able to determine the extent to which the programs are able to adapt to meet educational and skill-set requirements of businesses within the RC/EZ.

Recommended strategy 3. An RC/EZ office can obtain data from SESA on use of WOTC and the WtW Credit.

SESA is required to report WOTC certifications, including the number within each specific targeted group. However, this will not be an accurate reflection of the number of employees that actually generated credits because some of them may leave before meeting the minimum number of hours or the business may decide not to take the credit. RC/EZ offices may need to establish ways to track the incentives to a specific RC or EZ if there is more than one in the State.

Recommended strategy 4. An RC/EZ can tap into local resources to develop and interpret surveys on the use of incentives.

In recognition that a company may be very reluctant to disclose the exact dollar amount of tax benefits it was able to take, RC/EZ offices may want to develop surveys to gather information within an approximate or range basis. For example, if participants in the training programs were tracked, they could be asked to respond to a survey indicating which incentives they had taken, the range of the dollar value of these incentives to their businesses, and the perceived difficulty of taking the incentives. The surveys could solicit volunteers to mentor other businesses, appear as panelists in future programs, or prepare testimonials to use in marketing materials or Web site development.

The General Accounting Office and other researchers have used surveys to gather data on the use of the RC/EZ tax incentives. The reports prepared for these programs may provide guidance with respect to the types of questions that can be asked. Also, RC/EZ offices may be able to work with professional survey developers or with local colleges or universities that provide this type of training or service.

Recommended strategy 5. An RC/EZ can use hits on its Web site to provide limited data on use of the incentives.

Visits to an RC/EZ Web site can be another gauge of the use of incentives and the program's marketing efforts. In particular, this data may indicate which incentives generated more interest or more questions. The Web site can also include survey questions about which incentives a business expects to be able to use, which ones it has already used, and in which areas it needs additional information. The number of hits on a Web site is merely a rough measure of incentive use, but it may be helpful in explaining the results of information gathered from other sources and methods or it may fill gaps in the other information.

Part 2: Case Studies

Enterprise Zone Facility Bonds Fund Major Projects in Boston

In 1999 HUD designated areas in Boston as a Round II Empowerment Zone (EZ). It includes nearly 60,000 residents, covers 5.8 square miles, and expands over sections of the city's Chinatown, downtown, and seaport district as well as Dorchester, Jamaica Plain, Mission Hill, Roxbury, South Boston, and South End. The EZ has used its designation and its financial savvy to obtain a combined $61.4 million in bond financing in just 3 years.

Boston Connects, Inc., established in November 1999, administers and implements the Boston EZ's Strategic Plan for expanding human and economic development. Boston Connects Inc. has 24 members on its board, 12 of whom were appointed by Mayor Thomas M. Menino and 12 of whom are EZ residents who were elected to the board.

Enterprise Zone Facility Bonds. In early 2001 the Best Western Roundhouse Suites Hotel became the first hotel to open in a Federal EZ in the northeast due in part to the use of available Enterprise Zone Facility Bond financing. The hotel cost $10 million to build of which $8 million was financed through Enterprise Zone Facility Bonds. The hotel provides approximately 24 full-time jobs, most of which are held by city residents. This development has had the added impact of rehabilitating a long-vacant historic structure and assisting in the revitalization of this section of the EZ. Because many of the hotel's employees also reside in the EZ, Best Western took advantage of the EZ Wage Credit. The hotel received approximately $20,000 in these credits in 2001 and can continue receiving these credits yearly through 2009.

Pilot Seafood Distribution in the seaport district opened in April 2000. This new 65,000-square-foot seafood processing, packaging, and distribution center supports Boston's $650 million seafood industry. The project used $10 million in Enterprise Zone Facility Bonds, all guaranteed by the Commonwealth of Massachusetts' port authority.

Most recently, Boston used Enterprise Zone Facility Bonds to help fund phase I of the Crosstown Center, a multi-use complex where construction began in fall 2002. This $140 million project received approval from the Boston Connects, Inc. board for $48 million in bond financing and will be built in two phases. Phase I, for which $43.42 million in bonds has been issued, will include a 190-room Hampton Inn and Suites and more than 15,000 square feet of ground-level retail space and a parking structure.

Phase II will include offices and additional parking. When the center is complete, there will be as many as 1,500 permanent employment positions in the hotel, offices, stores, and parking structures. It is expected that EZ residents will hold a significant number of these jobs.

Collaboration with the city of Boston's industrial development financing authority helped facilitate these transactions. For more information on these successful tax incentive transactions in the Boston Empowerment Zone, please call Christine Araujo, executive director of Boston Connects, Inc., at (617) 541–2670 or visit the Web site at www.bostonEZ.org.

Wage Credits and Work Opportunity Tax Credits Generate Savings for Cleveland Empowerment Zone Businesses

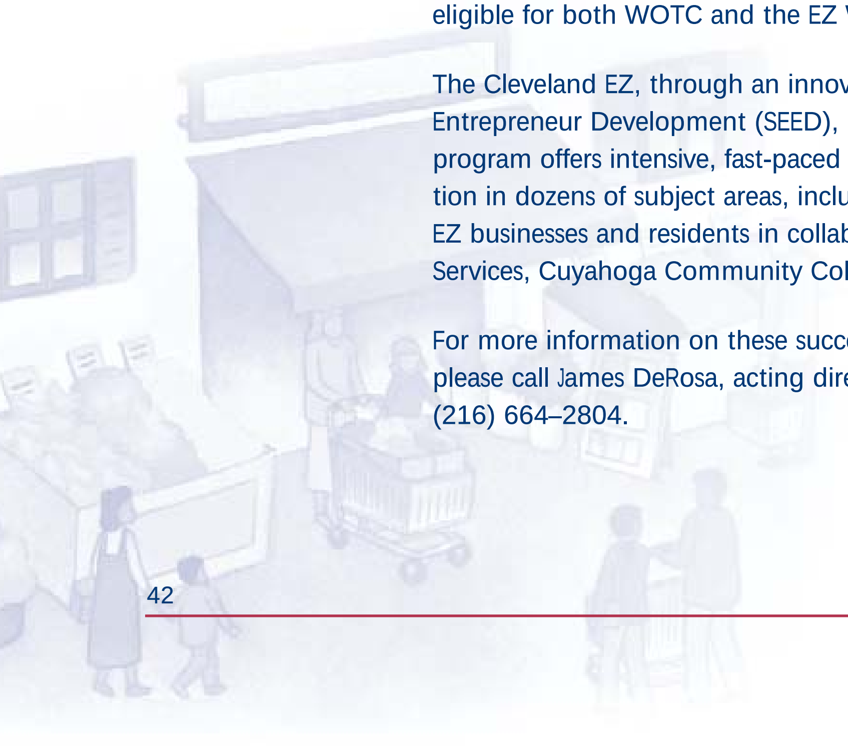
In 1997 HUD designated a supplemental Round I EZ in distressed areas of Cleveland. The EZ Wage Credit became available in these areas on January 1, 2000.

The Cleveland EZ has worked with accountants to help market the EZ tax incentives to businesses located in this area. The owner of a small company that provides security services worked with one of these accountants to take advantage of both the EZ Wage Credit and the Work Opportunity Tax Credit (WOTC). (This company has been located in the EZ since 1993, which is prior to EZ designation.) Approximately 90 percent of the company's employees live in the EZ.

The company began taking the EZ Wage Credit for its existing employees in the latter half of 2001 and will be able to receive the wage credit on those employees until the EZ designation ends. The EZ Wage Credit creates significant tax savings for this business because it can receive a $3,000 yearly credit for each resident employee who receives annual wages of $15,000 or more. In addition, since becoming aware of the incentive, the company has been more attentive to hiring employees who would be eligible for both WOTC and the EZ Wage Credit.

The Cleveland EZ, through an innovative new program called Start-up and Existing Entrepreneur Development (SEED), is now assisting companies like this one. The SEED program offers intensive, fast-paced business counseling services and classroom instruction in dozens of subject areas, including tax incentives. This program is offered to EZ businesses and residents in collaboration with American Express Tax and Business Services, Cuyahoga Community College, and Shorebank Cleveland.

For more information on these successful uses of WOTC and the EZ Wage Credit, please call James DeRosa, acting director of the Cleveland Empowerment Zone at (216) 664–2804.



Work Opportunity Tax Credit and Enterprise Zone Facility Bond Funding Boost Business in Cumberland County Empowerment Zone

The multijurisdictional Cumberland County EZ is located in New Jersey. The Bridgeton, Millville, Port Norris, Vineland, and Cumberland County governments applied together for 1 of 15 Round II EZ designations. After receiving its designation, the Cumberland County EZ identified a number of social and economic priorities in the area, including creating new jobs, expanding economic opportunity, enhancing the area's transportation system, and reducing welfare dependency.

To address these challenges, the Cumberland Empowerment Zone Corporation (CEZC) successfully established partnerships with several organizations to increase the use of the valuable Federal EZ tax incentives, including WOTC and Enterprise Zone Facility Bonds.

CEZC entered a partnership with the Workforce Investment Agency (WIA) in the early stages of applying for its EZ designation. (WIA is the county's designated employment and training agency.) CEZC requires businesses that receive EZ funding to use WIA as their first source for hiring. WIA thus provides a valuable service to EZ businesses and also emphasizes job placement for qualified EZ residents. Businesses do have the flexibility to hire other qualified candidates for vacant positions.

Work Opportunity Tax Credit. WIA is responsible for completing certifications for WOTC and the Welfare to Work credit (WtW Credit). CEZC, WIA, and a convenience store company recently worked together to create a successful program using WOTC to hire summer youth from the EZ. WIA screens potential employees and certifies the youth as being members of a WOTC-targeted group. The company has several convenience stores near tourist areas along the Jersey Shore that need increased staff for the summer months. The company does not put youth on the payroll for training before May 1 because the tax incentive is available only if the youth work between May 1 and September 15.

This group of partners identified transportation as a barrier to getting jobs for residents. To help overcome this barrier, CEZC, WIA, and the convenience store company established a bus system to transport youth from different areas to their jobs. The three partners determined they could share the transportation costs. From 1999 through 2001, 118 employees certified for WOTC worked for the convenience store company, which exceeded the company's expectations.

Enterprise Zone Facility Bond Financing. CEZC developed a partnership with the New Jersey Economic Development Authority (EDA) to facilitate the issuance of tax-exempt bonds in the Cumberland County EZ. EDA is an active issuer of tax-exempt bonds within the State and had issued bonds over the past several decades for commercial and industrial projects similar to the types of projects that CEZC has been targeting. Knowledge about tax-exempt bond financing for projects in Federal EZs and

Enterprise Communities (ECs) is not as widespread as it could be among bond issuers and purchasers of tax-exempt bonds. CEZC evaluated possible issuers and concluded that EDA had both the type of experience and depth of resources, including specialized counsel and investment banking firm contacts, to make an Enterprise Zone Facility Bond transaction happen.

EDA began meeting with CEZC in January 2000. EDA participated in meetings with the business community, sponsored by CEZC, to make businesses aware of the bond financing technique.

CEZC and EDA entered into a memorandum of understanding (MOU) in July 2001 in anticipation of the first issuance of tax-exempt bonds for the Cumberland County EZ. The MOU outlined the procedure for referral and approval of bond issuance between the two entities as well as the services that EDA would perform. The MOU also outlined the services that CEZC would provide in monitoring compliance with the EZ Business criteria, particularly with respect to meeting the requirement that 35 percent of employees be residents of the EZ.

CEZC agreed to provide compliance training to any borrower of tax-exempt bonds used in the EZ and developed a compliance reporting agreement that would be executed by CEZC and a borrower. The reporting form is to be submitted annually by the borrower to CEZC and EDA. EDA and CEZC also reached an agreement on sharing the fees paid by the borrower to the EDA for the issuance of tax-exempt bonds and for EDA's services and obligations.

The first tax-exempt bond financing was closed in January 2002 for approximately $4.2 million. These bonds financed the construction of an ice skating facility used for ice hockey, family outings, and other recreational purposes. The ice rink will be a primary location for hockey tournaments, and CEZC expects that nearby hotels and restaurants will be indirect beneficiaries of the economic development project paid for with bond financing. WIA and CEZC are assisting the business in meeting its 35-percent resident employee requirement.

The Enterprise Zone Development Corporation of Vineland and Millville guarantees the repayment of a portion of the tax-exempt bonds. This commitment from the EZ helps to enhance the project. Its guarantee makes the transaction work from a cash flow standpoint and also illustrates the need to combine other incentives with tax incentives. The ice rink owner expects the tax-exempt bond financing rate to be at least 2 percent below that of a conventional loan, leading to substantial interest savings. The owner expects to save additional amounts by taking the EZ Wage Credit and WOTC for youth employees in their first year of employment.

For more information on these successful tax incentive transactions, please call Jerry Velazquez, executive director of the Cumberland Empowerment Zone Corporation at (856) 459–1700.



Marketing Tax Incentives and Using EZ Wage Credits and Enterprise Zone Facility Bonds Increase Success in the District of Columbia

Congress passed legislation in 1997 to create the District of Columbia Enterprise Zone (DC Zone), whose designation runs from January 1, 1998, through December 31, 2003. The DC Zone has many of the same tax incentives as EZs, including the EZ Wage Credit, WOTC, increased Section 179 expensing, and tax-exempt bond financing. In addition, the DC Zone has zero percent capital gains identical to the incentive permitted for Renewal Communities (RCs) under 2000 tax legislation.

Using Tax Professionals. Soon after the District received its Zone designation, the Greater Washington Society of Certified Public Accountants set up the DC Coalition for Utilizing Tax Reductions (DC-CUTR) to provide a forum for discussing how businesses could benefit from EZ tax incentives. DC-CUTR is a voluntary organization of accounting, association, business, government, and legal professionals and organizations. In October 1998 the Revenue and Enterprise Zone Bond Office (which is responsible for issuing tax-exempt bonds to benefit businesses) cosponsored a kickoff meeting on the tax incentives. Other sponsors included the District of Columbia Building Industry Association, the DC Chamber of Commerce, and the DC Marketing Center. A representative of DC-CUTR made a presentation on the impact of tax incentives for DC Zone businesses.

These groups have since sponsored similar conferences annually, with representatives of the accounting and legal communities making presentations. The 2001 conference included the owner of a small business that borrowed approximately $4.8 million in tax-exempt bonds to finance the rehabilitation of an office building. One accounting firm used its presentation on the benefits to businesses of the zero percent capital gains incentive for an article in the DC Building Industry Association's newsletter.

The District's Office of the Deputy Mayor for Planning and Economic Development surveyed local accounting firms to obtain information on how many businesses use the EZ Wage Credit. The survey found that approximately 30 firms claimed EZ Wage Credits totaling approximately $7.4 million between 1998 and 2001. The types of businesses claiming the credits included manufacturing, hotel, cleaning, sports, entertainment, and construction companies. This study provided valuable marketing information to the District government on the types of businesses that have been able to take advantage of the EZ Wage Credit.

Tax-Exempt Bond Financing. The District has successfully completed 10 financings using Enterprise Zone Facility Bonds in the aggregate amount of $83 million. These financings have supported a variety of new and existing businesses. Two DC Zone law firms used bond financing to provide tenant improvements. The District recently provided tax-exempt financing for a drugstore and a discount store in a revitalized neighborhood shopping area where a new subway stop recently opened. Both stores are parts of national chains.

Enterprise Zone Facility Bond financing was available to both the law firms and the national chain stores even though each of these businesses had locations outside the EZ. This is because tax-exempt bond rules permit businesses to allocate activities, income, and employees to Zone operations to help meet the EZ Business criteria.

The District has also used tax-exempt bond financing to make leasehold improvements at its new convention center and to finance office space for think tanks and nonprofit organizations.

Beneficiaries of tax-exempt bond financing are required to enter into a first-source employment agreement with the District's Department of Employment Services (DOES). Under this agreement, businesses agree to work with DOES to fill vacant job positions. From 1998 to 2001, these beneficiaries created approximately 6,000 jobs, and District residents filled approximately one-third of them. Although these businesses did receive some funding from other sources of tax-exempt financing, these numbers still illustrate how tax incentives are increasing employment opportunities for District residents.

For more information on Enterprise Zone Facility Bond financing transactions and on marketing EZ tax incentives, please call Gregory Johnson, DC Office of the Deputy Mayor for Planning and Economic Development, at (202) 727–6883.

Houston Uses Academy Bonds To Fortify a Public High School

Public schools located in Federal EZs and ECs can obtain interest-free loans when they apply partnerships to development efforts within public schools. (This Qualified Zone Academy Bond (QZAB) loan program is available in RCs also if at least 35 percent of the school's students are eligible for free or reduced-cost lunches.) In August 1999 the State of Texas approved $8 million in QZABs for the Houston Independent School District. The funds were used to make critical improvements to Jefferson Davis High School, located in Houston's Enhanced Enterprise Community.

For 20 years Jefferson Davis students shared a cafeteria and a library with students from Marshall Middle School, located across the street. The original concept for capital improvements to resolve this problem was to close the street, construct a park, and have a single academic center. The street was never closed and the park was never built. However, students continued to have difficulty crossing the busy thoroughfare. In addition, as enrollments for both schools increased, sharing facilities became unfeasible.

Through the use of the QZAB funds, a 60,000-square-foot two-story addition was added to Jefferson Davis High. The cafeteria is located on the first floor and the library is located on the second floor along with attendance offices and several classrooms. The library includes a teleconferencing room, a television production lab, and two computer rooms.

The QZAB program requires another party to provide funds or other resources to match at least 10 percent of the development costs. In this case, Project GRAD of Houston provided $1.5 million in matching resources. Project GRAD has worked with Jefferson Davis High and its feeder elementary and middle schools for approximately 10 years. Project GRAD is a scholarship program that guarantees a 4-year scholarship to every Jefferson Davis graduate who meets the program's academic and participation requirements.

For more information on Houston's successful development using QZABs, please call Judy Butler, director of the Houston Enhanced Enterprise Community at (713) 247–2666.

Enterprise Zone Facility Bonds and Work Opportunity Tax Credits Revitalize Huntington/ Ironton Empowerment Zone

The Huntington, West Virginia/Ironton, Ohio EZ is one of several that spans two States. Many EZs cover more than one local governmental jurisdiction, but EZs that must deal with two different State governments to make tax incentives work may encounter unique challenges.

Enterprise Zone Facility Bonds. The governance board of the Huntington/Ironton EZ (Corporation) decided at the beginning of EZ designation to take advantage of tax-exempt bond financing and the allocation of the $130 million in volume cap for Enterprise Zone Facility Bonds. The Corporation had been contacted about a possible bond issuance for a project; the company that was interested in the bond transaction was expected to request that a sizable portion of the volume cap be available for the entire EZ designation period. Federal tax rules do not place any limits on the amount of the volume cap allocated to any one project and do not specify annual allocation limits. Tax rules do require that the local jurisdiction provide certification to the bond financing allocation.

After discussion, the Corporation's board adopted a resolution on June 1, 1999, to provide guidance for allocation of the bond volume cap. The resolution specified two issuers of the bonds, one for each local jurisdiction: the Huntington Municipal Development Authority and the Lawrence Economic Development Corporation. The resolution further stated that the board would review applications for bond financing, but no bonds could be issued without the prior approval of the Corporation board. No single project could receive more than $25 million in allocation without a two-thirds vote of the board.

The Huntington/Ironton EZ held two half-day informational meetings in 1999, one in each State. These informational meetings and similar followup meetings were used to publicize tax-exempt bonds and the procedural steps for issuing them.

In January 2002, the governance board adopted a resolution supporting the issuance of approximately $10 million in tax-exempt bonds to finance a portion of the costs of an urban town center, a mixed-use development consisting of integrated retail, entertainment, office, and residential use that would be easily accessible to residents of both Huntington and Ironton.

Project participants met with Corporation staff to discuss how to structure an entity that could meet the definition of an EZ Business and to identify users of the retail project that could make use of tax-exempt bond financing for leasehold improvements and equipment. The staff also provided information to the project developers on the EZ Wage Credit, which could be of significant interest to other companies interested in leasing space in the project.

This bond transaction is the first issuance under the resolution and is a good example of how planning and coordination can facilitate issuance of bonds and avoid some potential political problems.

Work Opportunity Tax Credit. The Corporation was able to attract the customer service distribution operations of a national Internet sales company. The company was attracted to the area because of the availability of college students who could work on a part-time basis and the general lower cost of doing business in the area. The company's business model involves leasing space and equipment instead of purchasing a facility and making a large capital investment in equipment purchases. However, the leasehold improvement and equipment costs were not large enough to use tax-exempt bond financing. The operation in Huntington is part of a larger nationwide company with substantial activities outside of the EZ, so the company did not qualify for the increased Section 179 expensing incentive.

The EZ staff focused on wage credits to attract the company, particularly WOTC, because the 18- to 24-year-old age range fit with the age range of a substantial number of the employees the company expected to hire. The EZ Wage Credit was not yet available in the Huntington-Ironton EZ at the time the company moved into the EZ.

WOTC also played a part in attracting the company. The EZ provided a cash grant to the company on the condition that it meet specified hiring targets and pay wages at certain levels. West Virginia provided funding to a local university to enhance its business program to include Web-based training for its graduates, and the company had input into the course curriculum.

For more information on these successful tax incentive transactions, please call Cathy Burns, executive director of the Huntington/Ironton Empowerment Zone at (304) 399–5454.

Eastern Kentucky Renewal Community Helps Residents With Combination of Credits

The Eastern Kentucky Renewal Community (EKRC) includes four southeastern Kentucky counties in the heart of Appalachia. Since receiving its designation at the end of 2001, EKRC has been excited about helping local businesses take advantage of RC tax credits and deductions. EKRC also wanted to focus efforts on empowering local residents and made a commitment at the start of its designation to help residents become self-sufficient, employed, and proud of themselves.

Beginning in early 2002 EKRC partnered with the Kentucky Department for Community Based Services (DCBS) to inform residents about the RC Wage Credit, WOTC, and the WtW Credit. As part of this outreach effort, EKRC created a brochure titled *How Residents Can Use the Renewal Community Tax Credits to Get a Job in the Eastern Kentucky Renewal Community.* DCBS distributes this brochure to job-seeking local residents. The Owsley County Action Team (OCAT) also works with local residents to explain how the employment credit benefits local employers. OCAT helps residents determine if they are eligible for the WOTC and WtW Credit programs. OCAT staff give qualified residents the forms that employers need to gain the tax credits and guide clients in completing the forms correctly. OCAT advises the clients to attach these forms to all job applications. EKRC staff also advise clients to notify prospective employers within the four-county area of their RC residency and to remind employers of the valuable tax benefits available for hiring them.

Additionally, EKRC assists RC residents who travel outside the RC to find jobs by giving copies of its marketing brochure to these individuals and reminding them that employers located outside the RC can claim WOTC and the WtW Credit if the employee meets certain eligibility criteria.

This marketing method has proven successful for local residents. EKRC has found that the more residents know about the RC incentives, the better their chances of getting jobs. In addition, residents who have this information while looking for jobs seem to be more confident. EKRC's marketing efforts also are reduced when residents apply their energies to promoting themselves.

For more information on these successful tax incentive efforts in the Eastern Kentucky Renewal Community, please call Susan Ramos, director of the Owsley County Industrial Authority at (606) 593–7296.

Marketing Efforts and EZ Wage Credit Make Dollars and Sense in Rural Kentucky

The Kentucky Highlands Empowerment Zone (KHEZ) was one of three original rural zones designated by the U.S. Department of Agriculture in December 1994. The lead entity for KHEZ is Kentucky Highlands Investment Corporation (KHIC), a nonprofit community development corporation that has been actively involved in economic development in the region for 34 years. KHIC has historically provided development assistance through equity investments and debt financing for new and emerging businesses in southeast Kentucky. The EZ program marked an expansion of the KHIC mission into community development, which is now an integral part of its other programs.

From the outset, KHEZ's primary focus has been job creation. To support this effort, it used $15 million of the $40 million EZ award to capitalize revolving loan funds for business and agriculture. In addition, KHEZ made a concentrated effort to promote the EZ Wage Credit and the increased Section 179 expensing benefits that came with EZ designation. These efforts have been successful as total employment in the KHEZ counties has grown by 5,635 jobs or 36.7 percent since designation. In comparison, total employment in the Commonwealth of Kentucky has grown by 9.9 percent for the same period.

Marketing EZ Tax Incentives. In 1995, the first year of EZ designation, KHEZ sponsored well-attended seminars to promote the tax benefits in each of the three zone counties. Presenters included representatives from the IRS, the Kentucky Revenue Cabinet, and private-sector certified public accountants.

When its designation was extended through December 2009, KHEZ felt it was important to bring businesses and tax practitioners up to date on the enhanced EZ benefits and changes in tax law. In January 2002, as the law took effect, KHEZ sponsored a workshop on the advantages for EZ businesses, which it promoted with a series of radio and newspaper advertisements. A nationally recognized tax attorney and accountant provided valuable technical information at the workshop, which overflowed with attendees. The audience included most of the accountants in the region because KHEZ had arranged for them to receive continuing education credits for the half-day seminar.

Empowerment Zone Employment Credits. The EZ Wage Credit and increased Section 179 expensing are key components of KHEZ's success in creating job opportunities for residents. One locally owned company with several hundred employees has been able to take approximately $1 million annually in wage credits since designation and will have more than $3.2 million in tax credits to carry forward. As a result, this company has invested more than $8 million in its plant and equipment during the period and created more than 300 new jobs. On a smaller but no less important scale, the employment credits have meant more than $50,000 to a small local restaurant. As a result, owners have been able to improve the employee benefit package.

Gauging the impact of the tax credits and expensing provisions available to EZs can be difficult. However, KHIC is a major lender in the zone with more than $19 million in bond financing. It thus has the opportunity to review borrowers' tax returns as part of the loan monitoring process. KHIC's analyses of these returns, along with the EZ job creation statistics, confirm the significant value of the tax benefits to business in the EZ.

For more information on these successful tax incentive transactions, please call Michael Hayes, executive director of the Kentucky Highlands Empowerment Zone at (606) 864–5175 or send an e-mail to mhayes@khic.org.

Louisiana Veterinarian Applies Multiple Renewal Community Incentives for Maximum Savings

The Sullivan Veterinary Clinic, which provides services for both small and large animals, is located in the Northern Louisiana RC in the town of Winnsboro. Dr. Chris Sullivan owns the clinic as a sole proprietorship and he wasted no time in taking advantage of the tax incentives and other savings available to RC Businesses.

In May 2002 Dr. Sullivan paid his accountant to travel to Washington, D.C., to attend HUD's Community Renewal Implementation conference. At this conference, the accountant had access to plenary sessions on the tax incentives themselves, on Federal resources, and on innovative tax incentives marketing techniques. The heavily attended conference also featured breakout sessions on performance measurement and tax incentives utilization.

Earlier this year, Dr. Sullivan built a new clinic and applied for a substantial portion of the RC commercial revitalization expenditure that could yield thousands in savings to his business. In addition, Dr. Sullivan divided the deductions for his equipment purchases between 2002 and 2003 to take full advantage of increased Section 179 expensing. He is also aware that his clinic qualifies as an RC Business because his business activity is focused within the RC. The assets that he purchased in 2002 for his clinic include a building, land, and equipment. He plans to hold these assets for at least 5 years before selling them. Dr. Sullivan will thus avoid capital gains and be able to apply the profits to his long-awaited retirement.

Dr. Sullivan also receives a $1,500 RC Wage Credit every year for each of his seven original employees, since they all live in the RC, and with his tax savings, he recently hired four new employees. He selected 18- to 24-year-old individuals who live in the RC. Dr. Sullivan thus is eligible to claim up to $2,400 in WOTC for each new employee.

For more information on this successful tax incentive application in the Northern Louisiana Renewal Community, please call Tana Trichel, president and chief executive officer of the Macon Ridge Economic Development Region at (318) 757–3033.

Combining Federal, State, and Local Tax Incentives Means Good Business in Los Angeles Empowerment Zone

HUD granted full EZ status to the Los Angeles Supplemental EZ in 1997, with the tax incentives becoming available January 1, 2000.

This EZ is maximizing its use of Federal tax incentives by marketing them as a package with State tax incentives and local business incentives. The EZ staff also worked with a local consulting firm to develop a marketing brochure that illustrates how much businesses can save by using different combinations of tax incentives. Two examples in the marketing brochure include a small bakery and a large manufacturing business.

The following promotional material and scenario on using tax incentives appear in the marketing brochure. The example focuses on how a manufacturing firm can use the incentives.

Help Lower Your Costs of Doing Business This Tax Year

The Los Angeles Federal Empowerment Zone	
• A generous Employer Wage Credit	• EZ/EC Bonds
• Additional Section 179 Expensing	• Waiver of City Business Tax

City of Los Angeles State Enterprise Zone tax credits and incentives	
• Employee Hiring Tax Credits	• Business Expense Deduction
• Sales & Use Tax Credit	• Net Interest Deduction
• Net operating loss carry-forward	• DWP 5-year electrical discount
• Double dipping on the MIC & sales-and-use tax credit	

A company designs and fabricates precision aerospace machine parts. On January 1, 2000, the business relocates from Glendale to the Los Angeles State Enterprise Zone and Federal Empowerment Zone. Relocation is to a larger, 180,000 sq. ft. building, which will allow the company to add 40 new hires to its current workforce of 190. As a result of its move, the company anticipates increasing its sales from $4 million to $13 million over the next five years.

During the year, the business buys new machinery and parts, including telecommunication equipment and computers, totaling $1.2 million.

Thirty-five of the anticipated new employees are TEA eligible, i.e. eligible under the California State Enterprise Zone Targeted Employment Area, and 20 of the new employees reside in the Los Angeles Federal Empowerment Zone.

The current workforce has 33 employees who are TEA eligible and were hired on January 1, 1999. Twenty current employees live in the EZ. Net income at the end of the year is $2 million. All employees earn $10.00 per hour.

Tax Analysis Assumptions

- Of the 190 current employees, 53 were hired on January 1, 1999 and 40 on January 1, 2000
- Employees worked 2,080 hours in 1999 and 2000
- Aerospace company is doing business as a "C" corporation
- 8.25 percent sales tax paid on new machinery
- Business qualifies as an "enterprise zone" business for purposes of the federal Increased Section 179 expensing
- Company will have $2 million of net income for the Year 2000

Tax Liability (Before Tax Incentives)

Taxable Income = $2,000,000
Federal Tax Liability (before tax credits) = $680,000 (@ 34 percent of $2,000,000)
California Tax Liability (before tax credits = $176,800 (@ 8.84 percent of $2,000,000)

I. Tax Incentives Calculations

Scenario A

53 current employees were hired on January 1, 1999. 33 are qualified under the TEA and 20 reside in the Federal EZ.

Federal EZ Wage Credit = $60,000
($60,000 = 20 qualified employees x $15,000 maximum qualified wages x 20 percent applicable credit)

Federal Increased Section 179 Deduction = $40,000 (based on purchase of $1.2 M of machinery)

California Enterprise Zone Hiring Credit = $236,808
($236,808 = 33 qualified employees x $17,940 qualified wages (2080 hours x $8.625 max.) x 40 percent applicable credit)

Scenario B

Of the 40 new hires on January 1, 2000, 20 reside in the Los Angeles EZ and 35 are TEA eligible.

Federal EZ Wage Credit = $120,000, for qualified employees hired 1/1/99 and 1/1/00
($120,000 = 40 qualified employees x $15,000 maximum qualified wages x 20 percent applicable credit)

Federal Increased Section 179 Deduction = $40,000 (based on purchase of $1.2 M of machinery)

California Enterprise Zone Hiring Credit = $550,758, calculated as follows:

(For qualified employees hired January 1, 1999, $236,808 = 33 qualified employees x $17,940 qualified wages (2080 x 8.625 max.) x 40 percent applicable credit)

(For qualified employees hired January 1, 2000, $313,950 = 35 qualified employees x $17,940 qualified wages (2080 x 8.625 max.) x 50 percent applicable credit)

California Enterprise Zone Sales and Use Tax Credit = $99,000
($99,000 = 8.25 percent x $1.2 million (cost of new machinery and parts))

California Manufacturer' Investment Credit (MIC) = $69,600
($69,600 = 6 percent x ($1,200,000 – $40,000) (non qualified MIC cost due to Increased Section 179 expensing)

II. Tax Liability (After Tax Incentives)

Scenario A

Federal

Taxable Income =	$2,000,000
Fed. Increased Section 179 Deduction =	(40,000)
Fed. Taxable Income =	$1,960,000

Fed. Tax Liability =	$666,400 (@ 34 percent)
Less: Fed. Tax Credits =	60,000
Fed. Tax Liability =	$606,400 Federal Tax Credit Carry-forward: $0

California

Taxable Income =	$2,000.000
CA Taxable Income =	$2,000,000
CA Tax Liability =	$176,800 (@ 8.84 percent)
Less: CA Tax Credits =	($176,800)
CA Tax Liability =	$ 800

(*Tax Credit cannot reduce the minimum Franchise Tax of $800.)

Scenario B

Federal

Taxable Income =	$2,000,000
Fed. Increased Section 179 Deduction =	(40,000)
Fed. Taxable Income	$1,960.000

Fed. Tax Liability =	$666,400 (@ 34 percent)
Less: Fed. Tax Credits =	120,000
Fed. Tax Liability =	$546,400 Federal Tax Credit Carry-forward: $0

California

Taxable Income =	$2,000.000
CA Taxable Income =	$2,000,000
CA Tax Liability =	$176,800 (@ 8.84 percent)
Less: CA Tax Credits =	(176,800)
CA Tax Liability =	$800

(*Tax Credit cannot reduce the minimum Franchise Tax of $800.)

Savings

Federal taxes reduced by **$73,600,** OR **11 percent** (Scenario A)

Federal taxes reduced by **$133,600,** OR **20 percent** (Scenario B)

State taxes reduced by **$176,000,** OR **99 percent** (Scenarios A and B)

Other Benefits

DWP 5-Year Electrical Discount – 35 percent First Year = $132,000.00 Reduction
City Business Tax Liability: No business tax for 5 years; pay $25 yearly for 5 years.

Information on Federal, State, and local incentives is available on the Web site for the Los Angeles EZ (www.cityofla.org/cdd/business), which has seen an increase in the number of hits since the Federal tax incentives became available. (State hiring credits, sales and use tax credits, and manufacturing investment credits were enacted as part of a State enterprise zone program before the EZ received the Federal incentives.)

The examples in the marketing materials are fictitious but the EZ has many examples of actual use of the incentives. The EZ bond program, for example, has already created 280 jobs and retained 171 more with just three projects:

- AAA Packing and Shipping.
- MEGA Toys, Inc.
- Wing Hing Noodle.

Many of those jobs are well-paying, skilled positions with full benefits. Since the bonds are purchased by private investors and backed by letters of credit from commercial banks, no city or grant funds were risked or expended to achieve the results.

These projects were funded when Los Angeles had to compete with other municipalities in the State for bond allocations and individual projects were limited to about $3 million in funding. Under the terms of the Federal Community Renewal Tax Relief Act of 2000, the city has received its own allocation of bond funds worth $230 million to be used over 8 years for manufacturing, office, retail, and other types of projects. The city already has four potential EZ bond projects in progress that are worth more than $30 million. Each project will be required to fill a minimum of 36 percent of available jobs with EZ residents.

For more information on these successful tax incentive transactions, please call Robert Perez, program coordinator for the Los Angeles Empowerment Zone at (213) 485–8161.

Maximizing Use of Enterprise Zone Facility Bonds Results in Convention Center/Hotel in St. Louis/East St. Louis Empowerment Zone

The St. Louis/East St. Louis EZ is a multijurisdictional urban EZ designated as a HUD Round II EZ in 1998. The EZ has up to $130 million in volume cap for Enterprise Zone Facility Bonds over the designation period.

The regional EZ board worked for several years with city and State officials, investors, underwriters, and developers to bring a major project to the EZ. In December 2000 the St. Louis Industrial Development Authority issued $95 million in tax-exempt Enterprise Zone Facility Bonds—the largest Enterprise Zone Facility Bond transaction in the Nation—to finance a portion of the costs of a $266 million convention center hotel project.

The Authority also issued a $3 million tax-exempt enterprise community bond to finance a portion of the project. These bonds were part of an overall financing package that also included taxable loans, contributions from the hotel owners, grants, and subordinated loans from the city of St. Louis. The package also included the sale of State brownfield remediation and historic rehabilitation tax credits. The hotel is the centerpiece of a large economic development project.

For more information on this successful tax incentive transaction, please call Michael Jones, executive director of the Greater St. Louis Regional Empowerment Zone at (314) 241–0002.

A Prescription for Economic Prosperity in Renewal Communities and Empowerment Zones

Community Renewal Tax Relief Incentives

HUD WorkPad Instructions

The $22 billion package of Tax Incentives for businesses is a key benefit of the Renewal Community and Empowerment Zone designations. HUD developed these workpads to help RC/EZ businesses claim their part of this package. The workpads can serve as any of the following resources for your RC/EZ community.

(1) A quick and easy first step in determining whether a business is eligible for one or more of the available tax incentives and the related tax savings;
(2) A teaching and marketing tool for EZs and RCs that allows them to calculate the potential financial benefits that an EZ/RC business would receive in fully utilizing the available tax incentives, and
(3) A potential tool for data gathering and tracking that an EZ/RC designee can use to evaluate the extent that their business community is taking advantage of the tax incentives.

The Workpads are divided into two parts. First, we have provided descriptions of several tax incentives and eligibility requirements and formulas for calculating estimated tax savings. We have also provided examples to show how the tax incentive applies.

Second, we have created a "Fast Formulas" Workpad. This Workpad allows those already generally familiar with the tax incentives to conduct their tax savings calculations on one page.

Importantly, the formulas contained in these Workpads result only in estimated tax savings and should not be officially relied upon for Federal government tax purposes. Please consult your tax preparer or the IRS for official guidance and note the disclaimer on the Workpads.

The formulas contained in the workpad result only in estimated tax savings and should not be officially relied upon for Federal government tax purposes. Please consult your tax preparer or the IRS for official guidance.

Community Renewal Tax Relief Incentives – HUD WorkPad

If you are in a RENEWAL COMMUNITY (RC) then the following tax incentives apply:

Renewal Community Employment Credit (RC Wage Credit)

WorkPad for a Business Located in the Renewal Community

Description: Credit against Federal taxes up to $1,500 for each year of RC designation for every existing employee and new hire who lives and works in the RC. The credit is available beginning January 1, 2002 through December 31, 2009.

- The wage credit is 15 percent of wages up to the $10,000 wage amount.
- No limit on number of employees taking the credit

Note: Cannot count same wages for both the WOTC and WtW credits and the RC Wage Credit.

Applicable IRS Tax Form: Form 8844

Applicable IRS Publication: Publication 954

Example 1: Bob hires 4 employees who live and work in the RC and pays each of them $12,000. Bob's RC Wage Tax Credit would be: 4 x $10,000 x .15 = $6,000.

Example 2: Joe hires 6 employees who live and work in the RC, paying three of them $15,000 and three of them $8,000. Joe's RC Wage Tax Credit would be: ((3 x $10,000) + (3 x $8,000)) x .15 = $8,100.

Formula

______	x	______	x	**.15**	=	______
Number of RC employees		Wage (*up to $10,000*)		RC Credit Rate		Wage Credit

The formulas contained in the workpad result only in estimated tax savings and should not be officially relied upon for Federal government tax purposes. Please consult your tax preparer or the IRS for official guidance.

Zero Percent Capital Gains Rate for Renewal Community Assets

WorkPad for a Business Looking to Sell a Building or to Sell New Stock or Capital Interests in Its Corporation or Partnership in the Renewal Community

Description: Excludes from gross income any capital gain from the sale or exchange of a qualified District of Columbia Zone or RC asset, if held for more than 5 years.

Qualifying assets include:

- stock in a domestic corporation acquired by the taxpayer at its original issue from the corporation solely in exchange for cash and the corporation was a DC Zone or RC business at the time the stock was issued and the corporation qualified as a DC Zone or RC business during substantially all of the taxpayer's holding period for the stock;
- any capital or profits interest in a domestic partnership if the interest was acquired by the taxpayer from the partnership solely in exchange for cash and the partnership was a DC Zone or RC business at the time the interest was acquired and the partnership qualified as a DC Zone or RC business during substantially all of the taxpayer's holding period for the partnership interest; and
- tangible business property acquired by the taxpayer by purchase and the taxpayer is the first person to use the property in the DC Zone or RC and substantially all of the use of the property was in the taxpayer's DC Zone or RC Business.

Note: In order to qualify, the DC Zone asset must be acquired between January 1, 1998 and December 31, 2003. The RC asset must be acquired between January 1, 2002 and December 31, 2009. Gain excluded is limited to capital gain on a DC Asset between January 1, 1998 and December 31, 2008 and on an RC Asset between January 1, 2002 and December 31, 2014.

Applicable IRS Publication: Publication 954

Example: Rachael acquires an abandoned building in the RC and does a total rehabilitation of the building suitable for light manufacturing. Total costs of acquisition and rehabilitation are $750,000. The building is leased to a business that is a Renewal Community business for Federal tax purposes. After owning the building for six years, Rachael decides to sell to the lessee for a sales price of $1,250,000. After taking into account depreciation over the period of ownership, Rachael has $250,000 in gain from appreciation in the building. Without the tax incentive which permits a zero percent rate for gain, Rachael would have to pay taxes on the gain at a rate of 20%. Rachael will have a savings equal to $250,000 x .20 = $50,000.

Formula

______	x	.20	=	______
Amount of Gain from Appreciation		Federal Tax Rate		Amount of Taxes Saved

The formulas contained in the workpad result only in estimated tax savings and should not be officially relied upon for Federal government tax purposes. Please consult your tax preparer or the IRS for official guidance.

HUD WorkPad – Renewal Community Continued

WOTC (Work Opportunity Tax Credit)

WorkPad for a Business Located Inside or Outside of the Renewal Community

Description: Credit against Federal taxes up to $2,400 for each new hire from a targeted group.* The credit expires for individuals who begin work after December 31, 2003, although the credit may be extended.

Note: Cannot be combined with the WtW credit.

Applicable IRS Tax Forms: Forms 5884 and 8850

*Targeted groups include:

- Veterans,
- Ex-felons,
- Vocational rehabilitation referrals,
- Food stamp recipients,
- TANF recipients,
- High-risk youth (ages 18 to 24 who live in an EZ, EC or RC),
- Summer youth employee (16 to 17 who live in an EZ, EC or RC), and
- SSI recipients.

Example 1: Bob hires a cashier who is 20 years old and lives in an RC. At $6 an hour for a 35-hour week, with one week paid vacation, for a total annual wage of $10,920. Bob's WOTC Credit would be: 1 x $6,000 x .40 = $2,400.

Example 2: Joe hires 6 employees from the designated groups, three of them for year-round jobs at an annual wage of $15,000. The three others are 16-year olds who live in the RC for 8-week summer jobs and receive total wages of $2,000. Joe's WOTC Credit would be: (3 x $6,000 x .40) + (3 x $2,000 x .40) = $9,600.

Formula

____	x	____	x	.40	=	____
Number of WOTC employees *working at least 400 hours*		Wage, up to $6,000		Credit Rate		WOTC Wage Credit
____	x	____	x	.25	=	____
Number of WOTC employees *working at least 120 hours*		Wage, up to $6,000		Credit Rate		WOTC Wage Credit

The formulas contained in the workpad result only in estimated tax savings and should not be officially relied upon for Federal government tax purposes. Please consult your tax preparer or the IRS for official guidance.

Increased Section 179 Deduction

WorkPad for Purchasing New Equipment

Description: Allows an increased section 179 deduction up to $35,000 on purchases of certain depreciable property, such as equipment and machinery.

Note: Only applicable in EZs and RCs (cannot be used in ECs). The RC Asset must be acquired by the taxpayer by purchase between January 1, 2002 and December 31, 2009.

Applicable IRS Tax Form: Form 4562

Applicable IRS Publication: Publication 946

Example: Leslie runs a wholesale florist operation in an RC. She purchases refrigeration equipment, work tables, a cash register, a delivery van and desk for a total of $65,000. Without the RC tax incentive she could only expense (take an immediate deduction) for $24,000 and she would have to depreciate the remaining $41,000 over the time period assigned by the Federal tax rules. With the RC tax incentive, she will be able to take an additional immediate deduction of $35,000, bringing her total deduction for the year to $59,000 and only $6,000 will have to be depreciated over time. That additional $35,000 in deductions will reduce the amount of taxes she pays that year. If she is paying taxes at a 35% rate, the savings would be equal to: $35,000 x .35 = $12,250.

Formula

______	x	**.35**	=	______
Cost of Qualified Equipment *up to $35,000*		Assumed Federal Tax Rate		Amount of Taxes Saved

The formulas contained in the workpad result only in estimated tax savings and should not be officially relied upon for Federal government tax purposes. Please consult your tax preparer or the IRS for official guidance.

Commercial Revitalization Deduction

WorkPad for a Business Planning to Construct, Expand, or Acquire and Renovate a Building in the Renewal Community

Description: Deduction of either all qualified costs (up to $10 million per project) equally over 120 months or deduction of one-half of qualified costs (up to $10 million per project) in the first year a building is placed in service (with depreciation of the remaining amounts over the standard 39 years).

Note: Available for buildings placed in service after December 31, 2001 and before January 1, 2010 that receive an allocation of the deduction from the state.

Applicable IRS Tax Form: Form 4562

Applicable IRS Publication: Publication 946

Example: Acme Corporation places in service a $10 million project in 2002 in State A and State A has allocated $10 million of commercial revitalization deductions to this project in 2002.

- Without the incentive, the $10 million would be depreciated over 39 years (or roughly $256,400 per year).
- With the 120 Month Depreciation Option, the $10 million would be depreciated in 10 years (or $1 million per year).
- With the 1/2 Expensing, 1/2 Depreciation Option, $5,000,000 would be depreciated in the first year and the remaining $5,000,000 would be depreciated over the standard 39 years (or roughly $128,000 per year).

Formula

Without the incentive:

________	÷	39	=	________
Total Cost of Project		Period of Depreciation		Per Year Deduction

With the 120 Month Depreciation Option:

________	÷	10	=	________
Total Cost of Project		Period of Depreciation		Per Year Deduction

With the ½ Expensing, ½ Depreciation Option:

________	÷	2	=	________
Total Cost of Project		Period of Depreciation		First Year Deduction
________	÷	39	=	________
1/2 Cost of Project		Period of Depreciation		Per Year Deduction for Remaining Costs

The formulas contained in the workpad result only in estimated tax savings and should not be officially relied upon for Federal government tax purposes. Please consult your tax preparer or the IRS for official guidance.

If you are in an EMPOWERMENT ZONE (EZ) then the following tax incentives apply:

EZ Wage Credit

WorkPad for a Business Located in the Zone

Description: Credit against Federal taxes up to $3,000 for each year of EZ designation for every existing employee and new hire who lives and works in the EZ. The credit is available beginning January 1, 2002 through December 31, 2009.

- A wage credit of up to $3,000 for every employee that lives and works in the EZ.
- No limit on the number of employees.

Note: Cannot count same wages for the WOTC and WTW credits and the EZ Wage Credit.

Applicable IRS Tax Form: Form 8844

Applicable IRS Publication: Publication 954

Example 1: Bob hires 2 employees who live and work in the EZ and pays each of them $17,000. Bob's EZ Wage Tax Credit would be:
2 x $15,000 x .20 = $6,000.

Example 2: Joe hires 6 employees who live and work in the EZ, paying three of them $17,000 and three of them $10,000. Joe's EZ Wage Tax Credit would be: ((3 x $15,000) + (3 x $10,000)) x .20 = $15,000.

Formula

______	x	______	x	.20	=	______
Number of EZ employees		Wage (*up to $15,000*)		EZ Credit Rate		Wage Credit

The formulas contained in the workpad result only in estimated tax savings and should not be officially relied upon for Federal government tax purposes. Please consult your tax preparer or the IRS for official guidance.

Increased Section 179 Deduction

WorkPad for Purchasing New Equipment

Description: Allows an increased section 179 deduction up to $35,000 on purchases of certain depreciable property, such as equipment and machinery.

Note: Only applicable in EZs and RCs (cannot be used in ECs). The RC Asset must be acquired by the taxpayer by purchase between January 1, 2002 and December 31, 2009.

Applicable IRS Tax Form: Form 4562

Applicable IRS Publication: Publication 946.

Example: Leslie runs wholesale florist operation in an EZ. She purchases refrigeration equipment, work tables, a cash register, delivery van and desk for a total of $65,000. Without the EZ tax incentive she could only expense (take an immediate deduction) for $24,000 and she would have to depreciate the remaining $41,000 over the time period assigned by the Federal tax rules. With the EZ tax incentive, she will be able to take an additional immediate deduction of $35,000, bringing her total deduction for the year to $59,000 and only $6,000 will have to be depreciated over time. That additional $35,000 in deductions will reduce the amount of taxes she pays that year. If she is paying taxes at a 35% rate, the savings would be equal to: $35,000 x .35 = $12,250.

Formula

______	x	**.35**	=	______
Cost of Qualified Equipment *up to $35,000*		Assumed Federal Tax Rate		Amount of Taxes Saved

The formulas contained in the workpad result only in estimated tax savings and should not be officially relied upon for Federal government tax purposes. Please consult your tax preparer or the IRS for official guidance.

Zero Percent Capital Gains Rate for District of Columbia Enterprise Zone Assets

WorkPad for a Business Looking to Sell a Building or to Sell New Stock or Capital Interests in Its Corporation or Partnership in the District of Columbia

Description: Excludes from gross income any capital gain from the sale or exchange of a qualified DC Zone or RC asset, if held for more than 5 years.

Qualifying assets include:

- stock in a domestic corporation acquired by the taxpayer at its original issue from the corporation solely in exchange for cash and the corporation was a DC Zone or RC business at the time the stock was issued and the corporation qualified as a DC Zone or RC business during substantially all of the taxpayer's holding period for the stock;
- any capital or profits interest in a domestic partnership if the interest was acquired by the taxpayer from the partnership solely in exchange for cash and the partnership was a DC Zone or RC business at the time the interest was acquired and the partnership qualified as a DC Zone or RC business during substantially all of the taxpayer's holding period for the partnership interest; and
- tangible business property acquired by the taxpayer by purchase and the taxpayer is the first person to use the property in the DC Zone or RC and substantially all of the use of the property was in the taxpayer's DC Zone or RC business.

Note: In order to qualify, the DC Zone asset must be acquired between January 1, 1998 and December 31, 2003. The RC asset must be acquired between January 1, 2002 and December 31, 2009. Gain excluded is limited to capital gain on a DC Asset between January 1, 1998 and December 31, 2008 and on an RC Asset between January 1, 2002 and December 31, 2014.

Applicable IRS Publication: Publication 954

Example: Rachael purchases an abandoned building in the RC and does a total rehabilitation of the building suitable for light manufacturing. Total costs of acquisition and rehabilitation are $750,000. The building is leased to a business that is a Renewal Community business for Federal tax purposes. After owning the building for six years, Rachael decides to sell to the lessee for a sales price of $1,250,000. After taking into account depreciation over the period of ownership, Rachael has $250,000 in gain from appreciation in the building. Without the tax incentive which permits a zero percent rate for gain, Rachael would have to pay taxes on the gain at a rate of 20%. Rachael will have a savings equal to $250,000 x .20 = $50,000.

Formula

________	x	**.20**	=	________
Amount of Gain from Appreciation		Federal Tax Rate		Amount of Taxes Saved

The formulas contained in the workpad result only in estimated tax savings and should not be officially relied upon for Federal government tax purposes. Please consult your tax preparer or the IRS for official guidance.

WOTC (Work Opportunity Tax Credit)

WorkPad for a Business Located Inside or Outside of the Zone

Description: Credit against Federal taxes up to $2,400 for each new hire from a targeted group.* The credit expires for individuals who begin work after December 31, 2003, although the credit may be extended.

Note: Cannot be combined with the WtW credit.

Applicable IRS Tax Forms: Forms 5884 and 8850

*Targeted groups include:

- Veterans,
- Ex-felons,
- Vocational rehabilitation referrals,
- Food stamp recipients,
- TANF recipients,
- High-risk youth (ages 18 to 24 who live in an EZ, EC, or RC),
- Summer youth employee (ages 16 to 17 who live in an EZ, EC, or RC), and
- SSI recipients.

Example 1: Bob hires a cashier who is 20 years old and lives in an EZ. At $6 an hour for a 35-hour week, with one week paid vacation, for a total annual wage of $10,920. Bob's WOTC Credit would be:
1 x $6,000 x .40 = $2,400.

Example 2: Joe hires 6 employees from the designated groups, three of them for year-round jobs at an annual wage of $15,000, and three of them are 16-year olds who live in an EZ for 8-week summer jobs at an annual wage of $2,000. Joe's WOTC Credit would be:
(3 x $6,000 x .40) + (3 x $2,000 x .40) = $9,600.

Example of When a Business is Qualified for Both the WOTC and the EZ Wage Credit. Ann hires Maria, a 20-year old woman who lives in the Empowerment Zone, to work part-time for her. Ann obtains the certifications from the State Employment Services Agency that Maria qualifies for the WOTC. Maria continues to work for Ann throughout the year and Ann pays her $15,000 that year. Ann takes the WOTC for the first $6,000 in wages paid to Maria, for a credit of $2,400 (40% times $6,000) and then is able to take the EZ Wage Credit on the remaining $9,000 paid that year for a $1,800 EZ Wage Credit. Even though Ann paid Maria $15,000, she cannot take the EZ Wage Credit on the full $15,000 because she took the WOTC on the first $6,000 in wages. Ann's total credit (WOTC plus EZ Wage Credit) is $4,200. The next year Ann would be able to take the EZ Wage Credit, but not the WOTC, calculated on up to $15,000 in wages paid.

Formula

______	x	______	x	**.40**	=	______
Number of WOTC employees *working at least 400 hours*		Wage, up to $6,000		Credit Rate		WOTC Wage Credit
______	x	______	x	**.25**	=	______
Number of WOTC employees *working at least 120 hours*		Wage, up to $6,000		Credit Rate		WOTC Wage Credit

The formulas contained in the workpad result only in estimated tax savings and should not be officially relied upon for Federal government tax purposes. Please consult your tax preparer or the IRS for official guidance.

Partial Exclusion of Gain on Sale of Empowerment Zone Stock

WorkPad for Selling New Stock in Your Corporation in the Zone

Description: A taxpayer other than a corporation excludes 60 percent of the gain on sale of qualified small business stock of a C corporation that is a qualified small business entity located in an EZ other than the District of Columbia provided the stock was held for more than 5 years.

Note: Qualified small business stock must be acquired after December 21, 2000, and before January 1, 2010, at original issuance for cash, property (other than stock), or as compensation for services provided to the corporation.

Applicable IRS Publication: Publication 550

Stock must be acquired after December 21, 2000 and before January 1, 2010, at original issuance for cash.

Example 1: Bob realizes a $300,000 gain from the sale of stock he purchased six years ago. If the maximum 20% capital gain rate applies, Bob's tax on the gain would be: $300,000 x .20 = $60,000.

If Bob realized the $300,000 gain from the sale of qualified small business stock of C corporation that was a qualified small business entity located in an EZ, 60 percent of the gain would be excluded from gross income. The portion of the gain included in gross income would be characterized as section 1202 gain subject to tax at a maximum rate of 28%. If the maximum rate applies, Bob's tax on the gain would be: $300,000 x.40 x.28=$33,600.

Note: The maximum rate of tax on section 1202 gains is 28%. The maximum rate of tax on capital gains other than section 1202 gains is generally 20%.

Formula

Without the Exclusion

______	x	**1.00**	x	**.20**	=	______
Amount of Gain		% of Gain Subject to Tax		Assumed Federal Tax Rate		Amount of Tax

Formula

With the Exclusion

______	x	**.40**	x	**.28**	=	______
Amount of Gain		% of Gain Subject to Tax		Assumed Federal Tax Rate		Amount of Tax

The formulas contained in the workpad result only in estimated tax savings and should not be officially relied upon for Federal government tax purposes. Please consult your tax preparer or the IRS for official guidance.

Enterprise Zone Facility Bonds

Description: State and local governments can issue EZ Facility Bonds to make loans at lower interest rates to EZ Businesses to finance Qualified Zone Property.

Applicable IRS Publication: Publication 954

- no per borrower limit in EZ
- bonds are subject to a volume cap allocated to each EZ

Example 1: Bob borrows $1 million on a tax-exempt basis. Bob saves about 2 percent on his interest rate compared to a conventional loan. Compare the costs (assuming level debt service amortized over 30 years):

	5% tax-exempt rate	7% taxable rate	Savings
Annual payment	$65,051	$80,586	$15,535
Total interest	$951,543	$1,417,59	$466,049

Formula

Fast Formula not applicable

The formulas contained in the workpad result only in estimated tax savings and should not be officially relied upon for Federal government tax purposes. Please consult your tax preparer or the IRS for official guidance.

HUD WorkPad - Empowerment Zone Continued

Determining Eligibility of an RC/EZ Business

The table of Yes/No Questions is designed to help a business determine whether it meets the definition of "Enterprise Zone Business" in order to qualify for the following five tax incentives: Increased Section 179 Deduction; Enterprise Zone Facility Bonds; Zero Percent Capital Gains Rate for DC Zone Assets; Nonrecognition of Gain on Sale of Empowerment Zone Assets, and Partial Exclusion of Gain on Sale of Empowerment Zone.

The table can also be used to help a business determine whether it meets the definition of "Renewal Community Business" in order to qualify for the following two Federal tax incentives: Increased Section 179 Expensing Deduction; and Zero Percent Capital Gains for RC Assets.

What it takes to be an RC or EZ Business

Qualifying as an EZ or RC Business will make you eligible for many tax incentives. See how you fare in meeting the requirements for being an EZ or RC Business. Answer the questions below only with respect to your separate legal entity (ignore so-called "related" parties).

	Yes	No
Are you a sole proprietorship, partnership or corporation for federal taxes?	❏	❏
Is the business in the Zone the only business you have?	❏	❏
Will at least 50% of the gross income of the business come from actively carrying out business in the Zone (for businesses in the DC Zone, substitute "80%" for "50%")?	❏	❏
Is a substantial part of the use of the equipment and real property of your business in the Zone?	❏	❏
Does a substantial part of the work your employees do for you occur in the Zone?	❏	❏
Do at least 35% of your employees live in the Zone (does not apply to businesses in the DC Zone)?	❏	❏
Is a substantial part of the intangibles of your business used in the active conduct of your business in the Zone?	❏	❏
Is less than 5% of the average of the total unadjusted bases of the property owned by your business from collectibles not held primarily for sale to customers?	❏	❏
Is less than 5% of the average of the total unadjusted bases of the property owned by your business from nonqualified financial interests (e.g., debt, stock, partnership interests, options, futures contracts, forward contracts, warrants, notional principal contracts, and annuities)?	❏	❏

Continued on next page

The formulas contained in the workpad result only in estimated tax savings and should not be officially relied upon for Federal government tax purposes. Please consult your tax preparer or the IRS for official guidance.

What it takes to be an RC or EZ Business Continued

If the answer is YES to all of the above, you have met the initial set of requirements.
Now review the following:

	Yes	No
Is your business one of renting residential property (like apartment buildings)?	❑	❑
Do you predominantly develop or hold intangibles that are licensed or sold to others (e.g., software, movies, recordings)?	❑	❑
If you are in farming, are your total farming assets valued at more than $500,000?	❑	❑
If you rent commercial property, will less than 50% of your gross rental income come from an EZ Business?	❑	❑
Is your business any of the following:		
Liquor Store	❑	❑
Massage Parlor	❑	❑
Gambling facility	❑	❑
Racetrack	❑	❑
Suntan parlor	❑	❑
Country club	❑	❑
Golf Course	❑	❑
Hot tub facility	❑	❑
Is your business involved in selling insurance, stocks, or bonds or other financial products?	❑	❑
If you rent tangible personal property (e.g. equipment), will less than 50% of your rentals of the property be to Zone businesses or Zone residents?	❑	❑

If your answer is NO to each of the above, you may qualify for the following tax incentives:

Additional expensing of equipment

Low-cost tax-exempt bond financing

Partial exclusion of gain on sale of stock in your corporation

Ability to rollover gain on sale of stock or partnership interest or real estate

These are in addition to wage credits for employees that you hire that live in the Zone.

The formulas contained in the workpad result only in estimated tax savings and should not be officially relied upon for Federal government tax purposes. Please consult your tax preparer or the IRS for official guidance.

Tax Incentive WorkPad – *Fast Formulas*

If you are in an RENEWAL COMMUNITY (RC) then the following tax incentives apply:

Renewal Community Employment Credit (RC Wage Credit)

WorkPad for a Business Located in the Renewal Community

Formula

________	x	________	x	.15	=	________
Number of RC employees		Wage (*up to $10,000*)		RC Credit Rate		Wage Credit

Zero Percent Capital Gains Rate for Renewal Community Assets

WorkPad for a Business Looking to Sell a Building or to Sell New Stock or Capital Interests in Its Corporation or Partnership in the Renewal Community

Formula

________	x	.20	=	________
Amount of Gain from Appreciation		Federal Tax Rate		Amount of Taxes Saved

WOTC (Work Opportunity Tax Credit)

WorkPad for a Business Located Inside or Outside of the Renewal Community

Formula

________	x	________	x	.40	=	________
Number of WOTC employees *working at least 400 hours*		Wage, up to $6,000		RC Credit Rate		WOTC Wage Credit
________	x	________	x	.25	=	________
Number of WOTC employees *working at least 120 hours*		Wage, up to $6,000		RC Credit Rate		WOTC Wage Credit

Increased Section 179 Deduction

WorkPad for Purchasing New Equipment

Formula

________	x	.35	=	________
Cost of Qualified Equipment *up to $35,000*		Assumed Federal Tax Rate		Amount of Taxes Saved

Commercial Revitalization Deduction

WorkPad for a Business Planning to Construct, Expand, or Acquire and Renovate a Building in the Renewal Community

Formula

Without the incentive:

________	÷	39	=	________
Total Cost of Project		Period of Depreciation		Per Year Deduction

With the 120 Month Depreciation Option:

________	÷	10	=	________
Total Cost of Project		Period of Depreciation		Per Year Deduction

With the ½ Expensing, ½ Depreciation Option:

________	÷	2	=	________
Total Cost of Project		Period of Depreciation		Per Year Deduction
________	÷	39	=	________
1/2 Cost of Project		Period of Depreciation		Per Year Deduction for Remaining Costs

The formulas contained in the workpad result only in estimated tax savings and should not be officially relied upon for Federal government tax purposes. Please consult your tax preparer or the IRS for official guidance.

Tax Incentive WorkPad – *Fast Formulas*

If you are in an EMPOWERMENT ZONE (EZ) then the following tax incentives apply:

EZ Wage Credit
WorkPad for a Business Located in the Zone

Formula

______	x	______	x	.20	=	______
Number of EZ employees		Wage (*up to $15,000*)		EZ Credit Rate		Wage Credit

Increased Section 179 Deduction
WorkPad for Purchasing New Equipment

Formula

______	x	.35	=	______
Cost of Qualified Equipment *up to $35,000*		Assumed Federal Tax Rate		Amount of Taxes Saved

Zero Percent Capital Gains Rate for District of Columbia Enterprise Zone Assets
WorkPad for a Business Looking to Sell a Building or to Sell New Stock or Capital Interests in Its Corporation or Partnership in the District of Columbia

Formula

______	x	.20	=	______
Amount of Gain from Appreciation		Federal Tax Rate		Amount of Taxes Saved

WOTC (Work Opportunity Tax Credit)
WorkPad for a Business Located Inside or Outside of the Zone

Formula

______	x	______	x	.40	=	______
Number of WOTC employees *working at least 400 hours*		Wage, up to $6,000		RC Credit Rate		WOTC Wage Credit
______	x	______	x	.25	=	______
Number of WOTC employees *working at least 120 hours*		Wage, up to $6,000		RC Credit Rate		WOTC Wage Credit

Partial Exclusion of Gain on Sale of Empowerment Zone Stock
WorkPad for Selling New Stock in Your Corporation in the Zone

Formula

Without the Exclusion:

______	x	1.00	x	.20	=	______
Amount of Gain		% of Gain Subject to Tax		Assumed Federal Tax Rate		Amount of Tax

With the Exclusion:

______	x	.40	x	.28	=	______
Amount of Gain		% of Gain Subject to Tax		Assumed Federal Tax Rate		Amount of Tax

Empowerment Zone Facility Bonds
WorkPad for Planning to Construct or Expand a Building in the Zone

Fast Formula not applicable

The formulas contained in the workpad result only in estimated tax savings and should not be officially relied upon for Federal government tax purposes. Please consult your tax preparer or the IRS for official guidance.

Appendix

Current Renewal Communities, Empowerment Zones, and Enterprise Communities as Designated by HUD and USDA

HUD Designees

Renewal Communities (RCs)—40

Urban (U)—28
Rural (R)—12

Alabama
Greene-Sumter (R)
Mobile County (U)
Southern Alabama (R)

California
Los Angeles (U)
Orange Cove (R)
Parlier (R)
San Diego (U)
San Francisco (U)

Georgia
Atlanta (U)

Illinois
Chicago (U)

Kentucky
Eastern Kentucky (R)

Louisiana
Central Louisiana (R)
New Orleans (U)
Northern Louisiana (R)
Ouachita Parish (U)

Massachusetts
Lawrence (U)
Lowell (U)

Michigan
Detroit (U)
Flint (U)

Mississippi
West Central Mississippi (R)

New Jersey
Camden (U)
Newark (U)

New York
Buffalo-Lackawanna (U)
Jamestown (R)
Niagara Falls (U)
Rochester (U)
Schenectady (U)

North Dakota
Turtle Mountain Band of Chippewa (R)

Ohio
Hamilton (U)
Youngstown (U)

Pennsylvania
Philadelphia (U)

South Carolina
Charleston (U)

Tennessee
Chattanooga (U)
Memphis (U)

Texas
Corpus Christi (U)
El Paso County (R)

Vermont
Burlington (R)

Washington
Tacoma (U)
Yakima (U)

Wisconsin
Milwaukee (U)

Urban Empowerment Zones (EZs)—30

Round I Urban EZs—5

Illinois
Chicago

Maryland
Baltimore

Michigan
Detroit

New York
New York

Pennsylvania/New Jersey
Philadelphia/Camden

Supplemental Round I EZs—2

California
Los Angeles

Ohio
Cleveland

Round II Urban EZs—15

California
Santa Ana

Connecticut
New Haven

Florida
Miami-Dade County

Indiana
Gary-Hammond-East Chicago

Massachusetts
Boston

Minnesota
Minneapolis

Missouri/Illinois
St. Louis/East St. Louis

New Jersey
Cumberland County

Ohio
Cincinnati
Columbus

South Carolina
Columbia-Sumter

Tennessee
Knoxville

Texas
El Paso

Virginia
Norfolk-Portsmouth

West Virginia/Ohio
Huntington/Ironton

Round III Urban EZs—8

Arizona
Tucson

Arkansas
Pulaski County

California
Fresno

Florida
Jacksonville

New York
Syracuse
Yonkers

Oklahoma
Oklahoma City

Texas
San Antonio

Enterprise Zones—1

District of Columbia
Washington



Urban Enterprise Communities (ECs)—49

Round I Urban ECs—45

Alabama
Birmingham

Arizona
Phoenix

Arkansas
Pulaski County

Colorado
Denver

Connecticut
Bridgeport
New Haven

Delaware
Wilmington

District of Columbia
Washington

Florida
Miami
Tampa

Georgia
Albany

Illinois
East St. Louis
Springfield

Indiana
Indianapolis

Iowa
Des Moines

Kentucky
Louisville

Massachusetts
Springfield

Michigan
Muskegon

Minnesota
Minneapolis
St. Paul

Mississippi
Jackson

Missouri
St. Louis

Nebraska
Omaha

Nevada
Las Vegas

New Hampshire
Manchester

New Mexico
Albuquerque

New York
Newburgh-Kingston

North Carolina
Charlotte

Ohio
Akron
Cleveland
Columbus

Oklahoma
Oklahoma City

Oregon
Portland

Pennsylvania
Harrisburg
Pittsburgh

Rhode Island
Providence

Tennessee
Nashville

Texas
Dallas
El Paso
San Antonio
Waco

Utah
Ogden

Virginia
Norfolk

Washington
Seattle

West Virginia
Huntington

Round I Urban Enhanced ECs—4

California
Oakland

Massachusetts
Boston

Missouri/Kansas
Kansas City

Texas
Houston

USDA Designees

Round I Rural EZs—3

Kentucky
Kentucky Highlands

Mississippi
Mid-Delta

Texas
Rio Grande Valley

Round II Rural EZs—5

California
Desert Communities

Georgia
Southwest Georgia United

Illinois
Southernmost Illinois Delta

North Dakota
Griggs-Steele

South Dakota
Oglala Sioux Tribe

Round III Rural EZs—2

Maine
Aroostook County

Texas
FUTURO

Round I Rural ECs—28

Alabama
Chambers County

Arizona
Arizona Border Region

Arkansas
East Arkansas
Mississippi County

California
Imperial County
Watsonville

Florida
Jackson County

Georgia
Central Savannah River Area
Crisp-Dooly

Louisiana
Northeast Louisiana Delta

Michigan
Lake County

Mississippi
North Delta Mississippi

Missouri
East Prairie

New Mexico
La Jicarita

North Carolina
Halifax-Edgecombe-Wilson
Empowerment Alliance
Robeson County

Ohio
Greater Portsmouth

Oklahoma
Southeast Oklahoma

Oregon
Josephine County

Pennsylvania
Lock Haven

South Carolina
Williamsburg-Lake City

South Dakota
Beadle and Spink

Tennessee
Fayette-Haywood Counties
Scott-McCreary Area

Virginia
Accomack-Northampton

Washington
Lower Yakima County

West Virginia
Central Appalachia
McDowell County

Round II Rural ECs—20

Alaska
Metlakatla Indian Community

Arizona
Four Corners

California
Huron-Tule

Florida
Empowerment Alliance of
Southwest Florida

Hawaii
Molokai

Indiana
Austin

Kansas
Wichita County

Kentucky
Bowling Green

Maine
Empower Lewiston

Michigan
Clare County

Montana
Fort Peck Assiniboine and Sioux Tribe

New Mexico
Deming

Oklahoma
Tri-County Indian Nations

Pennsylvania
Fayette

South Carolina
Allendale County ALIVE

Tennessee
Clinch-Powell

Texas
FUTURO

Washington
Five Star

West Virginia
Upper Kanawha Valley

Wisconsin
Northwoods NiiJii

George W. Bush, President
United States of America

Mel Martinez, Secretary
U.S. Department of Housing and Urban Development

Roy A. Bernardi, Assistant Secretary
Office of Community Planning and Development

U.S. Department of Housing and Urban Development
www.hud.gov/offices/cpd/ezec

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