

PULASKI EMPOWERMENT ZONE

EXECUTIVE SUMMARY

THE THIRD SWING IS A BIG HIT !

After submitting the third application since 1993 Little Rock, North Little Rock and Pulaski County finally received the long sought HUD Urban Empowerment Zone (EZ) designation for economically distressed parts of Pulaski County.

The Pulaski EZ is one of seven urban areas nationwide to receive an Empowerment Zone designation from the Department of Housing and Urban Development in this third round of awards. The designation is designed to support growth and revitalization opportunities for distressed areas of communities, and is part of a business tax incentive package valued at \$17 to \$22 billion nationwide. The designation period will be from January 1, 2002 to December 31, 2009.

The Pulaski County designation was a collaborative partnership effort between Little Rock, North Little Rock, Pulaski County Government, UALR, Pulaski Enterprise Community Alliance, Rose Law Firm, Arkansas Department of Economic Development, Arkansas Development Finance Authority, Little Rock Regional Chamber of Commerce, Downtown Partnership, Central Arkansas Regional Transit Authority, Metroplan, Contractors/Developers, private businesses, and local financial institutions.

The EZ area is composed of fifteen census tracts in downtown Little Rock and North Little Rock that had to meet poverty and population criteria. The EZ area totaled 17.2 square miles. The EZ also includes an additional 2,000 acres of developable area that was exempt from poverty and population criteria. The EZ area and the developable sites will receive tax breaks and regulatory relief to help new and existing businesses provide more jobs for EZ residents and promote community revitalization. The three "EZ Developable Sites" include: Downtown LR Riverfront site; the University/Asher site; and the Little Rock Port site. (See EZ Map)

If you are a For-Profit business and your offices are within the zone and any of your employees live and work within the zone you will be eligible for valuable tax credits. The tax incentives available to your property sales or lease clients can make a substantial difference to their bottom line and be a defining factor in their location selection. Each EZ incentive offered is designed to meet the specific needs of a business and offer inducements to locate and hire additional workers.

TAX CREDITS

Empowerment Zone Employment Credit (EZ Wage Credit)

Businesses are entitled to a credit against their federal tax liability of up to \$3,000 (calculated as 20% of FUTA wages up to \$15,000) for every newly hired or existing employee who lives and works in the EZ. Substantially all (defined for other purposes as at least 85%; not defined for EZs) of the employee's services during a period (pay period or calendar year) must be in the EZ. Credit cannot be prorated within a period. Employer should obtain a statement from the employee, under penalty of perjury, that gives the address of the employee's principal residence and provides assurance that the employee will notify the employer of a change in the employee's principal residence. Applies to full and part-time employees. Credits can be passed through partnerships and S- corporations under rules similar to other business tax credits. Unused credit amounts can be carried forward up to 20 years and carried back one year (but not prior to January 2002). Business must reduce the deduction for salaries and wages by the amount of the credit taken. Alternative minimum tax may be reduced by 25% of the credit. Liquor stores are ineligible. Not available for 5% owners and family members. IRS Publication 954 and Form 8844.

Work Opportunity Tax Credit (WOTC)

Businesses are entitled to a credit against their federal tax liability of up to \$2,400 (calculated as 25% of FUTA wages paid to an individual who works at least 120 hours or 40% of FUTA wages paid to an individual who works at least 400 hours) for first year wages of each new employee hired from groups with traditionally high unemployment rates or other special employment needs, including (1) youth ages 18 to 24 who live in the EZ and (2) summer youth employees ages 16 and 17 who live in the EZ. [*This supplements existing WOTC not related to EZ designation for veterans, ex-felons, vocational rehabilitation referrals, food stamp recipients, recipients of assistance under AFDC or TANF, and SSI recipients.*]

Applies to full and part-time employees. Unused credit amounts can be carried forward up to 20 years and carried back one year (but not prior to January 2002). Business must reduce the deduction for salaries and wages by the amount of the credit taken. Employee must complete Form 8850 prior to making job offer. Form must be forwarded to State Employment Services Agency ("SESA") within 21 days of the date the employee starts

work. WOTC may be taken only for employees who have been certified by SESA. Cannot be combined with WtW credit.

Welfare to Work Credits (WtW)

The WtW provides existing credit not related to EZ designation for businesses that hire long-term family assistance recipients. Credits up to \$3,500 for the first year and \$5,000 for the second year for each new hire. IRS Publication 954 and Forms 8861 and 8850.

Definition of Enterprise Zone Business ("EZ Business")

Four of the Federal tax incentives-Increased Section 179 Deduction, Enterprise Zone Facility Bonds, Nonrecognition of Gain on Sale of Empowerment Zone Assets, and Partial Exclusion of Gain on Sale of Empowerment Zone Stock-require that the business meet the definition of EZ Business. An EZ Business is a corporation, partnership, or sole proprietorship that, for each taxable year, meets the following tests:

- Except with respect to a sole proprietorship, every trade or business of the entity is actively conducted in the EZ (legally separate entities are not aggregated with related entities for these tests).
- At least 50% of the total gross income or the net income is derived from the active conduct of business within the EZ.
- A substantial portion of the use of the tangible property of the entity (whether owned or leased) is within the EZ.
- A substantial portion of the intangible property of the entity is used in the active conduct of the business.
- A substantial portion of the services performed for the employer by its employees occurs within the EZ.
- At least 35% of the employees reside in the EZ. Calculate on either a per-employee fraction or an employee actual work-hour fraction. The business must apply the same method consistently over the period of the tax incentive once a method is selected. Employees include persons employed for at least 90 days and who work at least 15 hours per week. Percentages can be averaged over a rolling, consecutive 5-year period.
- No more than 5% of the property is nonqualified financial property (e.g., debt, stock, and various financial instruments) except for reasonable amounts of working capital held in cash, cash equivalents, or debt instruments with a term of 18 months or less and certain accounts receivable arising from sales of inventory.
- No more than 5% of the property is works of art or other collectibles unless held for sale to customers.

Certain types of businesses do not qualify, including liquor stores, residential rental properties, and businesses that predominately hold or develop intangibles for sale or license, or businesses that rent personal property. A real estate developer can qualify only if at least 50% of its gross rental income from real property is from EZ Businesses.

Definition of Qualified Zone Property ("QZP")

- 85% of the use of the property must be in the active conduct of an EZ Business by a taxpayer in the EZ.
- The taxpayer acquired the property by purchase after January 15, 2002.
- Original use of the property in the EZ commences with the taxpayer (that is, the taxpayer is the first person to use the property inside the EZ) or the taxpayer meets the substantial renovation rule. Property is substantially renovated if, during any 24-month period beginning after January 15, 2002, there are additions to the basis of the property equal to the greater of 100% of the adjusted basis of the property or \$5,000.

Capital Gains

EZ Businesses can postpone or only partially recognize the gain on the sale of certain assets, including stock and partnership interests.

- **Non recognition of Gain of Sale of Empowerment Zone Assets**

An EZ Business can elect to roll over gain from the sale of an Empowerment Zone Asset ("EZA") held for more than 1 year if the proceeds are used to purchase other qualifying EZA in the same EZ within 60 days of the sale of the original EZA. EZA includes (1) stock in a domestic company acquired by the taxpayer after December 21, 2000 and before January 1, 2010 at its original issue from the corporation solely in exchange for cash, (2) any capital or profit interest in a domestic partnership if the interest was acquired by the taxpayer after December 21, 2000 and before January 1, 2010 from the partnership solely in exchange for cash, and (3) tangible business property acquired by the taxpayer by purchase after December 21, 2000 and before January 1, 2010 where either the original use of the property in the EZ commences with the taxpayer or the taxpayer substantially improves the property. Gain from the sale of real property or intangible assets can be rolled over only if it is an integral part of the EZ Business. The amount of gain rolled over cannot exceed the cost of the replacement EZA. The gain on the replacement EZA can also be rolled over if it meets the test.

- **Partial Exclusion of Gain on Sale of Empowerment Zone Stock**

A taxpayer can exclude 60% of gain realized on the sale of stock in a small EZ Business (generally, a C corporation with gross assets of \$50 million or less) located in the EZ. The stock must be acquired by the taxpayer upon original issuance and after December 21, 2000 and must either be an EZ Business when the stock is purchased or be formed for

purposes of meeting the definition and must meet the definition for substantially all (i.e., 85%) of the taxpayer's 5-year holding period. The exclusion does not apply to gains after December 31, 2013.

Tax Deductions

- ***Increased Section 179 Deduction***

An EZ Business may take an additional expense deduction of up to \$35,000 per year on purchases of tangible personal property (i.e., equipment and machinery) acquired after January 15, 2002 for use in the EZ. The allowance is available only for QZP. For each \$1 of QZP greater than \$200,000 in a tax year, the expenses amount is reduced by 50 cents [The general tax rule is a \$1 for \$1 reduction over \$200,000.] IRS Form 4562.

Bond Financing

- ***Enterprise Zone Facility Bonds ("EZ Bonds ")***

A type of tax-exempt revenue bond can be issued to make a loan to an EZ Business to finance QZP. At least 95% of the net proceeds from the bond issue must be used to finance QZP principally used by an EZ Business and certain land used for a related purpose (for example, land where the business and its customer and employee parking lot are located). Overall limitation of \$130 million in EZ Bonds can be issued for EZ Businesses in the LR/NLR EZ, but there is no per-borrower limitation. Bonds can be issued for commercial, retail, or industrial purposes (however, under the Arkansas Constitution, revenue bonds cannot be issued for shopping centers or other establishments engaged in the sale of food or goods at retail; nor, without voter approval, for hotels or motels, rental or professional office buildings or facilities for recreation or entertainment). Note: nationally, this form of bond has been used rarely because the market has not accepted the risk that the business will cease to be an EZ business that would cause the bonds to be taxable.

- ***Qualified Zone Academy Bonds ("QZABs")***

Allows the state and local school districts to match no-interest loans with private funding sources to finance public school renovations and programs. Public schools located in the EZ can obtain interest-free loans if they partner with private businesses to establish programs within public schools. A business can partner through contributions (which may be tax deductible as a charitable contribution) or, in certain cases, by lending money to schools to improve the academic curricula, enhance graduation and employment rates, and better prepare students for college and the workforce. A Qualified Zone Academy must be a public elementary or secondary school located in the EZ or the school must have a reasonable expectation when the bonds are issued that at least 35% of the school's students will be eligible for free or reduced-cost lunches.

Other Incentives

Like all distressed communities, the EZ will also be able to take advantage of the **New Markets Tax Credits** that provide investors with a credit against their federal taxes of 5 to 6 percent of the amount invested in a distressed area. The credit is available to equity investors in community development entities ("CDE"); the CDE must use at least 85% of its cash infusion to make qualified low-income community investments. Also available in the EZ as elsewhere is the *Low- Income Housing Tax Credit* providing credit against Federal taxes for owners of newly constructed or renovated rental housing. Businesses in the EZ and elsewhere may deduct qualified cleanup costs of hazardous substances in **Brownfields**.

PULASKI LOCAL COMMITMENT

The strongest commitment of the EZ application is the solid business and civic commitment to action on a well-developed, long-range plan to improve the Downtown Little Rock/North Little Rock Core and River District of Central Arkansas. The thriving construction and commercial activities in the core area provide a fertile environment for implementation if EZ's overall goals of Economic Development, work Force Preparation and Education, Small Business Development, Housing Revitalization, Community Network and Leadership and the promotion and support of Technology-Based Industries.

EMPOWERMENT ZONE HISTORY

In 1994 six Urban Empowerment Zones (EZs) were designated in ROUND I, during the first term of President Clinton, as an initiative to rebuild communities in American's poverty stricken areas. ROUND I Urban EZs included: Atlanta, GA; Baltimore, MD; Chicago, IL; Detroit, MI; New York (Bronx / Upper Manhattan); and Philadelphia, PA/ Camden, NJ In 1995 two supplemental Urban EZs designated Los Angeles, CA and Cleveland, OH.

In 1998 the ROUND II designations, incorporated an additional fifteen urban EZs.

The ROUND II Urban EZ designations included Boston, MA; Cincinnati, OH; Columbus, OH; Cumberland Co., NJ; El Paso, TX; Gary/East Chicago/Hammond, IN; Huntington, WV/ Ironton, OH; Knoxville, TN; Miami/Dade Co., FL; Minneapolis, MN; New Haven, CT; Norfolk/Portsmouth, VA; Santa Ana, CA; St. Louis, MO/East ST. Louis, IL; and Sumter, SC.

The January, 15,2002 announcement of the 2001 ROUND III EZ designations added another seven Urban EZs. The designated areas announced with Pulaski County included: Fresno, CA; Jacksonville, FL; Syracuse, NY; Yonkers, NY; Oklahoma City, OK; and San Antonio, TX. The Round III EZ additional designations bring the national total HUD Urban EZ total to thirty. The EZ designation puts Pulaski County in a very select tear of Metropolitan areas with this highly coveted menu of economic development federal tax incentives. Atlanta, GA, a Round I EZ, forfeited it's 1994 designation in favor of becoming a Round III designated Renewable Community (RC), as a result Tucson, AZ was designated as a supplemental Round III Empowerment Zone, keeping the total number of Empowerment Zones at thirty.

NOTE: HUD implementation workshops are planned for May 20-22, 2002 in Washington D.C. The Pulaski EZ implementation plan will include workshops, seminars, community meetings and presentations on the utilization and marketing of the federal tax credits to employers, employees, and residents of the EZ, and the establishment of an EZ Reinvestment Fund.

FURTHER INFORMATION CAN BE FOUND BY CONTACTING:

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