

Professional Corner

FEDERAL AND STATE INCENTIVES AND TAX CREDITS AVAILABLE TO FINANCIAL INSTITUTIONS

Empowerment Zones and Renewal Communities

The federal government has designated certain economically depressed areas as tax advantaged "zones" across the country. The "zones" are referred to as Empowerment Zones and Renewal Communities. Many community banks do not take full advantage of the myriad of available "zone" programs, primarily because these programs are not very well known. The Empowerment Zone tax incentives are worth approximately \$5.3 billion to small and large businesses located in Empowerment Zones. These incentives encourage businesses to open and expand and to hire local residents. Empowerment Zone incentives include; hiring employment credits, low-interest loans, reduced taxation on capital gains, and other incentives.

Probably the most popular incentive generated by having a business within an Empowerment Zone is the hiring employment tax credit.

Businesses can take an annual federal income tax credit of up to \$3,000 for each employee who lives and works for a business within the Empowerment Zone.

Similar to the Empowerment Zone, the Renewal Community tax incentives are worth approximately \$5.6 billion to eligible businesses of all sizes in Renewal Communities. The Renewal Communities incentives also encourage businesses to open, expand, and to hire local residents. The incentives include; employment credits, a 0% tax on capital gains, accelerated depreciation through Commercial Revitalization

Deductions, and other incentives. Also the most popular incentive generated by having a business within a Renewal Community is the hiring employment tax credit. Businesses can take an annual federal income tax credit of up to \$1,500 for each employee who lives and works for a business within the Renewal Community.

Work Opportunity Tax Credit and the Indian Employment Credit

The work opportunity tax credit (WOTC) provides businesses with an incentive to hire individuals from groups that have a particularly high unemployment rate or other special employment needs. The business does not have to be located within an empowerment zone or renewal community to qualify for these credits. A bank can claim the credit if it pays or incurs "qualified first-year wages" to a "targeted group employee."

Qualified first-year wages are wages a bank pays or incurs for work performed by a targeted group employee during the 1-year period beginning on the date the employee begins work. A targeted group employee is any employee who has been certified by a state employment security agency (SESA) as a member of a group that has a particularly high unemployment rate or other special employment needs. Groups include, but are not limited to, Veterans, Food Stamp recipients, Supplemental security income (SSI) recipients and individuals age 18 to 24 who live in an empowerment zone or renewal community.

Businesses can take a federal in-

come tax credit of up to \$2,400 for each employee's first year of employment that is certified by SESA. Applications for certification must be filed with the agency within 28 days after the employee begins work.

The Indian Employment Credit provides businesses with an incentive to hire certain individuals who live on or near an Indian reservation. A bank can claim the Indian Employment Credit if it pays or incurs "qualified wages" to a "qualified employee." Qualified wages are any wages paid or incurred for services performed by an employee while the employee is a qualified employee. A qualified employee, for any tax period, is any employee who meets all the following tests; the employee is an enrolled member of an Indian tribe or the spouse of an enrolled member of an Indian tribe, the employee performs substantially all of his or her services within an Indian reservation and while performing those services, the employee has his or her main home on or near that reservation. Qualifying businesses can take an annual federal income tax credit of up to \$4,000 for each qualified employee.

California Tax Credits and Incentives for Financial Institutions

One of the more significant state tax credit and incentive programs available to financial institutions doing business in California are those provided by California's Enterprise Zone program (CAEZ). Like the fed's "zone" programs the CAEZ was established to stimulate business investment in depressed areas of the State and create job

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opportunities for Californians. There are currently 42 zones located throughout California of which 23 are being newly designated in 2007 and 2008.

Specific to Financial Institutions is the CAEZ "Net Interest Deduction" incentive. In order to compel investment into Enterprise Zones, the state has provided a deduction from income for the amount of "Net Interest" received from loans made to trade or businesses located within or near a zone. **The institution making the loan does not have to be located within a zone.**

Net Interest is the full amount of interest received less direct expenses incurred in making the loan. The types of loans that qualify for this deduction include; business loans, mortgages and loans from noncommercial sources. In order to qualify for the deduction all of the following requirements must be met; the trade or business receiving the loan must be within a zone, the money must be used strictly for the borrower's trade or business within the zone and the lender does not have an equity or other ownership interest in the borrower's trade or business.

Financial institutions and other businesses that have a location in a CAEZ and hire a qualified employee can generate a state income tax hiring credit for the employer of over \$37,000 per employee. Similar to the federal WOTC

credit discussed above, the employer can claim the credit if it pays or incurs "qualified wages" to a "qualified employee". Qualified wages are any wages paid or incurred when at least 51% of the services performed by an employee are within a zone. A qualified employee is any employee who, at the time of hire, can be certified by a state CAEZ coordinator as a member of a targeted group that has a particularly high unemployment rate or other special employment needs. Targeted groups include, but are not limited to, WOTC certified individuals, Veterans, Native Americans, Food Stamp recipients, Supplemental Security Income (SSI) recipients, dislocated workers, disabled workers and residents of a Targeted Employment Area. The credit is calculated based on the employee's wages and is taken over a 5 year period, the majority of which is taken in the first 2 years.

These same businesses also can qualify for a state income tax credit equal to the sales tax paid on qualified property purchased and placed in service at the business' zone location. Individuals, partnerships and S-Corporation shareholders may claim an annual credit equal to the sales tax paid to purchase \$1 million of qualified property. Corporations may claim an annual credit equal to the sales tax paid to purchase \$20 million of qualified property. Qualified property is machinery or machinery parts used to: manufacture a

product, produce renewable energy resources and control air or water pollution. The definition of qualified property was recently broadened to include data processing and communication equipment including but not limited to; computers, monitors, copy machines, fax machines and telephone systems.

For more information about how your bank might take advantage of any of these programs please contact David Estrada, Credits and Incentives Group, Moss Adams LLP at 480-366-8325 or e-mail him at david.estrada@mossadams.com