



Alert

Economic Development Incentives

Empire Zones: Update - Decertification and Retention Certificates

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As noted in our previous alert, the FY 2010 NYS budget significantly changed New York's Empire Zones (EZ) program. This alert brings you an update about the certification review process to be conducted by the Commissioner of Economic Development, and focuses more closely on the tax treatment of 2008 EZ credit claims. As noted in our prior email, the new law requires the immediate attention of all EZ businesses and EZ business owners to any correspondence from the Department of Economic Development (Empire State Development Corporation) or the Department of Taxation and Finance ("DTF") regarding the Empire Zones program or tax benefits.

1. ESD Certification Update

A great majority of the 9,000+ Empire Zone businesses are likely to receive word from the Commissioner in the next three to five weeks as to the status of their EZ certification. Many will simply receive notice that their Empire Zone Retention Certificates are being processed and will be issued in June or July. Others may receive a request for additional information in connection with the Commissioner's review. Still others may receive notice that their EZ certification will be revoked.

Businesses receiving notice that their EZ certificates will be revoked (or that they will be "decertified") will have just 15 business days from the date of the notice to appeal the Commissioner's determination. Businesses receiving requests for additional information will likely be given a timetable to respond. In either case, a prompt and complete response will be necessary.

2. Tax Impact

The budget law also addressed the impact of decertification on the Empire Zone tax incentives. On April 15, DTF issued a memorandum advising taxpayers about the procedures necessitated by the new law. DTF has since publicly clarified its interpretation of the new law, particularly with respect to the impact of the law on 2008 tax returns filed by EZ businesses and their owners. The following points summarize the current interpretation of the law by DTF:

- The budget law disallows carryovers into 2008 (and later years) of the EZ Wage Tax Credit, EZ Investment Tax Credit, and EZ Capital Tax Credit, if the entity that generated the credit does not receive a Retention Certificate. DTF has stated that no EZ credits (new or carryforward) can be claimed for 2008 without a Retention Certificate.
- 2008 tax returns claiming EZ credits (other than the EZ Zone Capital Credit for donations to non-profit "community development" projects) are being held by DTF until issuance of the EZ Retention Certificates. Taxpayers claiming only the EZ Zone Capital Credit for contributions to non-profit "community development" projects will not need to re-submit their returns.
- Businesses that receive EZ Retention Certificates will be asked to re-submit a copy of their 2008 return with the Retention Certificate attached. Businesses that "pass through" income to owners (S corporations, partnerships, and most LLCs) will have to provide their owners with a copy of the Retention Certificate. The owners, in turn, must also re-submit a copy of their 2008 returns with the Retention Certificate attached.
- For businesses not receiving a retention certificate, it appears that DTF will process those 2008 returns by disallowing the EZ credits, and calculate interest

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(at the rate of 7.5% annually, compounded daily) on any underpayment of the recalculated tax, with interest accruing from April 15th. No penalties will be assessed for EZ credits disallowed because the Retention Certificate is not issued.

Although DTF's April 15 memorandum also described procedures for businesses (and their owners) who do not receive Retention Certificates by the due date (including extension) for the 2008 returns, it appears that these procedures will be delayed for a period of time to allow the Commissioner of Economic Development to complete her retention/decertification review.

Based upon recent information, there is a general expectation that Empire State Development will complete its retention/decertification review process by the end of July. Therefore, DTF intends to wait until late July or August before issuing notice of underpayment to taxpayers whose EZ businesses do not receive a Retention Certificate.

Because the EZ retention/decertification reviews are expected to occur in the next two months (perhaps sooner), taxpayers concerned with the 7.5% interest accrual (which would be charged if a Retention Certificate is not received) should consider whether to simply wait for the initial review process to be completed before deciding whether to start making additional tax deposits. Similarly, taxpayers whose 2008 returns have been extended should wait at least until the end of July to file, to allow time for the completion of the process for their EZ business.

3. Additional EZ Program Changes

The new law made other changes to the EZ program, summarized below.

- No businesses will be certified after June 30, 2010. Businesses certified before that date will retain their original 10 or 15 year benefit period (unless decertified).
- For businesses certified on or after April 1, 2009, the QEZE credit for real property taxes will be calculated as before, and then multiplied by 75%. Applicants will have to pass a 20:1 cost/benefit test (10:1 for manufacturers), based on estimates for the first three years of EZ certification. The Commissioner adopted regulations in March 2008 setting forth the 20:1 test; in our experience based on the 2008 regulations, very few businesses will pass this test.
- The QEZE Sales Tax Exemption has been eliminated as of August 31, 2009. Instead, Empire Zone businesses will have to pay the full sales and use tax on purchase of taxable goods or services, and then claim a credit (and refund) when filing their sales and use tax returns (the credit/refund can be claimed on a quarterly basis). Businesses certified after March 31, 2009 will be allowed the credit/refund only if their municipality has approved the local portion. Under current law only six jurisdictions (out of more than 80) adopted a local exemption; these jurisdictions are deemed by law to have also adopted the new credit/refund. Except for businesses in these jurisdictions and in jurisdictions that adopt the local exemption, the Empire Zone sales tax benefit will be effectively eliminated for business certified after March 31, 2009.
- Effective immediately, the Commissioner will have sole responsibility for EZ certification decisions - the local EZ administrative boards will recommend certification.

Finally, word has been circulating that the New York State Senate will be proposing legislation to address some of the technical aspects of the Empire Zone law changes. We will keep you apprised of these changes in future alerts.

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