

**REPORT OF THE
CHIEF LEGISLATIVE ANALYST**

DATE: March 18, 2013

TO: Honorable Members of the Rules, Elections and Intergovernmental Relations Committee

FROM: Gerry F. Miller *HEK*
Chief Legislative Analyst

Council File No: 13-0002-S28
Assignment No: 13-02-0124

SUBJECT: Resolution (Englander-Huizar-Wesson) to OPPOSE any reductions, changes, or elimination of the enterprise zone program.

CLA RECOMMENDATION: Adopt Revised Resolution to include in its 2013-2014 State Legislative Program OPPOSITION to the proposed changes to the Enterprise Zone program UNLESS AMENDED to leave retroactive vouchering and self-certification rules unchanged.

SUMMARY

Resolution (Englander-Huizar-Wesson), introduced on February 8, 2013, states that since 1984, the California Enterprise Zone program has provided a variety of incentives to stimulate economic development. These incentives have resulted in significant relief to businesses in some of the City's hardest hit neighborhoods. The Resolution states that Enterprise Zone hiring credits are designed to encourage the hiring of individuals who live in disadvantaged areas, are currently on unemployment, receiving government assistance, or are veterans entering the workforce. Describing Governor Jerry Brown's recent proposal to scale back the program by limiting the time available to apply for tax credits, remapping the zones, and reducing the amount of tax credits, the Resolution states such an action will be devastating to thousands of Los Angeles businesses and potentially result in job losses. Therefore, the Resolution resolves that the City oppose any reductions, changes, or elimination of the enterprise zone program.

BACKGROUND

The California Enterprise Zone program is a State program established in 1984. The program provides businesses located in geographically defined zones that have been determined to be economically distressed with tax incentives geared to promote business growth and the creation of new jobs. Each Enterprise Zone is administered by a local jurisdiction. In the City of Los Angeles, the Community Development Department (CDD) manages the City's three Enterprise Zones:

- Hollywood (expires 10/14/2021)
- East LA (expires 1/10/2023)
- Harbor Gateway Communities (expires 4/30/2027)

Businesses located in Enterprise Zones are eligible for tax credits and benefits including:

- **Hiring Credits.** Firms can earn \$37,440 or more in state tax credits for each qualified employee hired, including hiring targeted unemployed, underemployed, or individuals living in a Targeted Employment Area who may otherwise be at a disadvantage in obtaining employment;
- **Up to 100% Net Operating Loss (NOL) carry-forward.** NOL may be carried forward 15 years under most circumstances;
- **Sales Tax Credits.** Corporations can earn sales tax credits on purchases of up to \$20 million per year of qualified machinery and machinery parts;
- **Up-front expensing of certain depreciable property.** Lenders to zone businesses may receive a net interest deduction;
- **Unused tax credits** can be applied to future tax years, stretching out the benefit of the initial investment;
- **State Contracts.** Enterprise Zone companies can earn preference points on state contracts; and
- **DWP rate discount** (under certain circumstances).

In 2011, Governor Jerry Brown proposed eliminating the Enterprise Zone program, citing evidence that showed the program was not creating new jobs. The effort was eventually abandoned when the Governor did not receive support from the Legislature. This year, the Governor is taking a new strategy by focusing on making regulatory changes to the program. The California Department of Housing and Community Development (HCD), which administers the program at the State level, recently proposed changes to the program, citing an investigation which found that:

- Enterprise Zones create too few jobs. This assertion is based on a 2009 Public Policy Institute of California study that found that enterprise zones have no overall effect on job growth. Note that this finding is contentious, as it contradicts a 2010 study by the University of Maryland, USC, and the Korea Institute of Public Finance, which found that enterprise zones have positive impacts on local labor markets in terms of the unemployment rate, the poverty rate, the fraction with wage and salary income, and employment.
- Retroactive vouchering. HCD reports that 20-30 percent of the vouchers issued each year for hiring tax credits were made for hires that were made at least two years prior to the application for a voucher, which HCD uses as evidence that the hiring was not incentivized by the program. In order to claim a hiring tax credit, an employer must receive a voucher from a local enterprise zone administrator (in this case the Community Development Department) certifying that the employer has hired as “qualified employee” for a job in an enterprise zone.

HCD is proposing the following changes to the program:

- Eliminate retroactive vouchering. HCD will issue a regulation requiring voucher applications to be made within one year from an employee’s hire date. Currently, there is no deadline to apply for a voucher.

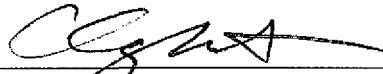
- **Eliminate self-certification for voucher applications.** The proposed regulations require Targeted Employment Area voucher applications to include utility bills, government ID, or other third-party documents demonstrating employee residency. Current regulations provide no means for local zone administrators to verify employee residency.
- **Streamline vouchering process.** HCD will make it easier for businesses to receive tax credit vouchers for hiring veterans, the disabled, and recipients of public assistance.
- **Auditing and data collection.** The State will collect data in order to evaluate the program and audit individual Enterprise Zones.

HCD reports that the new regulations will reduce the number of Enterprise Zone vouchers that are issued and save the State approximately \$40M in the first year and \$310M over the first five years of implementation. After the first five years, projections estimate annual savings of \$55M. CDD reports that the new one year deadline to file a hiring tax credit voucher following the hire date will be a further burden on businesses in Los Angeles trying to realize the tax incentives available to them. Marketing the benefits of the program to eligible businesses is difficult, and under the new rules, businesses who discover they are eligible late in the process could miss the deadline. Critics of the plan also point out that businesses often wait to file for tax credits until they are certain that the employee will remain with the company after a probationary period. The elimination of self-certification of voucher applications will also add additional burdens to businesses, which would have to demonstrate employee residency with utility bills, government ID, or other third-party documents, and not the IRS W-4 form, which had been accepted in the past. For these and other reasons, the California Chamber of Commerce and the mayors of Los Angeles, San Jose, Fresno, Santa Ana, Sacramento, San Diego, Long Beach, Oakland, Desert Hot Springs, and Anaheim all oppose portions of the State's plan.

The proposed changes to the Enterprise Zone program do include some beneficial reforms that should improve the program, notably the streamlining of the vouchering process for veterans, disabled, or recipients of public assistance; collecting data to assist with analysis; and auditing the zones to ensure accountability. Therefore, our Office recommends adoption of a revised Resolution, which seeks opposition to the proposed changes unless retroactive vouchering and self-certification rules remain unchanged.

DEPARTMENTS NOTIFIED

Community Development Department


Clay McCarter
Analyst

Attachment: 1. Revised Resolution.
2. Resolution (Englander-Huizar-Wesson).

RESOLUTION

WHEREAS, any official position of the City of Los Angeles with respect to legislation, rules, regulations, or policies proposed to or pending before a local, state or federal governmental body or agency must have first been adopted in the form of a Resolution by the City Council with the concurrence of the Mayor; and

WHEREAS, since 1984 the California Enterprise Zone program has provided businesses hiring credits, sales/use credits, and other tax incentives to stimulate business growth, attraction, and employment within economically challenged areas of the State; and

WHEREAS, the City of Los Angeles includes three enterprise zones that cover Sylmar, Warner Center, Canoga Park, Chatsworth, Northridge, Van Nuys, LAX, Hollywood, Mid-City, Koreatown, the Harbor, and Downtown; and

WHEREAS, countless numbers of businesses in these areas of Los Angeles have received hiring credits, sales and use tax credits, expense and interest deductions, DWP rate discounts, and other benefits that have resulted in significant business cost relief, promoting job growth and economic improvement in some of the City's hardest hit neighborhoods; and

WHEREAS, Enterprise Zone hiring credits are designed to encourage employers to hire people who live in disadvantaged areas, are currently on unemployment, receiving government assistance, or are veterans entering the workforce; and

WHEREAS, under the direction of Governor Jerry Brown, the State recently proposed reforming the program to eliminate the ability of businesses to retroactively apply for hiring tax credits after one year from the date of hire and eliminate self-certification for voucher applications; and

WHEREAS, these changes to the program will be devastating to thousands of Los Angeles businesses, increasing their cost of doing business, impacting their future growth plans, and potentially resulting in job losses; and

WHEREAS, in these tough economic times, the State should be looking for ways to promote the growth of business rather than saddling businesses with new costs;

NOW, THEREFORE, BE IT RESOLVED, with the concurrence of the Mayor, that by the adoption of this Resolution, the City of Los Angeles hereby includes in its 2013-2014 State Legislative Program OPPOSITION to the proposed changes to the Enterprise Zone program UNLESS AMENDED to leave retroactive vouchering and self-certification rules unchanged.

13-0002-528

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RESOLUTION

RULES, ELECTIONS & INTERGOVERNMENTAL RELATIONS

WHEREAS, any official position of the City of Los Angeles with respect to legislation, rules, regulations, or policies proposed to or pending before a local, state or federal governmental body or agency must have first been adopted in the form of a Resolution by the City Council with the concurrence of the Mayor; and

WHEREAS, since 1984 the California Enterprise Zone program has provided businesses hiring credits, sales/use credits, and other tax incentives to stimulate business growth, attraction, and employment within economically challenged areas of the State; and

WHEREAS, the City of Los Angeles includes two enterprise zones that cover Sylmar, Warner Center, Canoga Park, Chatsworth, Northridge, Van Nuys, LAX, Hollywood, Mid-City, Koreatown, and Downtown; and

WHEREAS, countless numbers of businesses in these parts of Los Angeles have received hiring credits, sales and use tax credits, expense and interest deductions, DWP rate discounts, and other benefits that have resulted in significant business cost relief, promoting job growth and economic improvement in some of the City's hardest hit neighborhoods; and

WHEREAS, Enterprise Zone hiring credits are designed to encourage employers to hire people who live in disadvantaged areas, are currently on unemployment, receiving government assistance, or are veterans entering the workforce; and

WHEREAS, during his State of the State address, Governor Jerry Brown proposed scaling back the Enterprise Zone Program by limiting the time available to apply for tax credits, remapping the zones, and reducing the amount of tax credits; and

WHEREAS, reducing or eliminating Enterprise Zone benefits will be devastating to thousands of Los Angeles businesses, increasing their cost of doing business, impacting their future growth plans, and potentially resulting in job losses; and

WHEREAS, in these tough economic times, the State should be looking for ways to promote the growth of business rather than saddling businesses with new costs;

NOW, THEREFORE, BE IT RESOLVED, with the concurrence of the Mayor, that by the adoption of this Resolution, the City of Los Angeles hereby includes in its 2013-2014 State Legislative Program OPPOSITION to any reductions, changes, or eliminations of the Enterprise Zone program.

PRESENTED BY: *M. Englander*
MITCHELL ENGLANDER
Councilmember, 12th District

SECONDED BY: *[Signature]*
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