

**INCENTIVES FOR DISTRESSED COMMUNITIES:
EMPOWERMENT ZONES AND RENEWAL COMMUNITIES**

Scheduled for a Public Hearing
Before the
SUBCOMMITTEE ON SELECT REVENUE MEASURES
of the
HOUSE COMMITTEE ON WAYS AND MEANS
on October 7, 2009

Prepared by the Staff
of the
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CONTENTS

	<u>Page</u>
INTRODUCTION AND SUMMARY	1
I. TAX INCENTIVES FOR EMPOWERMENT ZONES AND RENEWAL COMMUNITIES	3
A. Empowerment Zones	3
B. Renewal Communities	13
II. STUDIES OF PROGRAM EFFECTIVENESS	20

INTRODUCTION AND SUMMARY

The Subcommittee on Select Revenue Measures of the House Committee on Ways and Means has scheduled a public hearing for October 7, 2009, on tax incentives for distressed communities, including the empowerment zones and renewal communities programs. This document,¹ prepared by the staff of the Joint Committee on Taxation, provides a description of the present law Federal tax incentives under the Internal Revenue Code (“Code”)² for empowerment zones and renewal communities.³

Congress created two economic development programs to revitalize certain economically distressed communities across the nation: the empowerment zones⁴ program and the renewal communities⁵ program. These initiatives aim to encourage economic growth and investment in distressed areas by providing Federal tax incentives⁶ to businesses located within the designated boundaries.⁷ There are 40 areas designated as empowerment zones and 40 areas designated as renewal communities. The targeted areas are those that have pervasive poverty, high

¹ This document may be cited as follows: Joint Committee on Taxation, *Incentives for Distressed Communities: Empowerment Zones and Renewal Communities* (JCX-38-09), October 5, 2009. This document can also be found on our website at www.jct.gov.

² Except as otherwise noted, all references to sections in this document are to sections of the Code of 1986, as amended.

³ This document also describes the tax incentives available to businesses and individuals in designated areas within the District of Columbia known as the “District of Columbia Enterprise Zone.”

⁴ Empowerment zones were created by the Omnibus Budget Reconciliation Act of 1993 (“OBRA 93”), Pub. L. No. 103-66. The first empowerment zones were established in large rural areas, which received a total of \$40 million in grants, and large cities, which received a total of \$100 million in grants. OBRA 93 also authorized the designation of 95 enterprise communities, which were located in smaller rural areas and cities. Enterprise communities received an average of \$2.95 million in grants per designated area and were eligible for only one tax benefit: tax-exempt bond financing. For tax purposes, the areas designated as enterprise communities continued as such for the ten-year period starting 1995 and ending at the end of 2004. However, after 2004 the enterprise communities may still be eligible for other Federal benefits (e.g., grants and preferences). U.S. Government Accountability Office, *Empowerment Zone and Enterprise Community Program: Improvements Occurred in Communities, but the Effect of the Program is Unclear*, GAO-06-727, September 2006. The enterprise communities program is not discussed in this report other than when referenced in connection with the empowerment zones program.

⁵ Renewal communities were created by the Community Renewal Tax Relief Act of 2000, Pub. L. No. 106-554. The Secretary of Housing and Urban Development has awarded renewal community designations to 40 selected communities (12 rural and 28 urban), including areas that remained distressed after previously having received empowerment zone or enterprise community designations. To qualify as a renewal community, the community was required to have (1) a minimum unemployment rate of 9.45 percent (versus 6.3 percent for enterprise communities and empowerment zones) and (2) a maximum population of 200,000 and a minimum population of 4,000 within a metro area or 1,000 otherwise.

⁶ The empowerment zones program also provides Federal grants, as discussed below.

⁷ According to the Department of Housing and Urban Development, approximately 300,000 businesses are located in areas designated empowerment zones, enterprise communities, or renewal communities. www.hud.gov/offices/cpd/economicdevelopment/programs/rc/index.cfm

unemployment, and general economic distress, and that satisfy certain eligibility criteria, including specified poverty rates and population and geographic size limitations.

The tax incentives under the empowerment zones program include a Federal income tax credit for employers who hire qualifying employees, accelerated depreciation deductions on qualifying equipment, tax-exempt bond financing, deferral of capital gains tax on sale of qualified assets sold and replaced, and partial exclusion of capital gains tax on certain sales of qualified small business stock. The tax incentives provided under the renewal communities program include a Federal income tax credit for employers who hire qualifying employees, enhanced tax deductions on qualifying equipment and expenditures to construct or rehabilitate certain nonresidential buildings, and capital gains tax exclusion on sales of qualified assets. A chart comparing the tax benefits of the economic development programs is provided below.

These tax incentives are currently all scheduled to expire as of December 31, 2009. However, several pending legislative proposals would extend these incentives for five or ten years as well as expand the benefits for businesses operating in the designated areas.⁸ In addition, the Administration's fiscal year 2010 budget proposals include extending the tax incentives to December 31, 2010.⁹

⁸ H.R. 1677 was introduced by Rep. Artur Davis on March 24, 2009 while the companion bill, S. 1222 was introduced by Sen. Lincoln on June 9, 2009. Similar proposals have been introduced in each of the last two sessions of Congress (H.R. 2578 in the 110th Congress and H.R. 5660 in the 109th Congress) but have never been brought to a vote. H.R. 3500, a similar proposal to H.R. 1677, was introduced by Rep. Maffei on July 31, 2009.

H.R. 3100, as introduced by Rep. Rush on June 26, 2009, grants certain tax benefits to a qualified food desert business, including an increased tax credit rate for rehabilitation expenditures, empowerment zone status, and tax-exempt bond financing. H.R. 3465, as introduced by Rep. Butterfield on July 31, 2009, requires Federal agencies with excess electronic equipment ("transferring agencies") to give the highest preference to educational recipients located in an enterprise community or empowerment zone designated under the Code or a qualifying small town or county (those with certain levels of poverty). The agriculture appropriations bill, S. 1406, as introduced by Sen. Kohl on July 7, 2009, appropriates funds for Rural Development program purposes in communities suffering from extreme outmigration that are in empowerment zone-designated areas.

⁹ United States Department of the Treasury, *General Explanations of the Administration's Fiscal Year 2010 Revenue Proposals*, May 2009, p. 19.

I. TAX INCENTIVES FOR EMPOWERMENT ZONES AND RENEWAL COMMUNITIES

A. Empowerment Zones

In general

The Omnibus Budget Reconciliation Act of 1993 (“OBRA 93”) authorized the designation of nine empowerment zones (“Round I empowerment zones”) to provide tax incentives for businesses to locate within certain targeted areas designated by the Secretaries of the Department of Housing and Urban Development (“HUD”) and the U.S Department of Agriculture (“USDA”). The Taxpayer Relief Act of 1997 authorized the designation of two additional Round I urban empowerment zones, and 20 additional empowerment zones (“Round II empowerment zones”). The Community Renewal Tax Relief Act of 2000 (“2000 Community Renewal Act”) authorized a total of ten new empowerment zones (“Round III empowerment zones”), bringing the total number of authorized empowerment zones to 40.¹⁰ In addition, the 2000 Community Renewal Act conformed the tax incentives that are available to businesses in the Round I, Round II, and Round III empowerment zones, and extended the empowerment zone incentives through December 31, 2009.

Communities designated as empowerment zones are eligible for a combination of grants and tax incentives to encourage economic development. Grants have been made available by legislation. The tax incentives for empowerment zones generally are available through December 31, 2009.¹¹

The following is a description of the designation process and the tax incentives that are available within the designated empowerment zones.

¹⁰ The urban part of the program is administered by the HUD and the rural part of the program is administered by the USDA. The eight Round I urban empowerment zones are Atlanta, GA, Baltimore, MD, Chicago, IL, Cleveland, OH, Detroit, MI, Los Angeles, CA, New York, NY, and Philadelphia, PA/Camden, NJ. Atlanta relinquished its empowerment zone designation and was replaced by renewal community designation in Round III. The three Round I rural empowerment zones are Kentucky Highlands, KY, Mid-Delta, MI, and Rio Grande Valley, TX. The 15 Round II urban empowerment zones are Boston, MA, Cincinnati, OH, Columbia, SC, Columbus, OH, Cumberland County, NJ, El Paso, TX, Gary/Hammond/East Chicago, IN, and Ironton, OH/Huntington, WV. The five Round II rural empowerment zones are Desert Communities, CA, Griggs-Steele, ND, Oglala Sioux Tribe, SD, Southernmost Illinois Delta, IL, and Southwest Georgia United, GA. The eight Round III urban empowerment zones are Fresno, CA, Jacksonville, FL, Oklahoma City, OK, Pulaski County, AR, San Antonio, TX, Syracuse, NY, Tucson, AZ, and Yonkers, NY. The two Round III rural empowerment zones are Aroostook County, ME, and Futuro, TX.

¹¹ If an empowerment zone designation were terminated prior to December 31, 2009, the tax incentives would cease to be available as of the termination date.

Designation process

The first notice to apply for empowerment zone designation was issued on January 18, 1994, with applications due by June 30, 1994.¹² Applicants were required to submit a strategic plan based on four principles: economic opportunity, sustainable community development, community-based partnerships, and strategic vision for change. State and local governments and economic development corporations that were State-chartered could nominate distressed areas for designation as empowerment zones. Applications were evaluated by a review panel that delivered final recommendations to the Secretary of HUD (for urban areas) and the Secretary of USDA (for rural areas) on December 5, 1994.¹³

To be eligible for designation as a Round I urban empowerment zone an area must have satisfied the following criteria: (1) have a maximum population which is the lesser of: (a) 200,000, or (b) the greater of 50,000, or ten percent of the population of the most populous city located within the nominated area; (2) be one of pervasive poverty, unemployment, and general distress; (3) not exceed 20 square miles in total land area; (4) demonstrate a poverty rate which is not less than: (a) 20 percent in each census tract; (b) 25 percent in 90 percent of the population census tracts within the nominated area; (c) 35 percent for at least 50 percent of the population census tracts within the nominated area; (5) have a continuous boundary, or consist of not more than three noncontiguous parcels; (6) be located entirely within the jurisdiction of the unit or units of general local government making the nomination, and not be located in more than two contiguous States; and (7) not include any portion of a central business district unless the poverty rate for each population tract containing portions of the central business district is at least 35 percent for an empowerment zone.¹⁴

To be eligible for designation as a Round I rural empowerment zone an area must have satisfied the following criteria: (1) have a maximum population of 30,000; (2) be one of pervasive poverty, unemployment, and general distress; (3) not exceed 1,000 square miles in total land area; (4) demonstrate a poverty rate that is not less than: (a) 20 percent in each census tract or census block numbering area (“BNA”); (b) 25 percent in 90 percent of the population census tracts and BNAs within the nominated area; (c) 35 percent for at least 50 percent of the population census tracts and BNAs within the nominated area; (5) be located entirely within no more than three contiguous States; if it is located in more than one State, the area must have one continuous boundary; if located in only one State, the area may consist of no more than three noncontiguous parcels; (6) if the nominated area consists of noncontiguous parcels, each must independently meet the three poverty requirements; (7) be located entirely within the jurisdiction of the unit or units of general local government making the nomination; (8) not include any portion of a census-defined central business district unless the poverty rate for each population

¹² Notice Inviting Applications for Designation of Rural Empowerment Zones and Enterprise Communities, 59 F.R. 2696 (1994).

¹³ U.S. Office of the Inspector General, *Audit of Empowerment Zone, Enterprise Community and Economic Development Initiative Grant Selection Processes*, Audit Case No. 95-HQ-154-0002, 1995.

¹⁴ 24 C.F.R. Part 597.

census tract is at least 35 percent for an empowerment zone; and (9) not include any portion of an Indian reservation.¹⁵

Round II and Round III empowerment zones were subject to slightly modified eligibility criteria.¹⁶ First, the general square mileage limitations (i.e., 20 square miles for urban areas and 1,000 square miles for rural areas) were expanded to allow the empowerment zones to include an additional 2,000 acres. This additional acreage, which could be developed for commercial or industrial purposes, is not subject to the poverty rate criteria and may be divided among up to three noncontiguous parcels in the nominated area. In addition, the general requirement that at least half of the nominated area consist of census tracts with poverty rates of 35 percent or more does not apply to the Round II and III empowerment zones. However, at least 90 percent of the census tracts within a nominated area must have a poverty rate of 25 percent or more, and the remaining census tracts must have a poverty rate of 20 percent or more. For this purpose, census tracts with populations under 2,000 are treated as satisfying the 25 percent poverty rate criteria if (1) at least 75 percent of the tract was zoned for commercial or industrial use, and (2) the tract is contiguous to one or more other tracts that actually have a poverty rate of 25 percent or more. The restriction excluding areas within an Indian reservation also was removed.

Grants

Grant incentives for the empowerment zone and enterprise community programs have totaled approximately \$1.8 billion since inception. OBRA 93 authorized \$1 billion in grants to be made available through the Department of Health and Human Services to States.¹⁷ These grants are used to (1) prevent, reduce, or eliminate dependency on public assistance; (2) achieve or maintain self-sufficiency; and (3) prevent neglect, abuse, or exploitation of children and adults. Subsequent appropriations made available an additional \$436.5 million in grants through 2004.¹⁸ An additional \$300 million in grants is also available through the Department of Housing and Urban Development as Community Development Block Grants.¹⁹

¹⁵ 7 C.F.R. Part 25.

¹⁶ Sec. 1391(g)(3) and 1391(h)(3).

¹⁷ Round I urban empowerment zones received \$600 million, Round I rural empowerment zones received \$120 million, and Round I enterprise communities received \$280 million, through the Title XX Social Service Block Grant Program.

¹⁸ Pub. L. Nos. 105-277, 106-74, 106-377, 106-554, 107-73, 108-7, 108-199.

¹⁹ These grants for job creation and training, entrepreneurial activities, small business expansion, and job support services were available to two supplemental empowerment zones and four enhanced enterprise communities created by Executive Order 13005, May 21, 1996. These areas are not further discussed here.

Tax incentives for empowerment zones

Employment credit

A 20-percent wage credit is available to employers for the first \$15,000 of qualified wages paid to each employee (i.e., a maximum credit of \$3,000 with respect to each qualified employee) who (1) is a resident of the empowerment zone, and (2) performs substantially all employment services within the empowerment zone in a trade or business of the employer.²⁰

The wage credit rate applies to qualifying wages paid after December 31, 2001, and before January 1, 2010. Wages paid to a qualified employee who earns more than \$15,000 are eligible for the wage credit (although only the first \$15,000 of wages is eligible for the credit). The wage credit is available with respect to a qualified full-time or part-time employee (employed for at least 90 days), regardless of the number of other employees who work for the employer. In general, any taxable business carrying out activities in the empowerment zone may claim the wage credit, regardless of whether the employer meets the definition of an “enterprise zone business.”²¹

An employer’s deduction otherwise allowed for wages paid is reduced by the amount of wage credit claimed for that taxable year.²² Wages are not to be taken into account for purposes of the wage credit if taken into account in determining the employer’s work opportunity tax credit under section 51 or the welfare-to-work credit under section 51A.²³ In addition, the \$15,000 cap is reduced by any wages taken into account in computing the work opportunity tax credit or the welfare-to-work credit.²⁴ The wage credit may be used to offset up to 25 percent of alternative minimum tax liability.²⁵

Increased section 179 expensing limitation

An enterprise zone business is allowed an additional \$35,000 of section 179 expensing (for a total of up to \$285,000 in 2009) for qualified zone property placed in service after December 31, 2001, and before January 1, 2010.²⁶ The section 179 expensing allowed to a

²⁰ Sec. 1396.

²¹ Secs. 1397C(b) and 1397C(c). However, the wage credit is not available for wages paid in connection with certain business activities described in section 144(c)(6)(B), including a golf course, country club, massage parlor, hot tub facility, suntan facility, racetrack, or liquor store, or certain farming activities. In addition, wages are not eligible for the wage credit if paid to (1) a person who owns more than five percent of the stock (or capital or profits interests) of the employer, (2) certain relatives of the employer, or (3) if the employer is a corporation or partnership, certain relatives of a person who owns more than 50 percent of the business.

²² Sec. 280C(a).

²³ Secs. 1396(c)(3)(A) and 51A(d)(2).

²⁴ Secs. 1396(c)(3)(B) and 51A(d)(2).

²⁵ Sec. 38(c)(2).

²⁶ Sec. 1397D.

taxpayer is phased out by the amount by which 50 percent of the cost of qualified zone property placed in service during the year by the taxpayer exceeds \$500,000.²⁷ The term “qualified zone property” is defined as depreciable tangible property (including buildings) provided that (i) the property is acquired by the taxpayer (from an unrelated party) after the designation took effect, (ii) the original use of the property in an empowerment zone commences with the taxpayer, and (iii) substantially all of the use of the property is in an empowerment zone in the active conduct of a trade or business by the taxpayer. Special rules are provided in the case of property that is substantially renovated by the taxpayer.

An enterprise zone business means any qualified business entity and any qualified proprietorship. A qualified business entity means, any corporation or partnership if for such year: (1) every trade or business of such entity is the active conduct of a qualified business within an empowerment zone; (2) at least 50 percent of the total gross income of such entity is derived from the active conduct of such business; (3) a substantial portion of the use of the tangible property of such entity (whether owned or leased) is within an empowerment zone; (4) a substantial portion of the intangible property of such entity is used in the active conduct of any such business; (5) a substantial portion of the services performed for such entity by its employees are performed in an empowerment zone; (6) at least 35 percent of its employees are residents of an empowerment zone; (7) less than five percent of the average of the aggregate unadjusted bases of the property of such entity is attributable to collectibles other than collectibles that are held primarily for sale to customers in the ordinary course of such business; and (8) less than 5 percent of the average of the aggregate unadjusted bases of the property of such entity is attributable to nonqualified financial property.²⁸

A qualified proprietorship is any qualified business carried on by an individual as a proprietorship if for such year: (1) at least 50 percent of the total gross income of such individual from such business is derived from the active conduct of such business in an empowerment zone; (2) a substantial portion of the use of the tangible property of such individual in such business (whether owned or leased) is within an empowerment zone; (3) a substantial portion of the intangible property of such business is used in the active conduct of such business; (4) a substantial portion of the services performed for such individual in such business by employees of such business are performed in an empowerment zone; (5) at least 35 percent of such employees are residents of an empowerment zone; (6) less than 5 percent of the average of the aggregate unadjusted bases of the property of such individual which is used in such business is attributable to collectibles other than collectibles that are held primarily for sale to customers in the ordinary course of such business; and (7) less than 5 percent of the average of the aggregate unadjusted bases of the property of such individual which is used in such business is attributable to nonqualified financial property.²⁹

²⁷ Sec. 1397A(a)(2), 179(b)(2), (7). For 2008 and 2009, the limit is \$800,000.

²⁸ Sec. 1397C(b).

²⁹ Sec. 1397C(c).

A qualified business is defined as any trade or business other than a trade or business that consists predominantly of the development or holding of intangibles for sale or license or any business prohibited in connection with the employment credit.³⁰ In addition, the leasing of real property that is located within the empowerment zone is treated as a qualified business only if (1) the leased property is not residential property, and (2) at least 50 percent of the gross rental income from the real property is from enterprise zone businesses. The rental of tangible personal property is not a qualified business unless at least 50 percent of the rental of such property is by enterprise zone businesses or by residents of an empowerment zone.

Expanded tax-exempt financing for certain zone facilities

States or local governments can issue enterprise zone facility bonds to raise funds to provide an enterprise zone business with qualified zone property.³¹ These bonds can be used in areas designated enterprise communities as well as areas designated empowerment zones. To qualify, 95 percent (or more) of the net proceeds from the bond issue must be used to finance: (1) qualified zone property whose principal user is an enterprise zone business, and (2) certain land functionally related and subordinate to such property.

The term enterprise zone business is the same as that used for purposes of the increased section 179 deduction limitation (discussed above) with certain modifications for start-up businesses. First, a business will be treated as an enterprise zone business during a start-up period if (1) at the beginning of the period, it is reasonable to expect the business to be an enterprise zone business by the end of the start-up period, and (2) the business makes bona fide efforts to be an enterprise zone business. The start-up period is the period that ends with the start of the first tax year beginning more than two years after the later of (1) the issue date of the bond issue financing the qualified zone property, and (2) the date this property is first placed in service (or, if earlier, the date that is three years after the issue date).³²

Second, a business that qualifies as at the end of the start-up period must continue to qualify during a testing period that ends three tax years after the start-up period ends. After the three-year testing period, a business will continue to be treated as an enterprise zone business as long as 35 percent of its employees are residents of an empowerment zone or enterprise community.

The face amount of the bonds may not exceed \$60 million for an empowerment zone in a rural area, \$130 million for an empowerment zone in an urban area with zone population of less than 100,000, and \$230 million for an empowerment zone in an urban area with zone population of at least 100,000.

³⁰ Sec. 1397C(d). Excluded businesses include any private or commercial golf course, country club, massage parlor, hot tub facility, sun tan facility, racetrack, or other facility used for gambling or any store the principal business of which is the sale of alcoholic beverages for off-premises consumption. Sec. 144(c)(6).

³¹ Sec. 1394.

³² Sec. 1394(b)(3).

Elective roll over of capital gain from the sale or exchange of any qualified empowerment zone asset purchased after December 21, 2000

Taxpayers can elect to defer recognition of gain on the sale of a qualified empowerment zone asset³³ held for more than one year and replaced within 60 days by another qualified empowerment zone asset in the same zone.³⁴ The deferral is accomplished by reducing the basis of the replacement asset by the amount of the gain recognized on the sale of the asset.

Partial exclusion of capital gains on certain small business stock

For taxpayers other than corporations, 50 percent of the gain from the sale of qualified small business stock held for more than five years is excluded from gross income.³⁵ In the case of qualified small business stock acquired after December 21, 2000, in a corporation which is a qualified business entity (as defined in section 1397C(b)) during substantially all of the taxpayer's holding period, the exclusion is increased to 60 percent.³⁶

For all qualified small business stock acquired after February 17, 2009, and before January 1, 2011, the exclusion is increased to 75 percent.

Other tax incentives

Other incentives not specific to empowerment zones but beneficial to these areas include the work opportunity tax credit for employers based on the first year of employment of certain targeted groups, including empowerment zone residents (up to \$2,400 per employee), and qualified zone academy bonds for certain public schools located in an empowerment zone, or expected (as of the date of bond issuance) to have at least 35 percent of its students receiving free or reduced lunches.

³³ The term "qualified empowerment zone asset" means any property which would be a qualified community asset (as defined in section 1400F, relating to certain tax benefits for renewal communities) if in section 1400F—(i) references to empowerment zones were substituted for references to renewal communities, (ii) references to enterprise zone businesses (as defined in section 1397C) were substituted for references to renewal community businesses, and (iii) the date of the enactment of this paragraph were substituted for "December 31, 2001" each place it appears. Sec. 1397B(b)(1)(A).

A "qualified community asset" includes: (1) qualified community stock (meaning original-issue stock purchased for cash in an enterprise zone business), (2) a qualified community partnership interest (meaning a partnership interest acquired for cash in an enterprise zone business), and (3) qualified community business property (meaning tangible property originally used in a enterprise zone business by the taxpayer) that is purchased or substantially improved after the date of the enactment of this paragraph.

For the definition of "enterprise zone business," see text accompanying *supra* notes 28-29. For the definition of "qualified business," see text accompanying *supra* note 30.

³⁴ Sec. 1397B.

³⁵ Sec. 1202.

³⁶ The increased exclusion does not apply to gain attributable to periods after December 31, 2014.

Extension of work opportunity tax credit

The work opportunity tax credit is available on an elective basis for employers hiring individuals from one or more statutorily defined targeted groups, including “designated community residents.”³⁷ The amount of the credit available to an employer is determined by the amount of qualified wages paid by the employer. Generally, qualified wages consist of wages attributable to service rendered by a member of a targeted group during the one-year period beginning with the day the individual begins work for the employer (two years in the case of an individual in the long-term family assistance recipient category).

A designated community resident is an individual certified as being at least age 18 but not yet age 40 on the hiring date and as having a principal place of abode within an empowerment zone, enterprise community, renewal community or a rural renewal community. For these purposes, a rural renewal community is a county outside a metropolitan statistical area (as defined by the Office of Management and Budget) which had a net population loss during the five-year periods 1990-1994 and 1995-1999. Qualified wages do not include wages paid or incurred for services performed after the individual moves outside an empowerment zone, enterprise community, renewal community, or a rural renewal community.³⁸

The credit available to an employer for qualified wages paid to members of all targeted groups except for long-term family assistance recipients equals 40 percent (25 percent for employment of 400 hours or less) of “qualified first-year wages.” Generally, qualified first-year wages are qualified wages (not in excess of \$6,000) attributable to service rendered by a member of a targeted group during the one-year period beginning with the day the individual began work for the employer. Therefore, the maximum credit per employee is \$2,400 (40 percent of the first \$6,000 of qualified first-year wages).

The credit generally expires for individuals who begin work for the employer after August 31, 2011.

Qualified zone academy bonds

As an alternative to traditional tax-exempt bonds, States and local governments are given the authority to issue “qualified zone academy bonds,” a type of tax-credit bond to benefit certain public schools, including those located in empowerment zones.³⁹ A total of \$1.4 billion of qualified zone academy bonds is authorized to be issued annually for calendar years 2009 and 2010. The aggregate bond cap is allocated each year among the States according to their respective populations of individuals below the poverty line. Each State, in turn, allocates the credit authority to qualified zone academies within such State.

³⁷ Sec. 51(d).

³⁸ Sec. 51(d)(5).

³⁹ Secs. 54E and 1397E. For calendar years 1998 through 2008, the annual cap was \$400 million.

“Qualified zone academy bonds” are defined as any bond issued by a State or local government, provided that (1) 100 percent of the proceeds are used for the purpose of renovating, providing equipment to, developing course materials for use at, or training teachers and other school personnel in a “qualified zone academy,” and (2) private entities have promised to contribute to the qualified zone academy certain equipment, technical assistance or training, employee services, or other property or services with a value equal to at least ten percent of the bond proceeds.⁴⁰

A school is a “qualified zone academy” if (1) the school is a public school that provides education and training below the college level, (2) the school operates a special academic program in cooperation with businesses to enhance the academic curriculum and increase graduation and employment rates, and (3) either (a) the school is located in an empowerment zone or enterprise community designated under the Code, or (b) it is reasonably expected that at least 35 percent of the students at the school will be eligible for free or reduced-cost lunches under the school lunch program established under the National School Lunch Act.⁴¹

A taxpayer holding a qualified zone academy bond is entitled to an income tax credit. The nonrefundable credit is includible in gross income (as if it were a taxable interest payment on the bond), and may be claimed against regular income tax and alternative minimum tax liability.⁴²

District of Columbia Enterprise Zone

The Taxpayer Relief Act of 1997⁴³ designated certain economically depressed census tracts within the District of Columbia as the “District of Columbia Enterprise Zone,” or “DC Zone,” within which businesses and individual residents are eligible for special tax incentives. The census tracts that comprise the District of Columbia Enterprise Zone are (1) all census tracts that presently are part of the D.C. enterprise community designated under section 1391 (i.e., portions of Anacostia, Mt. Pleasant, Chinatown, and the easternmost part of the District of Columbia), and (2) all additional census tracts within the District of Columbia where the poverty rate is not less than 20 percent. The District of Columbia Enterprise Zone designation remains in effect for the period from January 1, 1998, through December 31, 2009.

The following tax incentives previously described in connection with empowerment zones are available in the District of Columbia Enterprise Zone: (1) 20-percent wage credit;⁴⁴

⁴⁰ Sec. 54E.

⁴¹ Sec. 54E(d)(1).

⁴² Sec. 54A(a)(f). The tax credit is calculated by multiplying the applicable credit rate by the face amount of the bond. The Treasury sets a credit rate each calendar month that allows the bonds to be issued without discount or interest cost to the issuer.

⁴³ Pub. L. No. 105-34.

⁴⁴ Unlike the empowerment zone employment credit, this credit is available to employers for the first \$15,000 of qualified wages paid to each employee, regardless of whether the qualified employee is a resident of the

(2) an additional \$35,000 of section 179 expensing for qualified zone property; and (3) expanded tax-exempt financing for certain zone facilities.⁴⁵

In addition, a zero-percent capital gains rate applies to capital gains from the sale of certain qualified DC Zone assets held for more than five years.⁴⁶ In general, a “qualified DC Zone asset” means stock or partnership interests held in, or tangible property held by, a DC Zone business. For purposes of the zero-percent capital gains rate, the DC Zone is defined to include all census tracts within the District of Columbia where the poverty rate is not less than ten percent.

In general, gain eligible for the zero-percent tax rate is that from the sale or exchange of a qualified DC Zone asset that is (1) a capital asset or (2) property used in a trade or business, as defined in section 1231(b). Gain that is attributable to real property, or to intangible assets, qualifies for the zero-percent rate, provided that such real property or intangible asset is an integral part of a qualified DC Zone business.⁴⁷ However, no gain attributable to periods before January 1, 1998, and after December 31, 2014, is qualified capital gain.

DC Zone. An employer is entitled to the credit as long as the qualified employee lives in the District of Columbia. Secs. 1396, 1400(d), 1400(e).

⁴⁵ A qualified DC Zone business is permitted to borrow proceeds from the issuance of qualified enterprise zone facility bonds by the District of Columbia. The issuance of such bonds is subject to the District's annual private activity bond volume limitation; and, the aggregate face amount of all outstanding qualified enterprise zone facility bonds per qualified DC Zone business may not exceed \$15 million. These bonds may only be issued while the DC Zone designation is in effect.

⁴⁶ Sec. 1400B.

⁴⁷ However, sole proprietorships and other taxpayers selling assets directly cannot claim the zero-percent rate on capital gain from the sale of any intangible property (i.e., the integrally related test does not apply).

B. Renewal Communities

Some of the provisions that target specific geographic areas for special Federal income tax treatment are part of the renewal community incentive, enacted in December 2000 as part of the 2000 Community Renewal Act.⁴⁸ These special tax incentives, like the ones for the empowerment zones discussed above, are designed to attract business and investment to distressed urban and rural areas.

The 2000 Community Renewal Act authorized the designation of 40 “renewal communities” within which special tax incentives are available. The tax incentives for renewal communities generally are available through December 31, 2009.⁴⁹ The following is a description of the designation process and the tax incentives that are available within the designated renewal communities.

Designation process

On January 24, 2002, HUD designated 40 communities as renewal communities from areas nominated by States and local governments. Twenty-eight of the communities are located in urban areas; twelve are located in rural areas.⁵⁰

The designation of an area as a renewal community generally became effective on January 1, 2002, and will terminate after December 31, 2009.⁵¹

⁴⁸ For legislative background of these provisions, see H. Rep. 106-1033 (Dec. 15, 2000), at 977-1000, and H. Rep. 106-1004 (Oct. 26, 2000) that accompanied H.R. 2614, at 330-353. H.R. 2614 was passed by the House of Representatives on October 26, 2000, but was not brought to a vote in the Senate.

Charged with auditing the renewal community program, the GAO included a detailed description of the renewal community program implementation in its 2004 report. U.S. General Accounting Office, *Community Development: Federal Revitalization Programs Are Being Implemented, but Data on the Use of Tax Benefits Are Limited*, GAO-04-306, (Mar. 2004). On July 7, 2004, the General Accounting Office was renamed the Government Accountability Office. The abbreviation GAO as used herein refers to the General Accounting Office for documents published before July 7, 2004, and to the Government Accountability Office for documents published on or after such date.

⁴⁹ If a renewal community designation is terminated prior to December 31, 2009, the tax incentives cease to be available as of the termination date.

⁵⁰ The 28 urban renewal communities are: Mobile, AL; Los Angeles, San Diego, and San Francisco, CA; Atlanta, GA; Chicago, IL; New Orleans and Ouachita Parish, LA; Lawrence and Lowell, MA; Detroit and Flint, MI; Camden and Newark, NJ; Buffalo-Lackawanna, Niagara Falls, Rochester, and Schenectady, NY; Hamilton and Youngstown, OH; Philadelphia, PA; Charleston, SC; Chattanooga and Memphis, TN; Corpus Christi, TX; Tacoma and Yakima, WA; and Milwaukee, WI.

The 12 rural renewal communities are: Greene-Sumter, AL; Southern Alabama; Orange Cove and Parlier, CA; Eastern Kentucky; Central and Northern Louisiana; West-Central Mississippi; Turtle Mountain Band of Chippewa, ND; Jamestown, NY; El Paso County, TX; and Burlington, VT.

To be designated as a renewal community, a nominated area must satisfy the following criteria: (1) each census tract must have a poverty rate of at least 20 percent;⁵² (2) in the case of an urban area, at least 70 percent of the households have incomes below 80 percent of the median income of households within the local government jurisdiction; (3) the unemployment rate is at least 1.5 times the national unemployment rate; and (4) the area is one of pervasive poverty, unemployment, and general distress. The designations were based on a ranking of eligibility factors (1), (2), and (3) above. The Secretary of HUD was required to take into account in selecting areas for designation the extent to which such areas have a high incidence of crime, as well as whether the area has census tracts identified in the May 12, 1998, report of the General Accounting Office (“GAO”) regarding the identification of economically distressed areas. In lieu of the poverty, income, and unemployment criteria, out-migration may be taken into account in the designation of one rural renewal community.

No geographic size limitations are placed on renewal communities. Instead, the boundary of a renewal community must be continuous. In addition, the renewal community must have a minimum population of 4,000 if the community is located within a metropolitan statistical area (at least 1,000 in all other cases), and a population of not more than 200,000. The population limitations do not apply to any renewal community that is entirely within an Indian reservation.

Required State and local commitments

For an area to be designated as a renewal community, State and local governments were required to submit a written course of action in which the State and local governments promised to take at least four of the following governmental actions within the nominated area: (1) a reduction of tax rates or fees; (2) an increase in the level of efficiency of local services; (3) crime reduction strategies; (4) actions to remove or streamline governmental requirements; (5) involvement by private entities and community groups, such as providing jobs and job training and financial assistance; and (6) the gift (or sale at below fair market value) of surplus real estate by the State or local government to community organizations or private companies.⁵³

In addition, the nominating State and local governments must have promised to promote economic growth in the nominated area by repealing or not enforcing four of the following: (1) licensing requirements for occupations that do not ordinarily require a professional degree; (2) zoning restrictions on home-based businesses that do not create a public nuisance; (3) permit requirements for street vendors who do not create a public nuisance; (4) zoning or other restrictions that impede the formation of schools or child care centers; and (5) franchises or other restrictions on competition for businesses providing public services, including but not limited to

⁵¹ The designation would terminate earlier than December 31, 2009, if (1) an earlier termination date is so designated by the State or local government, or (2) the Secretary of HUD revokes the designation as of an earlier date.

⁵² Determined using 1990 census data.

⁵³ Sec. 1397E(d)(2).

taxicabs, jitneys, cable television, or trash hauling, unless such regulations are necessary for and well-tailored to the protection of health and safety.⁵⁴

Empowerment zones and enterprise communities seeking designation as renewal communities

With respect to the first 20 designations of nominated areas as renewal communities, preference was given to nominated areas that were empowerment zones and enterprise communities that otherwise met the requirements for designation as a renewal community. If a renewal community designation was granted, then an area's designation as an empowerment zone or enterprise community ceased as of the date the area's designation as a renewal community.

Tax incentives for renewal communities

The following tax incentives generally are available during the period beginning January 1, 2002, and ending December 31, 2009.⁵⁵

Renewal community employment credit

A 15-percent wage credit is available to employers for the first \$10,000 of qualified wages paid to each employee (i.e., a maximum credit of \$1,500 with respect to each qualified employee) who (1) is a resident of the renewal community, and (2) performs substantially all employment services within the renewal community in a trade or business of the employer.⁵⁶

The wage credit applies to qualifying wages paid after December 31, 2001, and before January 1, 2010. Wages paid to a qualified employee who earns more than \$10,000 are eligible for the wage credit (although only the first \$10,000 of wages is eligible for the credit). The wage credit is available with respect to a qualified full-time or part-time employee, employed for at least 90 days, regardless of the number of other employees who work for the employer. In general, any taxable business carrying out activities in the renewal community may claim the wage credit, regardless of whether the employer meets the definition of a "renewal community business."⁵⁷

⁵⁴ Sec. 1397E(d)(3).

⁵⁵ If a renewal community designation is terminated prior to December 31, 2009, the tax incentives cease to be available as of the termination date.

⁵⁶ Sec. 1400H. This section treats a renewal community as an empowerment zone for purposes of section 1396 with respect to wages paid or incurred after December 31, 2001, subject to modifications of the applicable percentage amount (15 percent instead of 20 percent) and the qualified wage amount (\$10,000 instead of \$15,000).

⁵⁷ Sec. 1400G. However, the wage credit is not available for wages paid in connection with certain business activities described in section 144(c)(6)(B) or certain farming activities. In addition, wages are not eligible for the wage credit if paid to (1) a person who owns more than 5 percent of the stock (or capital or profits interests) of the employer, (2) certain relatives of the employer, or (3) if the employer is a corporation or partnership, certain relatives of a person who owns more than 50 percent of the business.

An employer's deduction otherwise allowed for wages paid is reduced by the amount of wage credit claimed for that taxable year.⁵⁸ Wages are not to be taken into account for purposes of the wage credit if taken into account in determining the employer's work opportunity tax credit under section 51 or the welfare-to-work credit under section 51A.⁵⁹ In addition, the \$10,000 cap is reduced by any wages taken into account in computing the work opportunity tax credit or the welfare-to-work credit.⁶⁰ The wage credit may be used to offset up to 25 percent of alternative minimum tax liability.⁶¹

Additional section 179 expensing

A renewal community business (as defined below in connection with the zero-percent capital gains rate) is allowed an additional \$35,000 of section 179 expensing for qualified renewal property placed in service after December 31, 2001, and before January 1, 2010.⁶² The section 179 expensing allowed to a taxpayer is phased out by the amount by which 50 percent of the cost of qualified renewal property placed in service during the year by the taxpayer exceeds \$500,000.⁶³

The term "qualified renewal property" is defined as depreciable tangible property (including buildings), provided that (1) the property is acquired by the taxpayer (from an unrelated party) after the designation took effect, (2) the original use of the property in the renewal community commences with the taxpayer, and (3) substantially all of the use of the property is in the renewal community in the active conduct of a trade or business by the taxpayer.⁶⁴ Special rules are provided in the case of property that is substantially renovated by the taxpayer.

Commercial revitalization deduction

Each State is permitted to allocate up to \$12 million of commercial revitalization expenditures to each renewal community located within the State for each calendar year after 2001 and before 2010. The appropriate State agency will make the allocations pursuant to a qualified allocation plan.⁶⁵

⁵⁸ Sec. 280C(a).

⁵⁹ Secs. 1400H(a), 1396(c)(3)(A) and 51A(d)(2).

⁶⁰ Secs. 1400H(a), 1396(c)(3)(B) and 51A(d)(2).

⁶¹ Sec. 38(c)(2).

⁶² Sec. 1400J.

⁶³ Sec. 1400J, 179(b)(2), 179(b)(7). For 2008 and 2009, the limit is \$800,000.

⁶⁴ Secs. 1400J(b), 1397D.

⁶⁵ Sec. 1400I.

A commercial revitalization expenditure means the cost of a new building or the cost of substantially rehabilitating an existing building. The building must be used for commercial purposes and be located in a renewal community. In the case of the rehabilitation of an existing building, the cost of acquiring the building will be treated as a qualifying expenditure only to the extent that such costs do not exceed 30 percent of the other rehabilitation expenditures. The qualifying expenditures for any building cannot exceed \$10 million.

A taxpayer can elect either to (a) deduct one-half of the commercial revitalization expenditures for the taxable year the building is placed in service or (b) amortize all the expenditures ratably over the 120-month period beginning with the month the building is placed in service.⁶⁶ No depreciation is allowed for amounts deducted under this provision. The adjusted basis of the building is reduced by the amount of the commercial revitalization deduction, and the deduction is treated as a depreciation deduction in applying the depreciation recapture rules.

The commercial revitalization deduction is treated in the same manner as the low-income housing credit in applying the passive loss rules. Thus, up to \$25,000 of deductions (together with the other deductions and credits not subject to the passive loss limitation by reason of section 469(i)) are allowed to an individual taxpayer regardless of the taxpayer's adjusted gross income. The commercial revitalization deduction is allowed in computing a taxpayer's alternative minimum taxable income.

Zero-percent capital gains rate

A zero-percent capital gains rate applies with respect to gain from the sale of a qualified community asset acquired after December 31, 2001, and before January 1, 2010, and held for more than five years.⁶⁷ A qualified community asset includes: (1) qualified community stock (meaning original-issue stock purchased for cash in a renewal community business); (2) a qualified community partnership interest (meaning a partnership interest acquired for cash in a renewal community business); and (3) qualified community business property (meaning tangible property originally used in a renewal community business by the taxpayer) that is purchased or substantially improved after December 31, 2001.

A renewal community business is defined as a corporation or partnership (or proprietorship) if for the taxable year (1) the sole trade or business of the corporation or partnership is the active conduct of a qualified business⁶⁸ within a renewal community; (2) at

⁶⁶ Sec. 1400I.

⁶⁷ Sec. 1400F.

⁶⁸ A qualified business is defined as any trade or business other than a trade or business that consists predominantly of the development or holding of intangibles for sale or license. In addition, the leasing of real property that is located within the renewal community is treated as a qualified business only if (1) the leased property is not residential property, and (2) at least 50 percent of the gross rental income from the real property is from renewal community businesses. The rental of tangible personal property is not a qualified business unless at least 50 percent of the rental of such property is by enterprise zone businesses or by residents of a renewal community.

least 50 percent of the total gross income is derived from the active conduct of a “qualified business” within a renewal community; (3) a substantial portion of the business’s tangible property is used within a renewal community; (4) a substantial portion of the business’s intangible property is used in the active conduct of such business; (5) a substantial portion of the services performed by employees are performed within a renewal community; (6) at least 35 percent of the employees are residents of the renewal community; and (7) less than 5 percent of the average of the aggregate unadjusted bases of the property owned by the business is attributable to (a) certain financial property, or (b) collectibles not held primarily for sale to customers in the ordinary course of an active trade or business. Property will continue to be a qualified community asset if sold (or otherwise transferred) to a subsequent purchaser, provided that the property continues to represent an interest in (or tangible property used in) a renewal community business.

The termination of an area’s status as a renewal community will not affect whether property is a qualified community asset, but any gain attributable to the period before January 1, 2002, or after December 31, 2014, is not eligible for the zero-percent rate.

Other tax incentives

See the discussion in section I.A for a description of the work opportunity tax credit, which is also available in renewal communities.⁶⁹

⁶⁹ In addition, although not specific to renewal communities, qualified zone academy bonds, also discussed above, could be used in a renewal community if a public school in the renewal community was expected (as of the date of bond issuance) to have at least 35 percent of its students receiving free or reduced lunches.

**Federal Tax Incentives Available for the Empowerment
Zones and Renewal Communities Programs**

Type of Benefit ¹	Empowerment Zones (EZ)	Renewal Communities (RC)
Credits		
EZ Employment Credit (annual credit of up to \$3,000 per employee living in the EZ)	X	
RC Employment Credit (annual credit of up to \$1,500 per employee living in RC)		X
Deductions		
Increased Section 179 Deduction (expense up to \$285,000 qualified assets in the year purchased)	X	X
Commercial Revitalization Deduction (deduction of either one-half of expenditures in first year building placed in service or all expenditures over ten years)		X
Bond Financing		
Enterprise Zone Facility Bonds	X	
Capital Gains		
Capital Gain Exclusion for RC Assets (exclude gain from qualified assets held at least 5-years)		X
Rollover of Gain from Sale of EZ Assets (no gain from sale of qualified assets held more than 1-year and replaced within 60 days)	X	
Increased Exclusion of Gain from Qualified Small Business Stock (exclude 60 percent of gain from sale of stock held more than 5 years; 75 percent for stock acquired after 2/17/2009 and before 1/1/2011)	X	

¹ Other incentives not specifically listed but beneficial to these areas include the work opportunity tax credit for employers based on the first year of employment of certain targeted groups, including empowerment zone and renewal community residents (up to \$2,400 per employee), and qualified zone academy bonds for certain public schools located in an empowerment zone, or expected (as of the date of bond issuance) to have at least 35 percent of its students receiving free or reduced lunches (\$1.4 billion for 2009 and 2010).

II. STUDIES OF PROGRAM EFFECTIVENESS

Department of Housing and Urban Development

HUD has not published any comprehensive study of the empowerment zones and renewal communities programs. However, in 2001, it published an interim assessment based on the initial years of the program.⁷⁰ The report was titled an “interim” assessment because it studied only the first five years of the ten-year program. No subsequent “final” assessment has yet been issued by HUD.⁷¹

HUD’s interim assessment studied the performance of six urban Round I empowerment zones and 12 urban enterprise communities over the first five years of the empowerment zone/enterprise community program. The report analyzed performance based on four metrics: economic opportunity, community-based partnerships, sustainable community development, and strategic vision for change. Applicants for empowerment zone designation were required to incorporate these four principles into the strategic plans submitted with their applications.

HUD made several findings consistent with a positive impact by the empowerment zone/enterprise community program: in aggregate, job growth accelerated in the six empowerment zones; job growth in four of the six empowerment zones outpaced job growth in comparison areas; the number of both empowerment zone resident-owned and minority-owned businesses increased substantially across all six empowerment zones; and workforce development activities created as many as 16,000 jobs for empowerment zone/enterprise community residents.

On the other hand, other findings were consistent with little or no positive impact. During the period studied, there was a general economic upturn, making it difficult to attribute employment growth to the empowerment zone/enterprise community program. In some empowerment zones, employment increases may have been attributable to nonempowerment zone activities. Of the businesses in the six empowerment zones, only 11 percent reported using empowerment zone employment credits, four percent reported using section 179 expensing, and three percent reported using work opportunity tax credits, while 65 percent of all empowerment zone businesses reported no benefits from being located in the empowerment zone.

Ultimately, the HUD study’s mixed results were inconclusive and did not show that the empowerment zone/enterprise community program causes community improvement.

⁷⁰ U.S. Department of Housing and Urban Development, *Interim Assessment of the Empowerment Zones and Enterprise Communities (EZ/EC) Program: A Progress Report*, November 2001.

⁷¹ In 2006, HUD published *Spotlight on Results*, an anecdotal report of the empowerment zone/enterprise community/renewal community programs' success. U.S. Department of Housing and Urban Development, *Spotlight on Results: Capturing Successes in Renewal Communities and Empowerment Zones*, May 2006. Through numerous stories and photos of individual community initiatives and projects, the report “highlights the successes of the tax incentives and celebrates successful programs and projects taking place in RCs and EZs.” *Ibid.*, p. iii.

Government Accountability Office

In accordance with the Community Renewal Tax Relief Act of 2000,⁷² which mandated that GAO issue reports of the empowerment zone/enterprise community programs and the renewal community program in 2004, 2007, and 2010, GAO has published periodic audits focusing on the programs' effects on poverty, unemployment, and economic growth.⁷³

In its 2004 report, GAO found that the IRS did not collect sufficient data on the use of many of the empowerment zone/enterprise community and renewal community tax benefits.⁷⁴ It consequently found it impossible to study the overall impact of the empowerment zone/enterprise community program and renewal community program, and it recommended better data collection.⁷⁵

GAO's most recent report concluded that the effects of Round I empowerment zone/enterprise community designation on community improvement were unclear.⁷⁶ GAO noted that the Department of Health and Human Services ("HHS"), HUD, and the United States Department of Agriculture ("USDA")—the three agencies that oversee the spending of grant funds under the empowerment zone/enterprise community program—had failed to collect data on how the grant funds were used.⁷⁷ Similarly, GAO found only limited data on the use of tax benefits, noting that HUD, USDA, and IRS had failed to reach agreement on a cost-effective approach to collect data and to identify standards for evaluating the effectiveness of those tax benefits.⁷⁸

⁷² Pub. L. No. 106-554.

⁷³ Prior to the creation in 2000 of renewal communities, GAO issued reports about the use of tax incentives by empowerment zones and enterprise communities. See U.S. General Accounting Office, *Community Development: Information on the Use of Empowerment Zone and Enterprise Community Tax Incentives*, GAO-98-203, June 1998; U.S. General Accounting Office, *Community Development: Businesses' Use of Empowerment Zone Tax Incentives*, GAO-99-253, September 1999.

⁷⁴ The report describes renewal communities but does not analyze their effectiveness. U.S. General Accounting Office, *Community Development: Federal Revitalization Programs Are Being Implemented, but Data on the Use of Tax Benefits Are Limited*, GAO-04-306, March 2004, p. 45.

⁷⁵ *Ibid.*, p. 45-46.

⁷⁶ U.S. Government Accountability Office, *Empowerment Zone and Enterprise Community Program: Improvements Occurred in Communities, but the Effect of the Program is Unclear*, GAO-06-727, September 2006, p. 4. While the report briefly mentioned renewal communities, it focused its analysis on the empowerment zone and enterprise community programs, since more data (dating back to 1994) existed for those programs.

⁷⁷ "HHS did not provide the states, EZs, and ECs with clear guidance on how to monitor the program grant funds, so the types and extent of monitoring performed by state and local participants varied. To some extent, the lack of reporting requirements may be an outcome of the program's design, which was intended to give communities flexibility in using program funds and relied on multiple agencies for oversight. But the result has been that little information is available on the amount of funds spent on specific activities, hindering the agencies' efforts to oversee the program." *Ibid.*, p. 4.

⁷⁸ *Ibid.*

Using available data on the eight Round I empowerment zones, GAO conducted a statistical study of economic data to measure the economic impact of empowerment zone/enterprise community designation. It found that “although improvements in poverty, unemployment, and economic growth had occurred,” the analysis “could not tie these changes definitively to the empowerment zone designation.”⁷⁹ The lack of data, combined with the difficulty of determining which changes would have occurred in each area in the absence of empowerment zone/enterprise community designation, made measurement of program impact particularly difficult.

Among its concluding observations, the GAO recommended that if Congress authorizes similar programs in the future, it should address limitations in agency oversight and coordination and the limited ability to evaluate program effectiveness due to insufficient data.⁸⁰

Economic literature

The economic literature assessing the impact of Federal empowerment zones is limited.⁸¹ In general, these studies have found modest effects overall with relatively high costs. Another issue is the difficulty of identifying which aspects of zone designation, grants or tax incentives, may be responsible for any observed increases in economic activity.

One study examined the Federal empowerment zones in Baltimore, Chicago, Detroit, and New York and found that, while poverty and unemployment decrease in some zone areas, similar changes occurred in comparison areas that did not receive the empowerment zone designation, suggesting that changes within zones are consistent with citywide economic trends. Overall the authors found no statistically significant change in income, unemployment, or poverty.⁸²

⁷⁹ *Ibid.*, p. 5. The report observes that nonempowerment zone areas used for comparison often had similar decreases in poverty and unemployment and increases in economic growth. In addition, the decrease in poverty within some empowerment zones was likely attributable to low-income residents moving out of the empowerment zone and being replaced by higher-income individuals.

⁸⁰ *Ibid.*, pp. 5-6, 48-49.

⁸¹ A number of studies have examined the effects of similar State programs, most of which preceded the Federal initiatives. See, e.g., Leslie E. Papke, “Tax Policy and Urban Development: Evidence from the Indiana Enterprise Zone Program,” *Journal of Public Economics*, 54, May 1994, pp. 37-49. For a review of the early literature, see Alan. H. Peters and Peter S. Fisher, *State Enterprise Zone Programs: Have They Worked?* Kalamazoo, MI: W.E. Upjohn Institute for Employment Research, 2002. For a more recent review, see Joel A. Elvery, “The Impact of Enterprise Zones on Resident Employment,” *Economic Development Quarterly*, 23, February 2009, pp. 44-59. We are unaware of economic literature assessing the impact of the tax benefits under the renewal community program.

⁸² Dierdre Oakley and Hui-shien Tsao, “A New Way of Revitalizing Distressed Urban Communities? Assessing the Impact of the Federal Empowerment Zone Program,” *Journal of Urban Affairs*, 28, November 2006, pp. 443-471.

Another study suggests that these overall modest or insignificant effects may mask countervailing effects on different subsets of firms.⁸³ Increases in employment, sales, and capital expenditures in new and existing establishments may be mostly offset by losses in employment, sales, and capital expenditures among firms that close or leave the zone. The authors note that if this churning of employment improves the desirability of living or locating a business in an empowerment zone, this benefit may be capitalized into local property values and zone effectiveness may be evaluated by estimating increases in property values.⁸⁴

Other researchers have found significant increases in property values within zones. One study found median home value appreciation in Round I empowerment zones was 25 percent faster than it would have been without the program.⁸⁵ The authors suggest that this effect may be a result of improved amenities (such as better services, lower crime, better infrastructure, or better access to employment), a reduction in the supply of low-quality housing, and/or an increase in the demand for commercial real estate to access program benefits, which could drive up the price of residential property.

Another study found that housing values increased by approximately 22 percent while rents increased by approximately seven percent, suggesting an overall increase in housing wealth within the Round I urban zones of approximately \$1.2 billion.⁸⁶ The authors also found that employment increased four percentage points while unemployment and poverty decreased by similar amounts. This translates into an increase in empowerment zone employment of approximately 30,000, a decrease in unemployment of approximately 13,000 individuals, and a decrease in the poverty headcount of around 50,000 individuals.

One critique noted that previously employed renters within an empowerment zone may be financially worse off as rents rise while earnings do not.⁸⁷ The authors also pointed out that the cost of empowerment zone incentives per year per job created is likely relatively high. They suggest that place-based initiatives can be justified only if the targeted areas exhibit stronger economies of scale in production and consumption than other areas, the evidence of which is absent, and that a more effective approach is to reconsider policies that require local businesses and workers to pay for local redistribution and to limit land use restrictions in high-income, high-productivity areas.

⁸³ Danielle Bondonio and Robert T. Greenbaum, "Do Local Tax Incentives Affect Economic Growth? What Mean Impacts Miss in the Analysis of Enterprise Zone Policies," *Regional Science and Urban Economics*, 37, 2007, pp. 121-136.

⁸⁴ *Ibid.*, p. 133.

⁸⁵ Douglas J. Krupka and Douglas S. Noonan, "Empowerment Zones, Neighborhood Change and Owner-Occupied Housing," *Regional Science and Urban Economics*, 39, 2009, pp. 386-396.

⁸⁶ Matias Busso and Patrick Kline, "Do Local Economic Development Programs Work? Evidence from the Federal Empowerment Zone Program," Cowles Foundation Discussion Paper No. 1638; Yale Economics Department Working Paper No. 36, February 2008.

⁸⁷ Edward L. Glaeser and Joshua D. Gottlieb, "The Economics of Place-Making Policies," *Brookings Papers on Economic Activity*, 2008, No. 1, pp. 155-239.