



NEW LAW REVOKES EMPIRE ZONE CERTIFICATIONS AND INTERPRETATION SEEKS TO APPLY REVOCATIONS RETROACTIVELY

On April 7, 2009 Governor Paterson signed legislation (the Budget Bill) that makes significant changes to the Empire Zone Program. The legislation requires the Commissioner of Economic Development (the “**Commissioner**”) to review all certified businesses in 2009 to determine whether their Empire Zone certification should be retained or revoked. The legislation also establishes several new grounds for decertifying (i.e., removing) a certified business from the Empire Zone Program and makes a number of other changes to the Empire Zone Program.

On April 15, 2009, the New York State Department of Taxation and Finance (the “**Tax Department**”) issued a memorandum setting forth its interpretation of the new law. According to this memorandum, the Tax Department will deny all Empire Zone tax credits claimed for the 2008 tax year unless a “retention certificate” is attached to the tax return. As explained below, however, retention certificates will not be issued until after the Commissioner completes her review of certified businesses in 2009.

This Tax Alert summarizes the new law regarding revocation of Empire Zone certifications, including the Tax Department’s interpretation of the legislation, and describes some issues arising out of the new law and its interpretation. Bond, Schoeneck & King is working to resolve these issues and protect our clients’ rights to continued Empire Zone certification and tax benefits.

We recommend that you be proactive if Empire Zone certification and the tax credits are important to your business. In that regard, you should call and write your New York State Senator and Assembly Person and express your concerns about the impact of the new law on your business, including its retroactive application to your 2008 tax return. We welcome the opportunity to help you navigate these issues. If you have any questions regarding the new law, please contact us.

New Law Regarding Revocation of Certification: The following summarizes the revocation of Empire Zone certification provisions under the 2009 Budget Bill (S.57-B):

- Added Decertification Grounds for Pre-August 1, 2002 Businesses: Two grounds were added for decertifying a business that was certified before August 1, 2002:
 - if the certified business caused a business with similar ownership to transfer its employees to the certified business, or
 - if the certified business acquired or otherwise obtained ownership of real estate from an entity with similar ownership.
- Added Decertification Grounds for all Businesses: Three grounds were added for decertifying a business regardless of when it was certified:
 - if the Empire Zone tax credits a certified business received exceed the compensation paid to its employees and investments in its facility (the “**1:1 cost benefit ratio**”); the Commissioner will apply the 1:1 cost benefit ratio based on at least three business annual reports (commonly referred to as the BAR Reports) filed by the certified business, or
 - if the business enterprise has changed ownership, or
 - if the certified business moves out of the Empire Zone.

- **Added Review of All Certified Businesses:** During 2009, the Commissioner of Economic Development is required to review all certified businesses to determine whether the business should be decertified on any of the first three new grounds for decertification (listed above). From a practical standpoint, because the Commissioner will be reviewing all certified businesses, she has the right to decertify any certified business if other grounds exist. Under the new law, however, the Commissioner (after consultation with the Director of the Budget), in her sole discretion, may forego decertification of a business if “other economic, social or environmental factors” warrant continued certification.
- **Added Retention Certificate and Notice of Decertification:** After the Commissioner’s review of a certified business, she will either:
 - issue a “retention certificate”, signifying that the business continues to be certified and is eligible to claim Empire Zone tax credits, or
 - issue a notice of decertification to begin the decertification process.

Although businesses will have the right to appeal the Commissioner’s decision to decertify, a successful appeal will be difficult to obtain. Accordingly, it is important for each certified business to make its case to the Commissioner, if she will hear it, before she renders her decision.

Tax Department Interpretation of Decertification Process Applies Revocation Retroactively: On April 15, 2009, the Tax Department issued a memorandum providing its interpretation of the new law (TSB-M-09(5)(C)). In this memorandum, the Tax Department states it will deny claims for Empire Zone tax credits for tax years beginning in 2008 unless a retention certificate is attached to the tax return. *This denial applies to all taxpayers claiming Empire Zone credits for 2008, regardless of when the business was first certified under the Empire Zone Program or whether the business is ultimately decertified.* The Tax Department further states that interest, but not penalties, will be imposed for any underpayment of 2008 taxes resulting from the disallowance of Empire Zone tax credits. Based on an informal conversation with the Tax Department, from a practical standpoint this means the Tax Department will deny all Empire Zone tax credits claimed on a 2008 tax return and will send deficiency notices to all taxpayers that claimed Empire Zone credits, requiring an additional payment equal to the Empire Zone tax credits claimed plus interest. If the certified business later receives a retention certificate, the business (or its owners) may file an amended 2008 tax return and claim the Empire Zone tax credits.

Issues Raised by the New Law and the Tax Department’s Interpretation: The Tax Department’s interpretation raises the following issues and concerns:

- Does the Tax Department have the authority to deny a certified business its Empire Zone tax credits generated in 2008 even though the Budget Bill was not effective until April 7, 2009?
- How can certified businesses, or their owners, attach a retention certificate to their 2008 tax returns when the retention certificates will not be issued to them until later this year?
- What is meant by “the business enterprise has changed ownership” as a grounds for decertification? Is this limited to asset sales or does it also include equity sales?
- What are the “economic, social and environmental factors” that the Commissioner will consider in exercising her discretionary authority to allow continued certification? What process will the Commissioner follow in her evaluation? Will written submissions or oral arguments be accepted?
- In seeking clarification, are businesses better served by approaching legislators, the Commissioner and the divisions of the executive branch that will be writing regulations individually or as coalitions?

Bond, Schoeneck & King's Tax Group and Administrative & Legislative Group are working together to develop a better understanding of these issues, to assist certified businesses through the implementation of these laws and to help craft potential legislative and regulatory solutions.

As issues are raised and resolved, BS&K will release subsequent Tax Alerts. For additional information and updates visit www.bsk.com (see Tax Practice Group web page). A Tax Alert summarizing the remaining changes to the Empire Zone Program under the Budget Bill will be sent to you shortly.

If you have any questions, please contact us.

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