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State Tax Break Benefits Companies, Not Workers;
Lax oversight, loopholes are blamed for failure of enterprise zones to help the needy as intended.

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A program designed to bring jobs to low-income Californians has given companies millions of dollars in tax breaks that have done nothing to create employment for the poor.

Loopholes, lax oversight and alleged cheating have allowed companies to profit from the state's enterprise zone program, in some cases shaving millions off their tax bills without meeting requirements.

State auditors have concluded that the city of Oakland handed out more than \$27 million in questionable tax breaks over a period of 2 1/2 years. Lawmakers and advocacy groups say the problems in Oakland -- the only city that the state has investigated -- are widespread.

"People have taken advantage of this, and nobody has questioned it," said state Sen. Michael Machado (D-Linden), chairman of the Senate Revenue and Taxation Committee. "The state has fallen down on this one."

Officials concede that oversight has been inadequate, and are auditing hundreds of companies that they suspect may have received dubious credits totaling \$100 million. Several firms have challenged the state's authority to revoke the credits. The first such case will be heard today by the Board of Equalization, whose five elected members decide state tax disputes.

It is unclear how many of the 9,000 companies that have participated in the program claimed credits, either through legal loopholes or illegally, for workers who were not disadvantaged. But state officials and some lawmakers are pushing for significant rule changes to thwart abuse.

Companies have been able to take advantage of enterprise zones in a number of ways. Among them:

* Businesses in upscale areas such as the Long Beach waterfront and San Francisco's fashionable South of Market district get tax breaks because zone boundaries are based on decades-old census data. Employees of such companies

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who live in town houses in and around parts of San Francisco's exclusive Nob Hill neighborhood, beach lofts in Long Beach and the vintage bungalows of Oakland's upscale Rockridge district can qualify their employers for credits; dated maps show those neighborhoods as low-income. The state is subsidizing six-figure salaries in these zones.

* The program allows credits retroactively for employees who have been on the payroll for years -- undermining the goal of providing incentives for companies to move into distressed areas, instead rewarding firms already there.

* Veterans, former felons and people recently laid off can qualify, and companies claim tax credits for them regardless of their salaries.

"There are plenty of \$100-an-hour and \$200-an-hour guys who qualify," said Tom Flanagan, director of Zone Credit Consulting, a Pasadena firm that helps companies secure credits. "Maybe they have a DUI on record or were caught with marijuana, so they are an ex-felon," and qualify their companies for a subsidy.

* Cities can use the program to make money. They can sell the credits to companies in other enterprise zones, collecting a fee for every application. Cities can process thousands of applications, generating hundreds of thousands of dollars in revenue.

"If the point of this program was to give an advantage to disadvantaged areas, they haven't done it. They have completely failed," said Lenny Goldberg, executive director of the California Tax Reform Assn., a nonprofit group that advocates for low-income Californians. "All they have done is create pockets of special tax breaks for companies that manipulate the system."

Businesses in depressed urban and rural zones can receive tax credits of up to \$34,000 for every employee they hire who has encountered discrimination, lives in a designated low-income area, receives public assistance or has faced "barriers" to employment, state law says.

California initially created 10 enterprise zones in 1984. Lawmakers trying to help businesses in their districts have since added 32 more zones and eased requirements. Now the program is California's biggest tax incentive for businesses.

But outdated boundaries and vague regulations have allowed businesses to claim tax breaks for employing people the state never intended to subsidize. In addition, some companies have claimed credits for employees who state officials say were clearly not eligible.

In the program's first decade or so, the credits, granted by cities, cost the state less than \$50 million a year. Last year, the cost was roughly \$300 million. Companies are holding \$650 million more in credits for use this year and in future years.

The Los Angeles Times is among the hundreds of companies benefiting from the program. Gary Weitman, a spokesman for Tribune Co., which owns The Times, declined to give details but said in a written statement that the credits the company has secured are "very modest" compared with those of other large California firms.

"From the beginning, we have been very careful to protect the privacy of our employees," his statement said. "We ... have no reason to believe that our credits will not be sustained. As a large California taxpayer, we are routinely audited on an annual basis in California, so all of the claimed tax credits will be reviewed."

Enterprise zones initially were the responsibility of the Department of Trade, Technology and Commerce, but it closed in 2003.

"Clearly, some things had not been done prior to when we took over," said Richard Friedman, who now oversees the program at the state Department of Housing and Community Development, which mostly deals with

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affordable-housing issues. The agency is now rewriting regulations governing enterprise zones.

"It happened at a time when the department was slated for elimination," Friedman said, "and staff probably started worrying about other things."

Documents obtained by The Times show that Oakland approved 100,000 tax-credit vouchers worth about \$1.6 billion in a 30-month period ending in the summer of 2003. The three city workers administering the program processed an average of one voucher every three minutes.

Another Pasadena consulting firm, California Credits Group, whose clients include The Times, submitted applications to Oakland already bearing the electronic signature of the official who was to review them.

Nearly a third of the credits granted by Oakland went to companies outside the city's own enterprise zones. Some were awarded to companies whose workers did not live in required areas, according to state documents, although the companies claimed they did.

In addition, employees reported by their companies as eligible for public assistance, thus allowing the firms to claim tax credits, were actually being paid handsomely.

Today, the Board of Equalization will hear the case of the Deluxe Corp., an Antelope Valley manufacturer of personal checks, business cards and stationery. The firm obtained nearly \$1 million in tax credits from Oakland without proving that the employees for which they were granted were eligible, according to the Franchise Tax Board, California's version of the IRS.

"Oakland has made its call," said Deluxe attorney Jeffrey Vesely. "The Franchise Tax Board is coming in and second-guessing. Our position is they don't have the right to do that. Whether the program is working right or not is not my call. I'm looking at the law."

Another company that will go before the board with that argument is formal-wear retailer Jessica McClintock. The state is trying to block \$239,000 of the company's credits, awarded for its San Francisco operation, questioning whether 25 of its employees were economically disadvantaged. One was earning more than \$94,000 a year, according to state records.

Oakland officials say they followed the rules of the program. The state disagrees, and has since prohibited Oakland from issuing tax credits to companies in other cities.

"The regulations were extremely vague and open to a wide range of interpretation," said Al Auletta, workforce development manager for Oakland. Before the state launched its investigation, he said, "We received no notification whatsoever that this was a problem."

Indeed, state records show that Sacramento provided little guidance and even approved some of Oakland's activities now being questioned.

As officials at the Department of Housing and Community Development scurry to put stricter standards in place, lawmakers like Machado want to refocus the program on creating jobs for the poor.

That isn't stopping other cities. The Bay Area community of Richmond processed more than 13,000 tax credits for companies outside its borders last year. One of the newest members of the Richmond Chamber of Commerce is the California Credits Group. The firm secured the disputed tax breaks for Deluxe and Jessica McClintock.

Richmond officials did not return calls, and an executive at California Credits Group declined to comment.

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