



# Empowerment Zones, Enterprise Communities, and Renewal Communities: Comparative Overview and Analysis

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February 14, 2011

Congressional Research Service

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[www.crs.gov](http://www.crs.gov)

R41639

## Summary

Empowerment Zones (EZs), Enterprise Communities (ECs), and Renewal Communities (RCs) are federally designated geographic areas characterized by high levels of poverty and economic distress, where businesses and local governments may be eligible to receive federal grants and tax incentives. Congress remains interested in these programs to revitalize selected areas affected by unemployment and a decline in economic activity, despite increased concern over the size and sustainability of the long-term budget outlook.

The objective of this report is to provide a comparative overview of the similarities and differences between the EZ, EC, and RC programs, and a review of congressional policy choices to target and provide federal incentives to economically distressed zones. The report also examines studies that have evaluated the impact of EZs, ECs, and RCs, and provides information on their current status. Finally, the report discusses recent legislative activity and congressional issues and options.

Since 1993, Congress has authorized three rounds of EZs (1993, 1997, 1999), two rounds of ECs (1993, 1997), and one round of RCs (2000) with the objective of revitalizing selected economically distressed communities. The three programs have different benefits and eligibility criteria. For example, the nine initial EZs each received tax incentives and grants of \$100 million (urban) and \$40 million (rural), whereas the 95 initial ECs each received tax benefits and smaller grants of \$2.95 million for smaller urban counties and rural communities. RCs did not receive grants, but benefitted from wage credits, and tax investment incentives. Eligibility varied depending on levels of population, unemployment, and poverty. In its FY2010 and FY2011 budgets, the Administration requested that Congress extend tax incentives for EZs and RCs until December 31, 2010 and 2011. EZ and RC tax incentives were extended in the Emergency Economic Stabilization Act of 2008 (P.L. 110-343), through December 31, 2009.

Currently, the estimated \$1.8 billion in grant incentives provided to EZs and ECs since 1993 have mostly been expended. The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (P.L. 111-312) enacted on December 17, 2010, extended EZ tax benefits, but not RCs, until the end of 2011. In addition, legislation such as the American Recovery and Reinvestment Act of 2009 (P.L. 111-5) provided broadband education, training, and equipment for selected facilities located within EZs and ECs, and recovery zone bonds for EZs. In 2009, P.L. 111-8 and P.L. 111-80 provided \$3 million in funding for EZs and ECs. While a short-term extension of EZ tax incentives was enacted in the 111<sup>th</sup> Congress, a similar extension of the RC tax incentives might continue to be an issue in the 112<sup>th</sup> Congress.

A number of studies have evaluated the effectiveness of the EZ, EC, and RC programs. Several government-sponsored studies have failed to link EZ and EC designation with a general improvement in community outcomes. In addition, several academic researchers have evaluated the effectiveness of zone incentives. Overall, these studies have found modest, if any, effects, and call into question the cost-effectiveness of these programs.

There are several options that Congress can consider regarding the EZ, EC, and RC programs. These options may range from permanently extending the programs to allowing them to expire. Other options include a temporary extension, increased oversight, a redesignation of economic development zones, program consolidation, or a combination of these options. This report will be updated as legislative developments warrant.



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## Introduction

Congress has long had an interest in the revitalization of distressed areas through expanded business and employment opportunities. This interest continues today, with combined federal government expenses of \$10.9 billion<sup>1</sup> and \$5.1 billion<sup>2</sup> in foregone tax revenue in FY2009 for the purpose of community and regional development. Given this commitment towards the goal of economic development, it is natural to ask about the effectiveness of the underlying programs.

Empowerment Zones (EZs), Enterprise Communities (ECs), and Renewal Communities (RCs) are federally designated geographic areas characterized by high levels of poverty and economic distress, where businesses and local governments may be eligible to receive federal grants and tax incentives. The objective of this report is to provide a comparative overview of the similarities and differences among the three programs, specifically policies to target and provide federal incentives to economically distressed zones. The report also examines studies that have evaluated the impact of EZs, ECs, and RCs, and provides information on their current status. Finally, the report discusses recent legislative activity and congressional issues and options.

Since 1993, Congress has authorized three rounds of EZs (1993, 1997, 1999), two rounds of ECs (1993, 1997), and one round of RCs (2000) with the objective of revitalizing selected economically distressed communities. In addition, Round I contained a supplemental round established by the Clinton Administration.<sup>3</sup> The three programs have different benefits and eligibility criteria.<sup>4</sup> For example, the nine initial EZs each received tax incentives and grants of \$100 million (urban) and \$40 million (rural), whereas the 95 initial ECs each received tax benefits and smaller grants of \$2.95 million for smaller urban counties and rural communities. RCs did not receive grants, but benefitted from wage credits, and tax investment incentives.<sup>5</sup> Eligibility varied depending on levels of population, unemployment, and poverty.

In its FY2010 and FY2011 budgets, the Administration requested that Congress extend tax incentives for EZs and RCs until December 31, 2010 and 2011. EZ and RC tax incentives were extended in the Emergency Economic Stabilization Act of 2008 (P.L. 110-343), through December 31, 2009. EZ and RC tax benefits lapsed from January 2010 until December 2010.

Currently, the estimated \$1.8 billion in grant incentives provided to EZs and ECs since 1993 have mostly been expended. The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (P.L. 111-312), enacted on December 17, 2010, extended EZ tax benefits, but not RCs, until the end of 2011. In addition, legislation such as the American Recovery and Reinvestment Act of 2009 (P.L. 111-5) provided broadband education, training, and equipment

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<sup>1</sup> U.S. Office of Management and Budget, *Historical Tables, Budget of the U.S. Government, FY2011*, Washington, DC, February 1, 2010, p. 69.

<sup>2</sup> U.S. Congress, Senate Committee on the Budget, *Tax Expenditures: Compendium of Background Material on Individual Provisions*, committee print, prepared by the Congressional Research Service, 110<sup>th</sup> Cong., 2<sup>nd</sup> sess., December 2008, 110-667 (Washington: GPO, 2008), pp. 537-556.

<sup>3</sup> U.S. Government Accountability Office, *Revitalization Programs: Empowerment Zones, Enterprise Communities, and Renewal Communities*, GAO-10-464R, March 12, 2010, p. 1, <http://www.gao.gov/products/GAO-10-464R>.

<sup>4</sup> For additional information, see CRS Report 94-953, *Social Services Block Grant: Background and Funding*, by (name redacted).

<sup>5</sup> U.S. Congress, Joint Committee on Taxation, *Incentives for Distressed Communities: Empowerment Zones and Renewal Communities*, October 7, 2009 (JCX-38-09).

for selected facilities located within EZs and ECs, and recovery zone bonds for EZs. In 2009, P.L. 111-8 and P.L. 111-80 provided \$3 million in appropriations for EZs and ECs. While a short-term extension of EZ tax incentives was enacted in the 111<sup>th</sup> Congress, a similar extension of the RC tax incentives might continue to be an issue in the 112<sup>th</sup> Congress.

After Congress authorized the programs, federal agencies responsible for administering the programs held competitions to designate a selected number of communities. According to estimates by the Government Accountability Office (GAO), 993 communities applied for designation and 184 were selected.<sup>6</sup> In addition to funding authorized through legislation in the three rounds, designated communities also received funding through annual appropriations laws from 1999 to 2009.

Federal block grant funds for Round I remained available to finance qualified projects until December 31, 2004.<sup>7</sup> By contrast, Round II funds are available to communities until expended, with the exception of FY2003 appropriations for Round II, which were available until September 30, 2005.<sup>8</sup> Tax incentives expired on December 31, 2009.<sup>9</sup> **Table 1** summarizes the three rounds of EZ, EC, and RC programs and the number of designated communities by urban and rural category.

**Table 1. Summary of Three Rounds of EZ, EC, and RC Programs**

Round	Legislative or Executive Action	Total EZs/ECs/RCs	Urban EZs	Rural EZs	Urban ECs	Rural ECs	Urban RCs	Rural RCs
Round I EZ and EC	Omnibus Budget Reconciliation Act of 1993 (P.L. 103-66), enacted on August 10, 1993. Federal regulations available at 24 C.F.R. 597.  Deadline for Round I nominations was June 30, 1994. A total of 520 communities were nominated and 104 were selected on December 1994. Block grants expired on December 2004.	104	6	3	65	30		
	Executive Order 13005 (May 21, 1996).	6	2		4			
Round II EZ and EC	Taxpayer Relief Act of 1997 (P.L. 105-34), enacted on August 5, 1997.	20	15	5				

<sup>6</sup> U.S. General Accounting Office, *Federal Revitalization Programs Are Being Implemented, but Data on the Use of Tax Benefits Are Limited*, GAO-04-306, March 2004, p. 26, <http://www.gao.gov/new.items/d04306.pdf>.

<sup>7</sup> *Ibid.* p. 14.

<sup>8</sup> *Ibid.* p. 16.

<sup>9</sup> EZ and RC tax incentives were last extended in the Emergency Economic Stabilization Act of 2008 (P.L. 110-343) through December 31, 2009. EC tax benefits expired in 2004, but ECs may still be eligible for other federal benefits such as grants and preferences.

Round	Legislative or Executive Action	Total EZs/ECs/RCs	Urban EZs	Rural EZs	Urban ECs	Rural ECs	Urban RCs	Rural RCs
	Omnibus Consolidated and Emergency Supplemental Appropriations Act of 1999 (P.L. 105-277), enacted on October 21, 1998.  A total of 279 communities competed for 40 designations in Round II.	20				20		
Round III EZ and RC	Consolidated Appropriations Act of 2004 (P.L. 108-199), enacted on January 23, 2004.  A total of 91 communities competed for 40 designations. Tax benefits expired on December 31, 2009.	40					28	12

**Source:** U.S. General Accounting Office, *Federal Revitalization Programs Are Being Implemented, but Data on the Use of Tax Benefits Are Limited*, GAO-04-306, March 2004, p. 3 and p. 25, <http://www.gao.gov/new.items/d04306.pdf>.

## Program Administration

As shown in **Table 2**, four federal agencies are responsible for administering the programs. Federal grants for the EZ and EC programs are administered by the Department of Health and Human Services (HHS),<sup>10</sup> the Department of Housing and Urban Development (HUD)<sup>11</sup> and the Department of Agriculture (USDA).<sup>12</sup> Although EZ and EC grants have mostly been expended, Congress has provided funding for selected EZs and ECs through annual HUD and USDA appropriations (see section “Grant Incentives”); in addition, legislation such as the American Recovery and Reinvestment Act of 2009 (P.L. 111-5) provided broadband education, training, and equipment for selected facilities located within ECs.

<sup>10</sup> For additional information from HHS on EZ and EC programs, see <http://www.acf.hhs.gov/programs/ocs/ez-ec/>.

<sup>11</sup> For additional information from HUD on urban EZ, EC, and RC programs, see <http://www.hud.gov/offices/cpd/economicdevelopment/programs/rc/index.cfm>.

<sup>12</sup> For additional information from USDA on rural EZ and EC programs, see <http://www.rurdev.usda.gov/rbs/ezec/>.

**Table 2. Program Administration by Federal Agency**

<b>Federal Agency</b>	<b>Program</b>	<b>Benefits</b>
HUD	EZ, EC	Economic Development Initiative and Section 108 benefits under Community Development Block Grants
USDA	EZ, EC	Social Services Block Grants for rural communities
HHS	EZ, EC	Social Services Block Grants for urban communities
IRS	RC	Tax benefits

**Source:** <http://www.hud.gov/offices/cpd/economicdevelopment/programs/rc/index.cfm>.

HHS is responsible for providing EZ and EC grants under the Social Services Block Grant program to (1) help prevent, reduce, or eliminate dependence on public assistance; (2) help individuals achieve or maintain self-sufficiency; and (3) prevent neglect, abuse, or exploitation of children and adults.

HUD administers the urban programs under its CDBG program to provide flexible economic development funds for local communities. Economic development activities include job creation and training, entrepreneurial activities, small business expansion, and job support services such as affordable child care and transportation services that would help EZ and RC residents gain employment in jobs that offer upward mobility.

USDA oversees the EZ and EC program in rural areas and administers the grants to Round II rural EZ and ECs and Round III EZs. According to the USDA, more than 53 million people live in rural areas of the United States, 16.4% of whom live in households with incomes below the federal poverty level.<sup>13</sup> EZ and EC grants target economic development projects in rural areas experiencing persistent poverty and unemployment levels.

The Internal Revenue Service (IRS) is responsible for administering the tax benefits available under the EZ, EC, and RC programs. A list of census tracts eligible for EC and EZ funding can be obtained from HUD.<sup>14</sup>

A Community Empowerment Board was established in 1993 to coordinate the EZ, EC program. The Board had 26 members from federal agencies, including the U.S. vice president, who served as chair. According to GAO:

The board's function was to consult in the designation of Round I and II EZs and ECs and coordinate the various federal agency resources that EZs and ECs would use to implement their strategic plans. For example, the Community Empowerment Board encouraged other agencies to provide preference points to EZs and ECs in selection competitions for other federal programs.<sup>15</sup>

The Community Empowerment Board was disbanded prior to Round III of the EZ program in 2004.

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<sup>13</sup> See, for example, <http://www.usda.gov/news//pubs/fbook97/6f.pdf>.

<sup>14</sup> For more information, see <http://www.hud.gov/offices/cpd/economicdevelopment/programs/rc/tour/census.xls>.

<sup>15</sup> U.S. General Accounting Office, *Federal Revitalization Programs Are Being Implemented, but Data on the Use of Tax Benefits Are Limited*, GAO-04-306, March 2004, p. 8, <http://www.gao.gov/new.items/d04306.pdf>.

## Eligibility Criteria

Communities nominated for EZ, EC, or RC designations have been required to meet certain eligibility criteria based largely on the socioeconomic characteristics of the residents living in the nominated areas. Specifically, during their initial application, nominated census tracts have been required to meet statutory or regulatory requirements for (1) poverty in each census tract, (2) overall unemployment, and (3) total population. In most cases, these requirements were initially based on 1990 census data since the programs were authorized in 1993. The levels required for eligibility differed by round, by program, and between urban and rural nominees, as shown in **Table 3**. In addition to the socioeconomic criteria, communities have also been required to meet criteria regarding geographic size and general economic distress. Further, Indian reservations were excluded from Round I EZ or EC designation. Only census tracts within nominated areas designated by HUD were eligible for tax credits.

**Table 3. Socioeconomic Eligibility Criteria for EZ/EC and RC Programs**

	Urban EZ/EC		Rural EZ/EC		RC
	Round I	Round II and III	Round I	Round II and III	
Minimum required poverty level in nominated census tracts	35% in 50% of tracts and 25% in 90% of tracts and 20% in all tracts	25% in 90% of tracts and 20% in all tracts	35% in 50% of tracts and 25% in 90% of tracts and 20% in all tracts	25% in 90% of tracts and 20% in all tracts	20% in all tracts
Minimum required unemployment rate	6.3%	6.3%	None specified	None specified	9.45%
Population in zone	Maximum: 200,000 or the greater of 50,000 or 10% of the population of the most populous city within the nominated area		Maximum: 30,000		Maximum: 200,000 Minimum: 4,000 if any portion is within a metro area; 1,000 otherwise

**Source:** U.S. General Accounting Office, *Federal Revitalization Programs Are Being Implemented, but Data on the Use of Tax Benefits Are Limited*, GAO-04-306, March 2004, <http://www.gao.gov/new.items/d04306.pdf> and P.L. 103-66, P.L. 105-34, P.L. 106-554, 24 C.F.R. 597, 24 C.F.R. 598, 24 C.F.R. 599, and 7 C.F.R. 25.

## Policy Overview and Legislative History

### Introduction

The enterprise zone concept originated in Great Britain in the mid-1970s. In 1978, Sir Geoffrey Howe, a member of the British Parliament, argued for the establishment of market-based enterprise zones, which would provide government tax relief in economically distressed areas.<sup>16</sup> By the mid-1980s, more than two dozen enterprise zones were established in England.

<sup>16</sup> Marilyn Rubin, "Can Reorchestration of Historical Themes Reinvent Government? A Case Study of the (continued...)"

In the United States, enterprise zone legislation was introduced in Congress as early as 1980. Republican Representative Jack Kemp introduced the first enterprise zone bill in May 1980 (H.R. 7240, the Urban Jobs and Enterprise Zone Act of 1980). Democratic Representative Robert Garcia co-sponsored with Representative Kemp H.R. 3824, the Urban Jobs and Enterprise Zone Act of 1981.<sup>17</sup>

Although federal legislation was not enacted in the 1980s, several states did implement enterprise zone programs.<sup>18</sup> By the late 1980s, over two thirds of the states had embraced the concept, enacted legislation, and started enterprise zone initiatives. According to one estimate, by July 1993, before the establishment of the federal programs, 37 states had established enterprise zone programs with different eligibility criteria, and benefits.<sup>19</sup>

## Designation Rounds

Congress has authorized three rounds for the designation of Empowerment Zones, Enterprise Communities, and Renewal Communities. Three designation rounds—in 1993-1994, 1997-1999, and 2000—applied to EZ programs, while only the first two rounds applied to ECs, and the third round applied to the RC program. In addition, Round I contained a supplemental round established by the Clinton Administration. The designation process is discussed in more detail below, and a list of EZ/E and RC communities is available in **Appendix A** to this report.

### First Round of EZs and ECs

The 103<sup>rd</sup> Congress established the EZ and EC programs in 1993 through the Omnibus Budget Reconciliation Act of 1993 (P.L. 103-66).<sup>20</sup> The legislation provided both grant and tax incentives to companies located in EZs and ECs that employed local residents and conducted business in economically distressed neighborhoods. Distressed neighborhoods were identified at the census tract level based on several indicators such as the percent of the population in poverty, the unemployment rate, and total population, as shown in **Table 3**.

To be considered in the first round of EZ and EC programs, areas had to be nominated by one or more local governments and the state or states in which they were located. Areas on Indian reservations were not eligible to apply in Round I. An area could also have met this nomination

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(...continued)

Empowerment Zones and Enterprise Communities Act of 1993,” *Public Administration Review*, vol. 54, no. 2 (March 1994), pp. 161-169.

<sup>17</sup> U.S. Congress, House Committee on Ways and Means, *The Enterprise Zone Tax Act of 1982*, Message from the President of the United States transmitting proposed legislation entitled, “The Enterprise Zone Tax Act of 1982”, 97<sup>th</sup> Cong., 2<sup>nd</sup> sess., March 23, 1982, H.Doc. 97-157 (Washington: GPO, 1982), pp. 1-5; and U.S. Congress, House Committee on Banking, Finance, and Urban Affairs, Subcommittee on the City, *Urban Revitalization and Industrial Policy*, 96<sup>th</sup> Cong., 2<sup>nd</sup> sess., September 17, 1980, Serial No. 96-72 (Washington: GPO, 1980), pp. 205-224.

<sup>18</sup> Sarah F. Liebschutz and State University of New York, “Empowerment Zones and Enterprise Communities: Reinventing Federalism for Distressed Communities,” *Publius: The Journal of Federalism*, vol. 25, no. 3 (1995), pp. 117-132.

<sup>19</sup> Marilyn Rubin, “Can reorchestration of historical themes reinvent government? A case study of the Empowerment Zones and Enterprise Communities Act of 1993,” *Public Administration Review*, vol. 54, no. 2 (March 1994), pp. 161-169.

<sup>20</sup> Omnibus Budget Reconciliation Act of 1993, OBRA 1993, P.L. 103-66, 107 Stat. 312, August 10, 1993.

requirement if nominated by an economic development corporation chartered by the state. The nominations were presented to the federal agencies responsible for administering the programs, including HHS, HUD, and USDA, where the appropriate Secretary made a final designation.

By the end of 1994, HHS, HUD, and USDA announced the designation of 104 EZs and ECs—pursuant to the 1993 authorizing legislation. The designated communities were chosen from over 500 communities that applied in a competitive selection process. The roughly \$1 billion in federal grant funding for the first round was allocated for use over the 10-year life of the program, from December 1994 to December 2004.

Businesses were provided the following tax credits: (1) a 20% wage credit for the first \$15,000 of wages paid to a zone resident who worked in the empowerment zone, (2) an additional \$20,000 of section-179 expensing for qualifying zone property,<sup>21</sup> and (3) tax-exempt financing for certain qualifying zone facilities.

### ***Supplemental Designations in First Round***

In 1994, HUD also created two additional supplemental designations, Supplemental Empowerment Zones and Enhanced Enterprise Communities. Unlike EZs or ECs, these designations were not legislatively mandated. Rather, under Executive Order 13005 (May 21, 1996),<sup>22</sup> President Clinton authorized HUD to designate two communities as Supplemental Empowerment Zones and four communities as Enhanced Enterprise Communities. HUD provided these communities with certain grants and loan guarantees, which could be used for activities eligible under the Community Development Block Grant program. The two supplemental EZs and four enhanced ECs received total federal grant funding of \$300 million.

### **Second Round of EZs and ECs**

In addition to the first round of funding authorized in 1993, Congress authorized the designation of two other rounds of competitions for EZs and ECs, with both grant and tax incentives. The Taxpayer Relief Act of 1997 (TRA, P.L. 105-34)<sup>23</sup> authorized the second round of Enterprise Zones and Enterprise Communities and expanded eligibility to Indian tribes. Rural communities in the second round were authorized under the Omnibus Consolidated and Emergency Supplemental Appropriations Act of 1999 (P.L. 105-277).<sup>24</sup>

Unlike Round I communities, Round II EZs and ECs received federal grant funding through HUD and USDA appropriations.

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<sup>21</sup> Section-179 benefits allow a small business to deduct up to \$250,000, for the current tax year, of the full purchase price of financed or leased equipment that qualifies for the deduction.

<sup>22</sup> Executive Order 13005, “Empowerment Contracting,” May 21, 1996.

<sup>23</sup> See Taxpayer Relief Act of 1997, P.L. 105-34, 111 Stat. 886, August 5, 1997, for authorization of Enterprise Zones and Enterprise Communities.

<sup>24</sup> See Omnibus Consolidated and Emergency Supplemental Appropriations Act of 1999, P.L. 105-277, 112 Stat. 2681, October 21, 1998.

### **Third Round of EZs and RCs**

The Consolidated Appropriations Act for the Fiscal Year Ending September 2001 (P.L. 106-554)<sup>25</sup> authorized a third round of Enterprise Zones and Enterprise Communities to provide tax incentives for communities; no federal grant funding was authorized for Round III communities. Congress authorized a new program in 2001 known as “Renewal Communities” under Appendix G of the Consolidated Appropriations Act for the Fiscal Year Ending September 2001.<sup>26</sup> As with the EZ and EC communities, Renewal Communities encouraged local businesses to hire local residents, open branches, and expand their business activities in designated areas. The incentives included employment credits, a zero percent tax on capital gains, increased tax deductions on equipment purchases, accelerated real property depreciation, and other incentives, and programs such as bonds to finance school programs; these are discussed in more detail below.

The Renewal Community (RC) legislation also authorized public schools that met certain criteria in enterprise communities and empowerment zones for qualified zone academy bonds (QZABs). Qualified zone academies are public schools and programs that provide education and training at the secondary level and below. QZABs are bonds designated for school modernization and renovation where the federal government offers annual tax credits to the bondholders in lieu of interest payments from the issuer. Issuers of QZABs are required to use the proceeds to finance public school partnership programs in economically distressed areas. The federal government is effectively paying the interest on the bonds for the state or local government issuers. QZAB holders are limited to banks, insurance companies, and corporations actively engaged in the business of lending money.<sup>27</sup>

In addition, the RC legislation allowed a 15% wage credit on the first \$10,000 of wages for qualified workers and an additional \$35,000 in capital equipment expensing in the designated regions. These qualified businesses were also allowed partial deductibility of qualified buildings placed in service. Renewal community tax benefits were available through December 31, 2009.

Several tax incentives for the District of Columbia were adopted in 1997, through the designation of the District of Columbia as an Enterprise Zone: a wage tax credit of \$3,000 per employee for wages paid to a District resident, tax-exempt bond financing, and additional first-year expensing of equipment. These incentives apply to areas with poverty rates of 20% or more. There is also a zero capital gains tax rate for business sales in areas with 10% poverty rates. These provisions were originally available through December 31, 2007, and subsequently extended through 2009 by the Emergency Economic Stabilization Act of 2008 (P.L. 110-343).

**Figure 1** presents a map with the location of EZs, ECs, and RCs by state and congressional district.

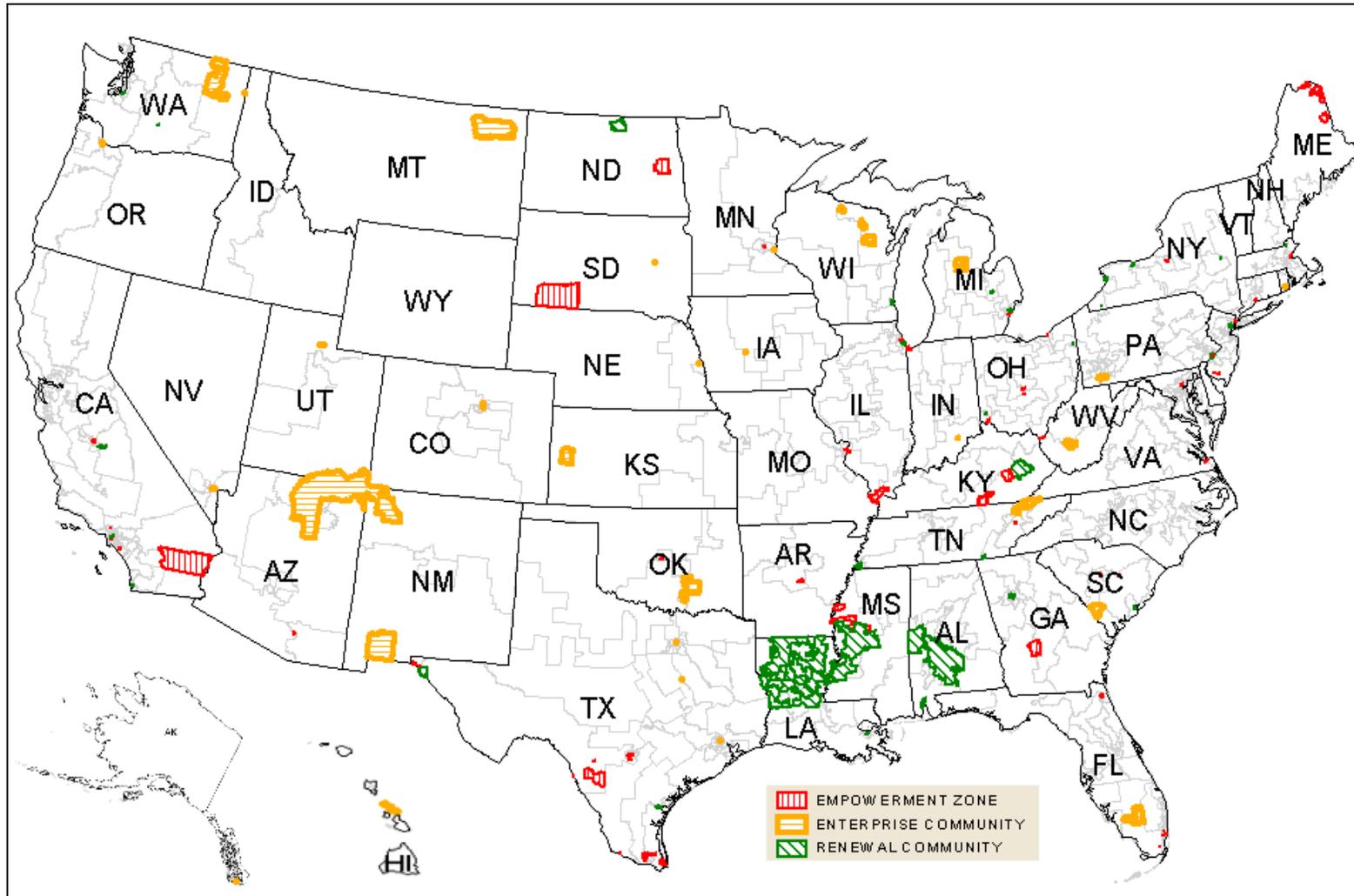
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<sup>25</sup> See Consolidated Appropriations Act for the Fiscal Year 2001, P.L. 106-554, 114 Stat. 2763A-589, December 21, 2000, for authorization of Enterprise Zones and Enterprise Communities.

<sup>26</sup> See Consolidated Appropriations Act for the Fiscal Year 2001, P.L. 106-554, Appendix G—H.R. 5662, Community Renewal Act of 2000, 114 Stat. 2763A-600, December 21, 2000 for authorization of tax incentives for Renewal Communities.

<sup>27</sup> See CRS Report R40523, *Tax Credit Bonds: Overview and Analysis*, by (name redacted).

Figure I. National Map of EZs, ECs, and RCs by State and Congressional District



Source: U.S. Department of Housing and Urban Development data provided to CRS.

Note: Map shows congressional district boundaries in gray.

## **Designations Through 2009**

A total of 40 EZs (30 urban and 10 rural), 95 ECs (65 urban and 30 rural), and 40 RCs (28 urban and 12 rural) have been authorized since 1993. The District of Columbia EZ was also authorized in the TRA and is afforded the same tax incentives as the other EZs. The DC Enterprise Zone incentives were extended through December 31, 2005, by P.L. 108-311, through 2007 by P.L. 109-432, through 2009 by P.L. 110-343, and through 2011 by P.L. 111-312.

## **Tax Incentives, Federal Grants, and Preferences for EZs, ECs, RCs**

Communities designated as EZs, ECs, and RCs are eligible for a combination of tax, grant incentives to encourage economic development, and preferences. Since the initial authorizing legislation was enacted, the number of tax incentives offered has grown, while the value of grant incentives has declined. In dollar terms, for example, the value of grants provided through the first 15 years of the programs is roughly equal to the tax incentives currently being offered every 16.5 months.

## **Tax Incentives for Empowerment Zones and Renewal Communities<sup>28</sup>**

Tax incentives, or tax expenditures, are in many ways equivalent to entitlement spending.<sup>29</sup> That is, tax expenditures are available to everyone who qualifies and federal budgetary costs depend on program rules (the tax code), economic conditions, and behavioral responses. Furthermore, they often remain in the tax code until changed or eliminated by congressional action.

Federal tax incentives for community development have historically taken the form of either employment or investment incentives. **Table 4** describes the tax incentives available to businesses located in Empowerment Zones and Renewal Communities on the basis of their designation. Descriptions of the provisions are provided below.

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<sup>28</sup> While Enterprise Community designation does not bring with it any tax incentives, **Appendix B** details a number of general federal tax incentives for economic development.

<sup>29</sup> Tax expenditures—special deductions, exclusions, exemptions, and credits in the tax code—are often used instead of direct expenditures (mandatory and discretionary spending) to achieve policy goals.

**Table 4. Federal Tax Incentives Available for Empowerment Zones and Renewal Communities**

Tax Incentive	Empowerment Zone (EZ)	Renewal Community (RC)
<b>Employment Incentives</b>		
EZ Employment Credit	X	
RC Employment Credit		X
<b>Investment Incentives</b>		
Increased Section 179 Deduction	X	X
Commercial Revitalization Deduction		X
Empowerment Zone Bonds	X	
Capital Gain Exclusion for RC Assets		X
Rollover of Gain from Sale of EZ Assets	X	
Increased Exclusion of Gain from Qualified Small Business Stock	X	

**Source:** CRS review of EZ, EC, and RC legislation.

**Notes:** EZ, EC, and RC communities may also be eligible for other tax incentives for distressed communities. These additional incentives are described in **Appendix B** and are not tied to zone designation.

## Employment Incentives

Incentives for employers to hire workers are used by both the EZ and RC programs with the goal of fostering economic development in those areas. From an economic perspective, these incentives reduce the after-tax wage paid by the employer and should result in an increase in employment, compared to a no incentive alternative.<sup>30</sup>

Both the EZ and RC employment credits are based upon similar criteria. That is, the credits are calculated using similar formulas and eligibility is defined using similar criteria. Both credits are equal to a set percentage of an eligible employee's wages, up to a cap.

For the Empowerment Zone employment credit, the credit is equal to 20% of the first \$15,000 in wages paid to an employee who is a resident of the empowerment zone and who performs most of their work within the empowerment zone. In the case of the Renewal Community employment credit, the credit is equal to 15% of the first \$10,000 in wages paid to an employee who is a resident of the renewal community and who performs most of their work within the renewal community. In both cases, the credit is claimed by the employer.

<sup>30</sup> According to economic theory and in a competitive market, labor will be added until the last unit of labor increases the after-tax income of the business by the after-tax wage paid. Thus an incentive that reduces the after-tax wage should, according to theory, increase employment.

## **Investment Incentives**

Investment incentives are used by both the EZ and RC programs with the goal of fostering economic development through an increase in the capital stock within the designated geographic areas. In contrast to the employment incentives, a variety of investment incentives are available.

### ***Section 179 Deduction***

Under section 179 of the Internal Revenue Code (IRC), firms in all lines of business and all sizes have the option of expensing the cost of new and used qualified property (or assets) they acquire in the year when the assets are placed in service, within certain limits. The maximum expensing allowance is \$250,000 for qualified assets bought and placed in service in 2010 by firms located outside Empowerment Zones and Renewal Communities. Firms located within Empowerment Zones or Renewal Communities are allowed to claim an additional \$35,000, for a total of \$285,000.

### ***Commercial Revitalization Deduction***

The commercial revitalization deduction reduces the after-tax cost of commercial construction within a Renewal Community. The deduction allows a taxpayer to either deduct one-half of the commercial revitalization expenditures for the taxable year the building is placed in service, or amortize all the expenditures on a pro-rata basis over the 120-month period beginning with the month the building is placed in service.<sup>31</sup> Under either choice, capital cost recovery occurs significantly faster than under standard tax rules. To avoid assigning benefits twice, no depreciation is allowed for amounts deducted under this provision and the adjusted basis of the building is reduced by the amount of the commercial revitalization deduction.

### ***Empowerment Zone Bonds***

Empowerment zone bonds are a type of tax-exempt private activity bond that can be issued for qualified economic development projects in the EZ.<sup>32</sup> The EZ and RC programs have been implemented in rounds and each round is subject to different tax-exempt debt rules. Round I EZ bonds are subject to the state volume cap and each zone can have only \$3 million of EZ bonds outstanding. There are also limits on the amount of Round I EZ bonds any one borrower can have outstanding. An EZ borrower can have an aggregate of \$20 million outstanding for all EZ projects throughout the country.

Round II EZs (and all EZs established after December 31, 2001) are subject to designation “lifetime” caps depending on the urban versus rural designation, and population for urban EZs. For the lifetime of the EZ designation, rural EZs can issue up to \$60 million; urban EZs with population less than 100,000 can issue up to \$130 million; and urban EZs with population greater than 100,000 can issue up to \$230 million. In contrast to Round I EZs, there are no limits on the amount any one entity can borrow for Round II EZs.

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<sup>31</sup> A commercial revitalization expenditure is an expenditure for the construction of a new building or the cost of substantially rehabilitating an existing building within a Renewal Community.

<sup>32</sup> For a discussion of the issues surrounding private activity bonds, see CRS Report RL31457, *Private Activity Bonds: An Introduction*, by (name redacted).

### ***Capital Gains Exclusion for Renewal Community Assets***

Qualified RC assets that are held for more than five years are eligible for an exclusion from capital gains taxes.<sup>33</sup> Qualified assets include original-issue stock purchased for cash in an RC business, a partnership interest acquired for cash in an RC business, and tangible property originally used in an RC business by the taxpayer that is purchased or substantially improved after December 31, 2001.

### ***Rollover of Gain from Sale of Enterprise Zone Assets***

Taxpayers can elect to defer recognition of gain on the sale of a qualified EZ asset held for more than one year and replaced within 60 days by another qualified EZ asset in the same zone.<sup>34</sup> 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.

### ***Increased Exclusion of Gain from Qualified Small Business Stock***

For taxpayers other than corporations, 50% of the gain from the sale of qualified small business stock held for more than five years is excluded from gross income.<sup>35</sup> 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%.<sup>36</sup> For all qualified small business stock acquired after February 17, 2009, and before January 1, 2011, the exclusion is increased to 75%.

## **Grant Incentives**

Grant incentives for the EZ, EC, and RC programs are estimated to have been nearly \$1.8 billion from 1993 through 2009. A total of \$1 billion was provided in the form of grants for the first round in 1994. A total of \$300 million was provided in Community Development Block Grant (CDBG) supplementary funding for Supplemental Empowerment Zones and Enhanced Enterprise Communities in Round I.<sup>34</sup> Annual HUD and USDA appropriations provided over \$480 million through FY2009 for Round II communities. Communities in Round III only received tax incentives and no grants. **Table 5** below presents a summary of grant incentives provided for EZs and ECs.

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<sup>33</sup> Technically, a zero-percent rate is applied to the gains from these assets.

<sup>34</sup> U.S. General Accounting Office, *Federal Revitalization Programs Are Being Implemented, but Data on the Use of Tax Benefits Are Limited*, GAO-04-306, March 2004, pp. 14-16, <http://www.gao.gov/new.items/d04306.pdf>.

**Table 5. Federal Grant Incentives Available for the EZ/EC and RC Programs**

Provision	Description	Estimated Amount
<p><b>ROUND I</b> EZ/EC Social Services Block Grants for Round I EZs and ECs. <b>Legislation:</b> Omnibus Budget Reconciliation Act of 1993 (P.L. 103-66), enacted on August 10, 1993.</p>	<p>Funds were to be used to (1) prevent, reduce, or eliminate dependency; (2) achieve or maintain self-sufficiency; and (3) prevent neglect, abuse, or exploitation of children and adults. Block grant funds remained available to finance qualified projects until December 21, 2004.</p> <p>Round I urban EZs. \$100 million provided to six urban areas.</p> <p>Round I rural EZs. \$40 million provided to three rural areas.</p> <p>Round I ECs (urban and rural). \$2.95 million provided to 95 smaller urban and rural areas.</p> <p><b>SUB-TOTAL</b></p>	<p>\$600 million</p> <p>\$120 million</p> <p>\$280 million</p> <p><b>\$1 billion</b></p>
<p><b>ROUND I</b> EZ/EC Community Development Block Grants (Economic Development Initiative) for Round I Supplemental Empowerment Zones and Enhanced Enterprise Communities.  Executive Order 13005 (May 21, 1996).</p>	<p>HUD created the Supplemental Empowerment Zone and Enhanced Enterprise Community designations at the same time as the Round I EZ/EC designations. HUD awarded \$300 million in Economic Development Initiative grants to the two Supplemental Empowerment Zones and four Enhanced Enterprise Communities.</p> <p><b>Two Supplemental Empowerment Zones</b></p> <p>Los Angeles, CA (city) Los Angeles, CA (county)</p> <p>Cleveland, OH</p> <p><b>Four Enhanced Enterprise Communities</b></p> <p>Boston, MA</p> <p>Oakland, CA</p> <p>Houston, TX</p> <p>Kansas City, MO Kansas City, KS</p> <p><b>SUB-TOTAL</b></p>	<p>\$125 million</p> <p>\$87 million</p> <p>\$22 million</p> <p>\$22 million</p> <p>\$22 million</p> <p>\$22 million</p> <p><b>\$300 million</b></p>
<p><b>ROUND II</b> HUD Appropriations for Round II Urban Designees, Fiscal Years 1999-2003. Appropriations<sup>a</sup></p>	<p>Year</p> <p>1999 (P.L. 105-277)</p> <p>2000 (P.L. 106-74)</p> <p>2001 (P.L. 106-554)</p> <p>2002 (P.L. 107-73)</p> <p>2003 (P.L. 108-7)</p> <p><b>SUB-TOTAL</b></p>	<p>\$45 million</p> <p>\$55 million</p> <p>\$185 million</p> <p>\$45 million</p> <p>\$30 million</p> <p><b>\$360 million</b></p>
<p><b>ROUND II</b> USDA Allocation of Appropriations for Round II Rural Designees, Fiscal Years 1999-2003<sup>b</sup></p>	<p>1999 (P.L. 105-277)</p> <p>2000 (P.L. 106-74)</p> <p>2001 (P.L. 106-554)</p> <p>2002 (P.L. 107-73)</p> <p>2003 (P.L. 108-7)</p>	<p>\$10 million</p> <p>\$10 million</p> <p>\$10 million</p> <p>\$10 million</p> <p>\$10 million</p>

	<b>SUB-TOTAL</b>	<b>\$50 million</b>
	2004 (P.L. 108-199)	\$26.5 million
<b>ROUND II</b>	2005 (P.L. 108-447)	\$22.2 million
Additional HUD and USDA appropriations for Fiscal Years 2004-2009	2005 (P.L. 109-97)	\$21.4 million
	2009 (P.L. 111-8)	\$2.5 million
	2009 (P.L. 111-80)	\$0.5 million
	<b>SUB-TOTAL</b>	<b>\$73.1 million</b>
	<b>TOTAL</b>	<b>\$1.784 billion</b>

**Source:** CRS analysis and U.S. Congress, Joint Committee on Taxation, *Incentives for Distressed Communities: Empowerment Zones and Renewal Communities*, October 7, 2009 (JCX-38-09).

- a. P.L. 105-277, P.L. 106-74, P.L. 106-377, P.L. 106-554, P.L. 107-73, and P.L. 108-7. In FY2001, funds were appropriated in two separate pieces of legislation. Appropriations in 2001 and 2003 were affected by rescissions.
- b. P.L. 105-277, P.L. 106-74, P.L. 106-377, P.L. 106-554, P.L. 107-73, P.L. 108-7, and GAO analysis. Only the FY1999 bill distinguished between appropriations to the rural EZs and rural ECs. For other years, Congress appropriated funds for the rural EZ/EC program, and USDA allocated the appropriations between the EZs and ECs. Appropriations in 2001 and 2003 were affected by rescissions.

## Zone Designation Preferences

The Community Empowerment Board—established in 1993 to coordinate federal agencies implementing the EZ and EC programs—recommended that preference points be given to EZs and ECs in competition for other federal benefits. According to GAO, several federal agencies followed the guidance proposed by the Community Empowerment Board and provided preference points for EZs and ECs. For example, EZs and ECs designated as part of Round I received preference for federal economic development programs, such as the Environmental Protection Agency’s 2003 National Brownfields Assessment, Revolving Loan Fund, and Cleanup Grants. According to GAO:

In 2003, the U.S. Department of Education’s Teacher Quality Enhancement Grants program provided a competitive priority to applicants who proposed to carry out activities in EZs or ECs. In addition, Congress has regularly earmarked federal funds, such as grants for low-income housing repair or direct loans for rural development projects, to projects located in EZs and ECs.<sup>35</sup>

In addition, the U.S. Department of Justice’s Weed and Seed program, provided assistance to reduce crime and drug abuse, and offered preferences for EZs, ECs, and RCs in Round I. Other communities that competed for, but did not receive, EZ or EC status received preferences for federal technical assistance programs. For example, USDA named some communities that competed, but did not win, rural EZ and EC designation as “Champion Communities.” These communities were eligible for technical assistance from USDA and preferences for other government programs. According to GAO, 118 Champion Communities were named by USDA. In addition, EZs and ECs sometimes received preferences from state and local government

<sup>35</sup> U.S. General Accounting Office, *Federal Revitalization Programs Are Being Implemented, but Data on the Use of Tax Benefits Are Limited*, GAO-04-306, March 2004, p. 68, <http://www.gao.gov/new.items/d04306.pdf>.

economic development programs.<sup>36</sup> In addition, legislation such as the American Recovery and Reinvestment Act of 2009 (P.L. 111-5) provided preference for broadband education, training, and equipment for selected facilities located within ECs.

Due to the lack of reporting data, it is difficult to determine the use and impact of these preferences. GAO indicated that the preferences may have decreased after the Community Empowerment Board disbanded. Finally, GAO concluded that limited data existed and that “the extent to which these applicants have taken advantage of these preferences is not known.”<sup>37</sup>

## **Studies of EZ/EC and RC Effectiveness**

A number of studies have evaluated the effectiveness of the EZ, EC, and RC programs. Government-sponsored studies by the Government Accountability Office (GAO) and the Department of Housing and Urban Development (HUD) have failed to link EZ and EC designation with improvement in community outcomes. It is worth noting that these studies examined the Round I EZs and ECs, which received significant grant funding for community organizations. In addition, several non-governmental economic studies have evaluated the effectiveness of zone incentives. Overall, these studies have found modest, if any, effects and call into question the cost-effectiveness of these programs.

This inability to link these programs to improvements in community level outcomes should not be interpreted as meaning that the EZ, EC, and RC programs did not aid economic development. Clearly, businesses and investors that received program benefits were made better off. The main conclusion from these studies is that the EZ, EC, and RC programs have not been shown to have caused a general improvement in the economic conditions of the locals. One possible cause for this inability to generalize the program effects is the size of the programs is small compared to the economic activity within any of the zones.

## **HUD Interim Assessment of EZs and ECs**

In 2001, HUD published a progress report covering the first five years of the Empowerment Zone and Enterprise Communities programs.<sup>38</sup> HUD’s study presented mixed results concerning the effectiveness of the programs. Taken together, the study’s mixed results were inconclusive and did not show that the EZ and EC programs result in community improvement. To date, no final report has been published.

HUD’s interim assessment studied the performance of several urban EZs and urban ECs over the first five years of the EZ and EC programs. The report evaluated performance based on four

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<sup>36</sup> Sarah F. Liebschutz and State University of New York, “Empowerment Zones and Enterprise Communities: Reinventing Federalism for Distressed Communities,” *Publius: The Journal of Federalism*, vol. 25, no. 3 (1995), pp. 117-132.

<sup>37</sup> U.S. General Accounting Office, *Federal Revitalization Programs Are Being Implemented, but Data on the Use of Tax Benefits Are Limited*, GAO-04-306, March 2004, p. 48, <http://www.gao.gov/new.items/d04306.pdf>.

<sup>38</sup> Debbie Gruenstein, Scott Hebert, Franklin James, et al., *Interim Assessment of the Empowerment Zones and Enterprise Communities (EZ/EC) Program: A Progress Report and Appendices*, Department of Housing and Urban Development, Washington, DC, November 2001, [http://www.huduser.org/portal/publications/econdev/ezec\\_rpt.html](http://www.huduser.org/portal/publications/econdev/ezec_rpt.html), hereinafter referred to as HUD’s “interim assessment.”

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 tentative findings consistent with a positive impact by the EZ and EC programs. In aggregate, the Interim Report found that 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 EZ 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 EZ and EC residents. These results might not be robust given that the results are sensitive to the selection of comparison areas. The rounds studied in the report may suggest grant funding as an important factor to consider in economic development policy.

On the other hand, other econometric findings were consistent with little or no positive impact. During the period studied, there was a general economic upturn, making it difficult to separate employment growth attributable to the EZ and EC programs from the overall rising economy. In addition, given the low take-up rate of the tax incentives, employment increases may have been attributable to activities not related to EZ activities.<sup>39</sup>

## **GAO Studies on Empowerment Zones, Enterprise Communities, and Renewal Communities**

The Community Renewal Tax Relief Act of 2000 (P.L. 106-554) mandated that GAO audit the effectiveness of the EZ, EC, and RC programs. The mandate specifically required GAO to examine the programs' effect on poverty, unemployment, and economic growth.

The 2004 GAO report documented the use of selected tax benefits, but did not attempt to determine their impact on community outcomes.<sup>40</sup> Using IRS data, the report found that corporations and individuals claimed an estimated \$251 million in EZ employment credits between 1995 and 2001. During the same time period, 36 different series of tax-exempt bonds, with an aggregate value of \$315 million, were issued to benefit businesses in EZs, Round I ECs, and the DC Enterprise Zone. Data on other tax benefits were not available from the IRS information. Given the lack of available data, GAO did not attempt to determine the impact of the programs on community outcomes and instead reported on earlier impact studies.

The 2006 GAO study analyzed the impact of Round I EZ and EC designation on community level outcomes using multiple methods, but researchers were unable to conclude that community designation improved community outcomes.<sup>41</sup> In one case, GAO used descriptive statistics to analyze the statistical significance of changes in community level outcomes and generally found

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<sup>39</sup> Of the businesses in the six empowerment zones, only 11% reported using empowerment zone employment credits, 4% reported using section 179 expensing, and 3% reported using work opportunity tax credits, while 65% of all empowerment zone businesses reported no benefits from being located in the empowerment zone.

<sup>40</sup> U.S. General Accounting Office, *Federal Revitalization Programs Are Being Implemented, but Data on the Use of Tax Benefits Are Limited*, GAO-04-306, March 2004, pp. 14-16, <http://www.gao.gov/new.items/d04306.pdf>.

<sup>41</sup> 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, <http://www.gao.gov/highlights/d06727high.pdf>.

improved community outcomes (reduced unemployment or poverty). A limitation of this methodology is the inability to attribute community outcomes to the EZ and EC programs. In the second case, GAO used an econometric methodology in an attempt to tie community outcomes to the EZ program. As in the first case, however, GAO was unable to determine whether the changes were a response to the program or other economic conditions.

Taken together, the GAO reports highlight the difficulty in indentifying a causal linkage between the EZ, EC, and RC programs and economic development. The 2004 report identifies data limitations which, effectively, eliminate large-scale econometric evaluation. Further, the 2006 report reiterates the observation from the HUD Interim Report that comparative methods are sensitive to the choice of comparable jurisdictions.

## **Economic Literature**

In addition to studies conducted by federal agencies, several studies have been completed by academic researchers on the potential impact of federal empowerment zones. Overall, these studies have found modest, if any, effects and call into question the cost-effectiveness of these programs. One persistent issue in conducting these studies is the inherent difficulty of identifying the effect of the programs from overall economic conditions. Evaluators might be required to track individuals, households, businesses, and local governments that receive benefits; in addition, researchers would have to match these with similar individuals, households, and businesses that do not receive the benefits, to prospectively estimate statistical differences between beneficiary and non-beneficiary groups.

Studies similar to the 2006 GAO study, examined four empowerment zones and found no economically significant effect.<sup>42</sup> One study found that, while poverty and unemployment decreased in some EZ areas, similar changes occurred in comparison areas that did not receive the EZ designation. A second study was also unable to isolate an effect from EZ designation.<sup>43</sup> These results suggest that the program had no statistically significant effect on income, unemployment, or poverty, a finding shared by recent research on state level enterprise zones.<sup>44</sup>

In addition, a number of studies have focused on the effect of the programs on the housing market. These studies have reached conflicting conclusions. Two studies have found that owner-occupied housing increased between 22% and 25% with zone designation.<sup>45</sup> A third study, however, found that empowerment zone renters are made worse off as rents rise faster than earnings.<sup>46</sup>

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<sup>42</sup> The study, 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*, vol. 28 (November 2006), pp. 443-471, focused on the empowerment zones in Baltimore, Chicago, Detroit, and New York.

<sup>43</sup> Andrew Hanson, "Local employment, poverty, and property value effects of geographically-targeted tax incentives: An instrumental variables approach," *Regional Science and Urban Economics*, vol. 39, no. 6 (November 2009).

<sup>44</sup> David Neumark and Jed Kolko, "Do enterprise zones create jobs? Evidence from California's enterprise zone program," *Journal of Urban Economics*, vol. 68, no. 1 (July 2010).

<sup>45</sup> Douglas J. Krupka and Douglas S. Noonan, "Empowerment Zones, Neighborhood Change and Owner-Occupied Housing," *Regional Science and Urban Economics*, no. 39 (2009), pp. 386-396 and Matias Busso and Patrick Kline, "Do Local Economic Development Programs Work? Evidence from the Federal Empowerment Zone Program," Yale Economics Department Working Paper No. 36 (February 2008)..

<sup>46</sup> Edward L. Glaeser and Joshua D. Gottlieb, "The Economics of Place-Making Policies," *Brookings Papers on* (continued...)

## **Legislative Activity and Policy Issues**

Congress has shown an ongoing interest in extending and reforming the EZ, EC, and RC programs, and several bills were introduced in the 111<sup>th</sup> Congress proposing changes. At the end of the 111<sup>th</sup> Congress, Empowerment Zone tax incentives were extended through December 31, 2011, by the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (P.L. 111-312).

Some of the bills in the 111<sup>th</sup> Congress would have extended tax benefits and revised benefits and requirements for these programs. Changes would have included a temporary extension of the programs, changes in eligibility requirements, adjustment of tax and grant benefits, and changes in boundaries. Changes would also have included the use of the empowerment zone concept to target federal assistance for other programs. In addition, some of the proposed legislation would have incorporated the Department of Commerce—previously not involved in the EZ, EC, and RC initiatives—and allowed for the provision of grants through this new venue.

Although most of the grant funding of EZs, ECs, and RCs expired several years ago, some of the legislation would have initiated new grant programs, and created new tax incentives for the EC program. One congressional proposal would have targeted EZ funds to manufacturing, clean energy, and agricultural enterprises by establishing an EZ revolving loan fund for small and medium-sized manufacturers to improve energy efficiency and to produce clean energy technology; the legislation would have provided a tax credit for farmers' investments in value-added agriculture. Finally, one bill would have created an Air and Health Quality Empowerment Zone under the Environmental Protection Agency. These policy issues and legislation are discussed in more detail below.

### **Temporary Extension of Benefits**

In the 111<sup>th</sup> Congress, H.R. 4213, the Tax Extenders Act of 2009, passed the House on December 9, 2009, by a vote of 241 to 181 and would have temporarily extended tax benefits for EZs and ECs. The legislation was enacted as P.L. 111-205, the Unemployment Compensation Extension Act of 2010—a vehicle to extend unemployment benefits—but the extension of RC and EZ incentives was not included in the enacted law. Section 201 of the House-passed version of the legislation would have extended Empowerment Zone tax incentives through December 31, 2010. The increased exclusion of gain on stock of EZ businesses would have been extended through December 31, 2015. Section 202 would have extended Renewal Community tax incentives through December 31, 2010.

H.R. 1677, the Empowerment Zone, Renewal Community and Enterprise Community Enhancement Act of 2009, and its identical companion bill in the Senate, S. 1222, would have extended the designation of Round I, II, and III EZs, ECs, and RCs through December 31, 2015. H.R. 3500, the Small and Medium Urban Regions Growth and Empowerment Act of 2009, would have extended the period of designation for EZs, ECs, and RCs through December 31, 2019. S.

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(...continued)

*Economic Activity*, vol. 1 (2008).

3787 would also have extended Rounds I, II, and III designations from December 31, 2009, through December 31, 2019.

Finally, at the end of the 111<sup>th</sup> Congress, Empowerment Zone tax incentives were extended through December 31, 2011 by the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (P.L. 111-312).

### ***Discussion***

The extension of EZ and RC benefits, which expired on December 31, 2009, was an issue for the 111<sup>th</sup> Congress and for local communities since early 2009. In its 2010 report, GAO indicated that communities responsible for managing the RC and Round III EZ programs identified several “pending or potential projects that could be implemented if the programs were extended beyond December 31, 2009.”<sup>47</sup> GAO surveyed a total of 50 RC and EZ projects and 39 communities, nearly 80%, indicated that they had pending projects. As a result of the expiration of the RC and EZ tax incentives at the end of 2009, most of these projects were on hold, pending the renewal of the tax incentives for the programs.

In both its FY2010 and FY2011 budget documents, the Obama Administration requested that Congress extend RC and EZ benefits. Because of competing economic priorities, such as the extension of unemployment benefits, legislation that originally included RC and EZ benefits was instead used as a vehicle to address unemployment issues. While a short-term extension of EZ tax incentives was enacted in the 111<sup>th</sup> Congress, a similar extension of the RC tax incentives might continue to be an issue in the 112<sup>th</sup> Congress.

### **Changes to Eligibility Requirements and Boundaries**

In the 111<sup>th</sup> Congress, H.R. 1677, the Empowerment Zone, Renewal Community and Enterprise Community Enhancement Act of 2009, and its identical companion bill in the Senate, S. 1222, would have established job creation criteria to revise the requirement that 35% of employees be residents of EZs. For example, if a business located in a zone creates 500 full-time jobs within EZ boundaries in three years, or a business outside the zone creates 1,000 full-time jobs within EZ boundaries, the residency requirement would be met. The bills would also have eliminated other residency requirements for the empowerment zone employment tax credit and would have granted authority to expand the boundaries of EZs and ECs, including those located in rural areas.

Over the last decade, several legislative proposals have sought to amend the process to designate the boundaries of Empowerment Zones. In the 110<sup>th</sup> Congress, S. 942, and in the 109<sup>th</sup> Congress, S. 2596, both proposed the modification of the boundaries for empowerment zone designation. In the 111<sup>th</sup> Congress, H.R. 3500, the Small and Medium Urban Regions Growth and Empowerment Act of 2009, would have provided authority to expand the boundaries of empowerment zones and enterprise communities, including those located in rural areas.

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<sup>47</sup> U.S. Government Accountability Office, *Revitalization Programs: Empowerment Zones, Enterprise Communities, and Renewal Communities*, GAO-10-464R, March 12, 2010, p. 37, <http://www.gao.gov/new.items/d10464r.pdf>.

### ***Discussion***

Changing eligibility requirements for EZ, EC, and RC programs, such as those pertaining to the hiring of residents living in distressed communities, might encourage more businesses to establish projects in these areas. Linking these requirements to the creation of full-time jobs might also contribute to further economic activity. On the other hand, a long-standing criticism of geographically targeted incentives is that they might encourage businesses to move from one location to another. That is, the result might be the redistribution of business activity that improves one geographic area at the expense of another rather than the addition of newly created business activity.

Proponents of adjusting the geographic boundaries of EZs, ECs, and RCs have argued that economic distress changes over time and census tracts that might have previously met unemployment, poverty, and population thresholds, might no longer meet these requirements. They have also argued that allowing for changes in designated census tracts over time based on data provided by the U.S. Census Bureau might help to target federal aid more effectively. Critics might argue that the law does not allow census tracts that were designated as economically distressed to have their designation removed. HUD and USDA are required by law in the EZ, EC, and RC programs to ensure that a community does not modify the boundaries of designated areas.

### **Changes to Benefits**

Selected legislation in the 111<sup>th</sup> Congress would have made changes to both tax and grant incentives available in EZs, ECs, and RCs. For example, H.R. 1677 and S. 1222 would have made changes to EZ and RC tax benefits, and would have allowed carryovers of unused expensing allowances for EZ businesses. In addition, certain EZ businesses would have been allowed to elect to receive payments in lieu of tax benefits. Local governments would have been permitted to issue tax-exempt rural EC bonds and EZ facility bonds to finance projects and to provide federal guarantees and tax exemptions for eligible businesses located in EZs and RCs.

S. 3787 would also have modified the benefits available in EZs and other tax-incentive areas, to require the Secretary of Commerce to establish a program for the award of grants to States to establish revolving loan funds for small and medium-sized manufacturers to improve energy efficiency and produce clean energy technology, to amend the Internal Revenue Code of 1986 to provide a tax credit for farmers' investments in value-added agriculture, and for other purposes.

H.R. 3500, the Small and Medium Urban Regions Growth and Empowerment Act of 2009, would have expanded the use of tax-exempt Gulf Opportunity Zone and facility bonds in such areas, and have authorized the Secretary of the Treasury to make grants to states, local governments, or nonprofit organizations to make businesses aware of the tax benefits of enterprise zones and to provide technical assistance to small businesses eligible for such benefits.

### ***Discussion***

Several bills have proposed adjusting, changing, and increasing both tax and grant incentives for EZs, ECs, and RCs. Supporters of these changes have argued that additional benefits may lead to more economic activity in distressed areas. In addition, creating a Revolving Loan Fund through the Department of Commerce may provide an ongoing source of funding for the EZ, EC, RC programs as the loans are lent and repaid back. Critics might argue that adding another federal

agency to the administration of the program might create challenges coordinating federal efforts dispersed across different entities. In addition, opponents might argue that creating new grant and loan programs might contribute to a higher federal deficit on the long term.

## **Use of EZ Concept to Model Other Federal Programs**

In the 111<sup>th</sup> Congress, H.R. 5296, the Air and Health Quality Empowerment Zone Designation Act of 2010, was introduced by Representative Jerry McNerney on May 13, 2010. The companion bill in the Senate, S. 3373, was introduced on the same day by Senator Barbara Boxer. Although unrelated to the EZ, EC, and RC programs, the bills would have used a model similar to that of Empowerment Zones to authorize the Administrator of the Environmental Protection Agency to designate areas nominated by local air pollution control districts as air and health quality empowerment zones, eligible for grants for replacing or retrofitting polluting vehicles and/or engines to improve the health of the population living in the zones. The legislation would have established eligibility criteria and matching fund requirements.

### *Discussion*

The lack of evaluation information to determine the effectiveness of EZ, EC, and RC programs continues to be a challenge. Thus, critics may question the use of geographically targeted incentives to provide federal benefits, while supporters might argue that these programs may provide a mechanism to provide resources to areas in economic distress. Using the concept of geographic targeting to provide federal benefits, without evaluation information, may lead critics to question these types of programs. In its final 2010 report, GAO indicated that

In summary, in many cases economic conditions improved in communities where the EZ/EC/RC grants and tax benefits were used. But as we reported previously, it has been difficult to isolate the impacts of these programs on conditions in distressed communities without the ability to attribute the tax benefits to EZ/EC/RC areas. We recognize the challenges inherent in evaluating economic development programs. However, without linking tax benefits to the communities where they are taken, important information remains unclear—for example, the extent to which various tax benefits are being used within each community. Such tax-related information, coupled with more current data on poverty and employment data in such areas, could help program administrators assess the effectiveness of a revitalization program.<sup>48</sup>

## **Policy Options**

There are several options that Congress can consider regarding the EZ, EC, and RC programs in particular, and for federal economic development policy in general. Two contrasting options are to permanently extend the programs as currently constituted or to allow the programs to expire. Allowing the EZ, EC, and RC programs to expire as scheduled might marginally improve the nation's fiscal condition, but could result in a slight reduction in economic recovery in these areas. On the other hand, permanently extending the programs would not weaken the economic

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<sup>48</sup> U.S. Government Accountability Office, *Revitalization Programs: Empowerment Zones, Enterprise Communities, and Renewal Communities*, GAO-10-464R, March 12, 2010, p. 44, <http://www.gao.gov/products/GAO-10-464R>.

recovery, but would worsen the longer-term fiscal outlook. In addition to these options, other options or combinations of options are also available.

## **Consolidation of Economic Development Initiatives**

The number of competing federal government economic development programs suggests a diffuse national economic development policy. This fragmented policy is the result of years of initiatives that have occurred in the absence of a unifying set of economic development principles. This may follow from the inherent difficulty in identifying economic distress using metrics. Current policy typically uses metrics such as unemployment and poverty rates as proxies for economic distress.

Supporters of the current diffuse approach could argue that the numerous federal economic development programs allow for the targeted application of policy tools to a diverse set of economic development needs. Proponents could further assert that the current federal approach best allows for Congress to target efforts as economic development needs evolve over time.

Detractors might argue that the absence of unifying principles renders current federal efforts ineffectual. That is, detractors may argue that without a clear goal, it is unlikely federal policy can efficiently spur economic development. Further, detractors argue that the current set of efforts increase the difficulty in conducting objective effectiveness studies, which hinders congressional oversight of these programs.

If the lack of unifying economic development principles is seen as a detriment to effective economic development policy, then a straightforward policy prescription is apparent. That is, a consolidation of economic development programs could result in the application of a unifying set of principles to the ongoing issue of economic development. As an alternative to consolidation, Congress could allow the existing programs to expire and implement a new program built around a single set of economic development principles.

## **Redesignation of Economic Development Zones**

The various competing federal economic development programs have evolved little over time. In most cases, the designation of economic development zones is a “one-time” event that may not be revisited. One result of this stagnation is that current efforts are not likely targeted at the areas of greatest current need for economic development. For example, some may argue that the current reliance on unemployment or poverty rates results in poor targeting of scarce economic development resources. They may argue that metrics such as foreclosure rates, retail vacancy rates, or the long-term unemployment rate would lead to more efficient targeting of these monies. Others may argue that the stability inherent in the current set of programs acknowledges the long-term nature of any solution to economic distress.

If this stagnation is seen as a detriment to effective economic development policy, then a straightforward policy prescription is apparent. That is, the existing programs could be retained, but with a redesignation of the various economic development zone designation. This option would allow Congress to realign its economic development efforts to the areas of greatest current need for economic development assistance.

## **Increased Program Oversight**

In several reports, GAO has indicated that conducting effective program oversight on these economic development programs is difficult. Specifically, GAO has noted that data limitations make a conclusive study of program effectiveness difficult and made recommendations to allow increased oversight.<sup>49</sup> If Congress chooses to implement these recommendations, then, GAO argues, these programs can be properly evaluated. Coupled with a limited term extension, this option could allow Congress to reevaluate the programs after a full consideration of their effectiveness.

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<sup>49</sup> GAO made the following recommendations in its March 2004 study, GAO-04-306: (1) identify the data needed to assess the use of the tax benefits; (2) determine the cost-effectiveness of collecting these data; (3) document the findings of the analysis; and, if necessary, (4) seek the authority to collect the data, if a cost-effective means is available. See <http://www.gao.gov/new.items/d04306.pdf>.

## **Appendix A. List of Empowerment Zones, Enterprise Communities, and Renewal Communities**

### **Round I Urban EZs (6)**

Atlanta, GA	Chicago, IL	New York, NY
Baltimore, MD	Detroit, MI	Philadelphia, PA/Camden, NJ

### **Round I Rural EZs (3)**

Kentucky Highlands, KY	Mid-Delta, MS	Rio Grande Valley, TX
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### **Round I Urban ECs (65)**

Akron, OH	Indianapolis, IN	Ogden, UT
Albany, GA	Jackson, MS	Oklahoma City, OK
Albany/Schenectady/Troy, NY	Kansas City, MO/Kansas City, KS	Omaha, NE
Albuquerque, NM	Las Vegas, NV	Ouachita Parish, LA
Birmingham, AL	Little Rock/Pulaski, AR	Phoenix, AZ
Boston, MA	Los Angeles, CA	Pittsburgh, PA
Bridgeport, CT	Louisville, KY	Portland, OR
Buffalo, NY	Lowell, MA	Providence, RI
Burlington, VT	Manchester, NH	Rochester, NY
Charleston, SC	Memphis, TN	San Antonio, TX
Charlotte, NC	Miami/Dade County, FL	San Diego, CA
Cleveland, OH	Milwaukee, WI	San Francisco, CA
Columbus, OH	Minneapolis, MN	Seattle, WA
Dallas, TX	Muskegon, MI	Springfield, IL
Denver, CO	Nashville/Davidson, TN	Springfield, MA
Des Moines, IA	New Haven, CT	St. Louis, MO
East St. Louis, IL	New Orleans, LA	St. Paul, MN
El Paso, TX	Newark, NJ	Tacoma, WA
Flint, MI	Newburgh/Kingston, NY	Tampa, FL
Harrisburg, PA	Norfolk, VA	Waco, TX
Houston, TX	Oakland, CA	Washington, DC
Huntington, WV		Wilmington, DE



Huron-Tule, CA  
Metlakatla Indian Community,  
AK

Molokai, HI  
Northwoods Nijjii, WI  
Town of Austin, IN

Tri-County Indian Nations, OK  
Upper Kanawha, WV  
Wichita County, KS

**Round III Urban EZs (8)**

Fresno, CA  
Jacksonville, FL  
Oklahoma City, OK

Pulaski County, AR  
San Antonio, TX  
Syracuse, NY

Tucson, AZ  
Yonkers, NY

**Round III Rural EZs (2)**

Aroostook County, ME

Futuro, TX

**Urban RCs (28)**

Atlanta, GA  
Buffalo-Lackawanna, NY  
Camden, NJ  
Charleston, SC  
Chattanooga, TN  
Chicago, IL  
Corpus Christi, TX  
Detroit, MI  
Flint, MI  
Hamilton, OH

Lawrence, MA  
Los Angeles, CA  
Lowell, MA  
Memphis, TN  
Milwaukee, WI  
Mobile, AL  
New Orleans, LA  
Newark, NJ  
Niagara Falls, NY  
Ouachita Parish, LA

Philadelphia, PA  
Rochester, NY  
San Diego, CA  
San Francisco, CA  
Schenectady, NY  
Tacoma, WA  
Yakima, WA  
Youngstown, OH

**Rural RCs (12)**

Burlington, VT  
Central Louisiana, LA  
Eastern Kentucky, KY  
El Paso County, TX  
Greene-Sumter, AL

Jamestown, NY  
Northern Louisiana, LA  
Orange Cove, CA  
Parlier, CA  
Southern Alabama, AL

Turtle Mountain Band of  
Chippewa, ND  
West-Central Mississippi, MS

**Source:** U.S. General Accounting Office, *Federal Revitalization Programs Are Being Implemented, but Data on the Use of Tax Benefits Are Limited*, GAO-04-306, March 2004, p. 55, <http://www.gao.gov/new.items/d04306.pdf>.

## Appendix B. Federal Tax Incentives Available to Distressed Communities

**Table B-1. Federal Tax Incentives Available to Distressed Communities**

<b>Employment Incentives</b>		
Indian Employment Credit	Work Opportunity Tax Credit	Welfare-to-Work Tax Credit
<b>Investment Incentives</b>		
Low Income Housing Tax Credit	Depreciation of Property Used on Indian Reservations	Environmental Cleanup Cost Deduction
Qualified Zone Academy Bonds	New Markets Tax Credit	

**Source:** U.S. Congress, Joint Committee on Taxation, Incentives for Distressed Communities: Empowerment Zones and Renewal Communities, October 7, 2009 (JCX-38-09).

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