

NEW REGULATIONS NJ URBAN TRANSIT HUB TAX CREDIT

The new Urban Transit Hub Tax Credit Act created a potentially powerful new incentive for urban redevelopment – full capital cost recovery – but contains many ambiguities and some regrettable limitations that could dilute its effectiveness. The new draft regulations, released last week, clarify many of the outstanding questions and provide relief from potential impediments to the program.

PROGRAM RECAP

This new program is complicated, so bear with us as we describe its key features.

Total Cost Recovery: The Act provides *potential* tax credits against a company's NJ corporate income, insurance premium or gross income tax liability in the amount of **up to 100% of a project's capital investment**. A project meeting the minimum capital investment threshold of \$75 million, and that employs at least 250 jobs at the facility (200 of which must be new jobs to NJ), may receive the credit, delivered in equal installments over a 10 year period. The tax credit decreases to 80% if fewer than 200 of the 250 jobs required are *not* new to NJ. Importantly, large tenants in such a qualifying facility also may be eligible for the credit so long as their allocable share of capital investment exceeds \$25 million. Typically, this will be for tenants occupying more than 75,000 sf.

Tale of Nine Cities: Only nine cities are eligible for the program including: Camden, East Orange, Elizabeth, Hoboken, Jersey City, Newark, New Brunswick, Paterson and Trenton. In order to meet the program parameters, properties within these cities must be located within a *one-half mile radius* surrounding the 'mid point' of a New Jersey Transit Corporation, Port Authority Transit Corporation or Port Authority Trans-Hudson Corporation rail station platform area. (Light rail stations were excluded.) The draft regulations provide that a property partially included within the radius shall only be included if over 50 percent is within the radius. In the case of multiple rail lines, separate midpoints will be determined. Applicants will have to confirm location by obtaining a detailed survey.

CLARIFYING DETAILS

The regulations have provided additional insight regarding eligibility parameters and restrictions, and resolve or mitigate many of the impediments to using the program.

- **Affiliates:** A threshold issue for many companies will be whether they aggregate affiliated subsidiaries to qualify for the credit. The way the statute defined the term 'business' could have made it impossible for affiliated corporate entities to aggregate their potential roles in a large project – e.g., one serving as the 'tenant' and/or creating the jobs, while a sister company makes the required investment, while another has the tax liability needed to utilize the credit – which could have made the program worthless to many companies. We proposed that the State remedy this situation by enabling the companies to aggregate affiliates in a 'control group' of entities, as

defined in the IRC. We are pleased to report that the draft regulations adopted this approach, expressly allowing the aggregation of affiliates to assure that, if there is an entity in the corporate family with adequate liability, the credit can be monetized.

Flexibility in accessing the credit is especially important because of restrictions on their use – i.e., they can't be transferred or carried forward or back, and must be used last among any other credits.

- **Exclusion from BEIP/BRRAG:** The statute was initially thought to completely preclude combined access to BEIP or BRRAG and the tax credit in the same project. In fact, at least as to BEIP, the language is somewhat more nuanced. Participation in the Urban Transit Hub tax credit program restricts companies from 'using the same capital investment, employees, and site' that are used for a BEIP grant. An example illustrates the potential opportunity: If a company is creating 500 new jobs, and otherwise qualifies for the tax credit, it arguably could apply 250 jobs to the tax credit program, and still obtain BEIP grants for the remaining 250 jobs – i.e., at the same site, but *not* the same jobs and capital investment. (The statute appears to more conclusively preclude using BRRAG in conjunction with the tax credit.)

The regulations remain ambiguous on some of these questions, and we will be continuing discussions with the Governor's office, Commerce and EDA to obtain clarification. Given the \$50,000 per job cap on BEIP grants versus the potentially unlimited value of this new tax credit, companies will need to carefully weigh the relative net realizable value of each in formulating their location strategy.

However, many businesses will *not* have enough new employment and capital investment to separately qualify for *both* the tax credit and BEIP in the same project, thus requiring a choice. Such existing BEIP grantees will have to repay a portion of the grants received before they can utilize the credit. BRRAG recipients face the same choice.

- **Job Retention:** If the employment drops below the statutory minimum of 250 employees at the facility, the company forfeits the credit for that year and until the minimum is restored. Similarly, if the requirement of 200 new NJ jobs drops below the minimum, the credit will be reduced by 20% for that year and all subsequent periods until the minimum is restored. Importantly, companies *and affiliates* that reduce *statewide* employment by more than 10% forfeit their tax credit for the given tax period, but can resume the credit if threshold is restored.
- **Full-time Employee:** The definition of a 'full-time' employee was carried over from the BEIP program. Unfortunately, it perpetuates the BEIP limitation on the eligibility of contract employees to those hired only by a professional employer organization (PEO) with which the business has an 'employee leasing' agreement. This excludes many IT contractors on 1099s and employees of vendors who provide services on site.
- **Forfeiture on Sublease:** The statute provided that tenants who sublease their space 'in whole or part' would forfeit *all* future credits – i.e., even a small portion, and even if the remaining leasehold is large enough to qualify on its own. This was illogical, and ignores the realities of the

market place. The regulations remedied this problem: so long as the remaining space continues to qualify, the credit will be pro rated.

REMAINING QUESTIONS: A number of questions remain on which we are following up, but among the most important is how *tenants* determine the value of their tax credit.

- **Tenant Capital Investment:** As noted, large tenants in a qualifying facility also are eligible for the credit so long as their allocable share of the capital investment in the facility exceeds \$25 million. However, accounting for any *additional* capital investment *made directly by a tenant* in their own space remains unclear in the regulations. The most rational and equitable interpretation of the statute and new draft regulations is that the amount of a tenant's tax credit includes *both* its pro-rata share of the owner's capital investment *plus* the full value of its direct capital investment made in its own space. There may be exceptions to this interpretation, on which we are following up with the applicable State officials.

BEST SUITED

The regulations provide further insight that enables us to further refine our view of the types of companies and projects that are best suited to maximize the benefits of the program. These include:

- Companies with a high level of predictable state corporate tax liability (including CBT and gross premium tax);
- Projects with a higher proportion of retained versus new employees (while still meeting the minimum new job threshold); and
- Projects with high capital investments; tenants with above-standard fit out and FF&E costs.
- Balancing the risks and rewards, companies creating new jobs that pay high salaries may find that BEIP grants generate more reliable net realizable value than the new tax credit. Although certain large projects with > 250 new jobs may qualify for both the tax credit and BEIP.
- Mixed use developments: Although occupants of residential, hotel and retail space will generally not be eligible for the credit, the capital investment in such space can be counted toward the \$75 million threshold, and large office tenants may receive a pro rata allocation of *that* investment, potentially enabling them to capture premium tax credit value (if they have adequate tax liability), and making mixed use projects especially attractive to large space users. This will advance the State's priority on mixed-use downtown development.

BLS continues to provide input on the draft regulations to make the program more accessible, and thus a more effective economic development tool. Comments are due by June 6, 2008. We also are working with potential end-users and developers to maximize the value of this and other incentives programs. The regulations outline an elaborate application process with which BLS will be assisting prospective participants. Please contact us with any questions.

This summary, which touches on selected topics and does not purport to be complete, is based on preliminary interpretation of information deemed reliable and current as of this date, but is subject to change, and is provided for information purposes only. This does not constitute legal advice and no one is entitled to rely upon the information contained herein. Independent analysis is required of the specific facts of each matter.

