Labhart Miles
consulting group, inc.

States of Affair

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Lenders & Businesses See EZ Green

From the EZ Hiring Credit…to the Sales/Use Tax Credit…to the Net Interest Deduction for Lenders – there are still very good California tax credit benefits available for companies active in one of the state's 39 zones. Zones blanket the state and are concentrated in the metropolitan areas such as the Bay Area, Los Angeles, San Diego, and Sacramento, but are also located in many rural areas.

As previously reported in *States of Affair,* California has some of the most financially lucrative tax credits in the country.

Lender's Net Interest Deduction – Realizing the critical financial impact of getting capital investments into enterprise zone areas, the state permits lenders to deduct the net interest they earn when lending to a commercial business in an EZ. Net interest is defined as ***"the full amount of interest received, less any direct expenses incurred in making the loan."*** The deduction also includes activities such as loans for multi-family housing and apartment buildings which are rental property held for commercial purposes. For a bank located solely in California, **the net tax benefit** from taking this deduction **is over 6%** of the net interest income amount. The challenge many banks face is that it is difficult to determine which loans are made to qualified businesses. Labhart Miles uses a tested methodology to efficiently determine loans made to businesses in qualifying zones.

EZ Hiring Credit – Benefits can be in excess of $31,000 per qualified employee, yet small companies (and sometimes their CPA firms) aren't aware that they qualify. We have been partnering with local CPA firms to bring these benefits to their clients.

EZ Sales/Use Tax Credit – Allowed for sales tax paid on qualified machinery and equipment.

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Inside this issue:

California Tax Amnesty - The Clock is Ticking

Unless you've been a cast member on a reality TV show taking place on a far-away island, you've heard about the California Tax Amnesty program, running now through March 31, 2005. *States of Affair* reported on some of the onerous penalties in our last edition.

Updates:

The Postman Calls - The FTB has sent approximately 31,000 amnesty applications to taxpayers who have pending Notices of Proposed Assessment (NPAs), protests, appeals and settlements in progress. The application instructions imply that the FTB may assess the increased 40% accuracy-related penalty if these taxpayers choose not participate in amnesty.

What Gives? Pending NPAs, protests and settlements with the FTB as of February 1, 2005 (the beginning of the amnesty program) will not be subject to the 40% accuracy-related penalty for any resulting deficiencies. Taxpayers will, however, be subject to the 50% interest penalty on any amounts unpaid as of March 31, 2005 (the end of the amnesty program), because there is no statutory abatement from this penalty.

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Happy Anniversary!

Labhart Miles Consulting Group, specializing in cost effective state and local tax solutions, is pleased to provide this newsletter as a resource for our clients and contacts.

This quarter we celebrate our 3 year anniversary! As we begin our 4th year, we'd like to thank all of our clients that helped us get to where we are today!

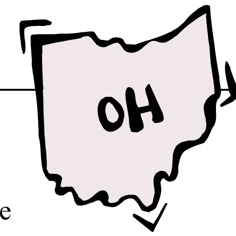
We welcome your comments. If you know of someone who could benefit from this publication, please let us know. For more information, please contact us at

408-266-2259 or www.labhartmiles.com

Bill Labhart & Monika Miles

Special Guest Article - Lawrence Evans, CPA

Ohio Governor Proposes Tax Reform



Governor Bob Taft (Ohio, R) on February 10, 2005 submitted his 2006-2007 Executive Budget to the Ohio General Assembly which includes fundamental tax reform. The reform is meant to improve Ohio's competitiveness and spur economic growth. The Governor's desire is to broaden the tax base, lower rates and reduce the burden on capital investment. Key components of the proposal affecting businesses include:

- Elimination of the Ohio franchise tax over five years (except for the net worth tax on financial institutions).

- Reduction of the tangible personal property tax by eliminating the tax on manufacturing equipment by the tax year 2007 and accelerating the gradual elimination of the tax on inventory to the tax year 2010; furniture, fixtures and other property would remain subject to tax; the public utility property tax would also remain in effect.

- Adoption of a new Commercial Activity Tax (CAT), applicable to all C corporations, which would be phased in over five years. The CAT would tax the gross revenues of all business entities, regardless of their form of organization, at a rate of .26%, with a taxpayer's first $1 million of gross revenue exempt from tax.

- Financial institutions, dealers in intangibles, insurance companies and companies subject to the public utility gross receipts tax would not be subject to the CAT; and pass-through entities would also be subject to the CAT.

- Reduction of the state sales tax from 6% to 5.5%.

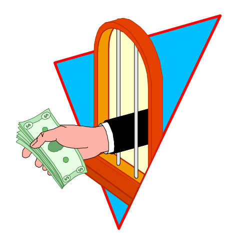
The administration expects high-volume/low margin businesses to object to the tax on gross revenues. However, it is believed that since the tax would be imposed on all similarly situated taxpayers and would replace the franchise and property taxes currently paid by those businesses, there is no good policy reason to start creating exemptions for special interests.

Other significant provisions include: reduction of all personal income tax rates by 21%, ratably over five years; increase taxes on cigarettes, tobacco products and some alcoholic beverages; increase kilowatt-hour tax rates on electric power consumption; a new state real property transfer tax at a rate of 1 mil; and, elimination of the 10% property tax rollback for commercial and industrial real property.

Lawrence Evans, CPA, L.J. Evans & Co., Pepper Pike, OH, provides multi-state tax planning, consulting and controversy assistance. e-mail: www.levans@ljevanscpa.com

Enterprise Zones - What's New? (continued from page 1)

Cross Jurisdictional Vouchering – After recent increased scrutiny by the Franchise Tax Board due to non-uniformity in vouchering, enterprise zones coordinators have collectively agreed to discontinue cross-jurisdictional vouchering (a process by which a zone coordinator in one zone could voucher an employee hired in another zone).



Vouchering Fees - On August 16, 2004, California Senate Bill 1097 was signed into law. SB 1097 authorized additional administrative funding for the State Department of Housing and Community Development (HCD) – the oversight department for the State Enterprise Zone Program. Pursuant to SB 1097, on October 1, 2004, all enterprise zones began to be assessed a $10 fee for each application accepted for issuance of vouchers for the Enterprise Zone Hiring Credit. The zones are pushing these costs down to the companies requesting vouchers, and many zones have begun to assess an additional processing fee per voucher. Additionally, some zones have hired third-party service providers to administer the vouchering process.

EZ Expansions – A moratorium limiting the geographical expansion of existing zones has been lifted. Effective February 28, 2005, HCD will once again begin accepting applications for expansion of zones. In general, expansion areas must have definitive boundaries and be contiguous to an existing enterprise zone. Further, total expansions are limited to 15% of the original designation.

Multi-State Tax News

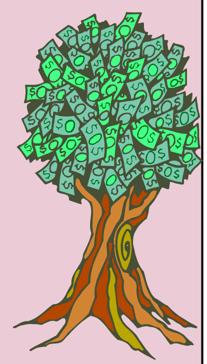
UPDATE: Ohio - *Cuno v. Daimler Chrysler*

As reported in *States of Affair* last quarter, in September 2004, the Sixth Circuit Court of Appeals ruled against the practice of states' offering tax credits as an incentive to encourage corporate investment and employment in targeted areas.

Prompted by questions regarding the challenge to Ohio's tax credit for purchases of new manufacturing machinery and equipment, the state has issued a release updating taxpayers and practitioners. At the present time, ***taxpayers may continue to claim the Ohio tax credit for new manufacturing machinery and equipment and all other tax credits*** that the Ohio Department of Taxation directly or indirectly administers. Because the State petitioned the U.S. Sixth Circuit Court of Appeals to stay the issuance of its mandate in the *Cuno* decision, the State is now free to petition the U.S. Supreme Court to review the circuit court's finding, which earlier enjoined the enforcement of the credit. If the U.S. Supreme Court issues to the U.S. Sixth Circuit Court of Appeals a writ of certiorari, then the U.S. Supreme Court will hear the State of Ohio's appeal of the *Cuno* decision. Federal law does not require the U.S. Supreme Court to issue the writ of certiorari - it is discretionary. If the U.S. Supreme Court does not issue the writ, then there are no further appeals and the decision becomes final. The state would be enjoined from enforcing the credit. The ramifications of this decision could be significant if the parties bringing the suit carry this issue into other states.

Credits & Incentives Updates

Market Watch…Incentive News!



New Mexico lands Aero Mechanical Industries' aircraft production and productions facility with $3.5 million over 10 years using state Jobs Training Grant, high-wage jobs credit and a city of Rio Rancho industrial revenue bond issue. The 150 jobs paid on average $35,000, to ramp up within 3 years.

League City, Texas used $857,000 over five years to encourage BP America to establish its olefins and chemical derivatives headquarters there. With an ultimate employment of 150 people, earning an average of $112,000, the city and state used grants which essentially lets BP America avoid 100% of city personal property taxes for three years and 50% for two additional years.

Glen Cove, New York granted Photocircuits Corp., a maker of computer printed circuit boards, $1.8 million to relocate a manufacturing facility from Georgia. An Empire State Development capital grant and a reduction in rate from the Long Island Power Authority was used for this incentive.

Speaking Out

Public Speaking:

Labhart Miles presented back-to-back meetings in December and January for the Silicon Valley Discussion Group breakfast meetings of the CA Society of CPAs.

Topics: "California Enterprise Zones" and "Nexus"

In Print:

Bill Labhart is an editor for the ***Journal of Multistate Taxation and Incentives***. If you have an article that you would like to submit for future publication, please contact us.

Conference Sponsorship:

Labhart Miles is a sponsor of the Pacific Coast Bankers' Bank 2005 CFO and Investment Conference for Bankers in Newport Beach, CA; March 9 - 11th.

Topics at Breakout Sessions:

"Taking Credit Where Credit is Due"

We invite all attendees to visit our booth!

Please visit our website for helpful links, current updates on other state tax information, and previous copies of our newsletter!

Focus On: Washington "The Evergreen State"

Business Climate:

Washington became the 42nd state to join the Union on November 11, 1889. The state boasts vast tracts of forested land, and timber production is naturally one of the state's economic assets. Nicknamed "the Evergreen State", Washington values its forests for their contribution to both the economy and to the region's ecosystems. The official state tree, the western hemlock, can attain towering size and beauty. It is the 15th largest state, with almost 6 million residents.

Taxes

B&O Tax

Washington does not impose a corporate income or franchise tax. Instead, the business and occupation (B&O) tax is imposed for the privilege of engaging in business activities in Washington. It is not equivalent to an income tax. The B&O tax is based on the value of products, gross proceeds of sale, or gross income of business, according to various business classifications. The tax is imposed upon individuals and entities of any type and there are over 30 taxpayer classifications based on business activity. A taxpayer engaged in different business activities may fall under different classifications and will have to calculate its tax liability using multiple rates.

The state rates vary from .138% to 1.5%. Localities may also impose their own B&O tax in addition to the statewide tax.

Sales Tax

Washington imposes a statewide 6.5% sales tax on most sales and leases of tangible personal property and on sales of specified services. Cities and counties may also levy a local sales-use tax. Thus, total actual rates range from 7.0% to 8.8%

Interaction between the two

Although the B&O tax is separate from the sales and use tax, they are closely intertwined, so cases and rulings affecting one type may be relevant to the other. Many of the main definitional statutes for the sales and use tax cross-reference to similar statutes for the B&O tax.

Credits & Incentives:

There are several credits allowed against the B&O tax, including a small business credit, multiple activities credit, and credit for tax paid to other jurisdictions. Others include:

R&D Credit: Taxpayers in selected high technology industries qualify for the credit. Unlike many states, note that the calculation of Washington's R&D credit is significantly different from the basic federal calculation, in that there is no base year.

Per Advisory Bulletin # 2021.04.24003 (Dec 2004), a "staffing company" whose employees perform qualified R&D activities on behalf of another company, may also qualify for the R&D credit. Only one taxpayer may take the credit but the staffing company may assign the credit to its R&D staffing client.

Rural County Jobs Credit: Companies increasing manufacturing or R&D employment in certain designated rural counties may be eligible for credits of up to $4,000 per person. However, total statewide credits cannot exceed $7.5 million for any fiscal year.

Annual Surveys Due by March 31, 2005: An annual survey must be completed and filed by March 31, 2005, by companies who participate in the programs described above, among others. There is a loss of credit for failure to file this report. Forms are available at http://dor.wa.gov/content/forms/.

Jobs for International Services Activities Credit: Effective July 1, 1998, eligible businesses that provide professional services to international customers are permitted a credit against their B&O tax. The credit is based upon qualified employment positions that provide international service activities in an eligible area. The credit equals $3,000 for each new qualified employment position.

Washington is known as the evergreen state because of its firs and pines, and because the state is always green. Obviously, that is illustrated in Washington's state flag - the only state flag that is green. It is also the only one to feature a picture of a President.

Washington Quotables

"***Success is a lousy teacher. It seduces smart people into thinking they can't lose."*** Bill Gates

"Even castles made of sand, fall into the sea, eventually." Jimi Hendrix, singer/songwriter.

Other Famous Washingtonians: Francis Scobee, astronaut; Bing Crosby, singer/actor; Bob Barker, game show host

CA Amnesty….Continued from page 1

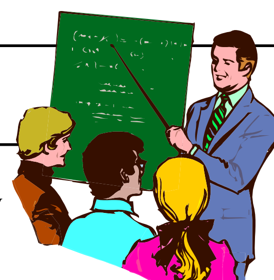
Pre-paying to Avoid Post-Amnesty Penalties - Taxpayers who are currently being audited or are in protest or appeal proceedings for periods prior to 2003 may prepay any potential franchise, or sales/ use tax liabilities to protect themselves against the imposition of the 50% interest penalty that will apply to FTB liabilities beginning April 1, 2005.

Franchise Tax: Taxpayers should consider making these payments outside of the amnesty program because claims for refund may not be filed for any amounts paid through the amnesty program. Make payments to the FTB no later than March 31, 2005, by sending a separate payment, EFT if necessary, along with a claim for refund (Form 540X or Form 100X) for each affected year. Write "Protective Claim" in red at the top of each claim for refund. In the explanation section, state that the protective claim is being filed to reduce the potential interest penalty under R&TC §19777.5.

Sales Tax – For potential BOE liabilities, taxpayers are allowed refund rights for amounts paid through amnesty, which will protect them against both the 50% interest penalty and against the imposition of double penalties on any underreported tax after March 31, 2005. According to the BOE staff, there is no system in place to accept a prepayment outside of the amnesty program, so it is safe to apply for amnesty on all unresolved issues.

As with all programs of this nature, don't wait until the last minute to perform adequate research before acting.

Employment Training Panel Funds



Is your company training employees in California? You may be eligible to receive funding to offset most of the cost of that training. As discussed in previous editions of "*States of Affair*", California's ETP program awards funding to companies engaging in qualified training. The program had been well funded in prior years ($60 to $80 million annually), but had its budget slashed for fiscal years ended 2004 and 2005 to approximately $35 million annually, as funding was diverted to other programs. The expectation is that the fiscal 2006 budget will again be at $35 million.

Funded training includes classroom and computer-based training. The program requires employees to receive a minimum 40 hours of qualified training over a contract period (up to 2 years). Funding is calculated based upon the number of hours of completed training . Recent changes to the program have relaxed requirements on up-front estimates of training, allowing companies to be reimbursed if employees perform training within an acceptable range of hours.

Before receiving funding, a company must be certified eligible, complete an application, and be approved by the 8 member Panel which generally meets monthly. Once approved, funds are distributed as training is completed.

Small business program After much success with a recent Small Business Pilot Project, a larger portion of the budget has been earmarked to target small business applicants employing 100 or fewer employees. Qualifying companies may receive funding for up to 60 hours per employee, and may now apply for a contract up to $50,000. The Program also uses a "fast track contracting process" that is less complicated than the standard program.

We encourage companies that meet the qualifications of either program to put their plans and applications together and be ready to present them to the Panel in June or July in order to have a better shot at a piece of the **$35 million**.

Proposed Legislation for Sales Tax Exemption on Manufacturing Property.

Silicon Valley Senators Elaine Alquist (D) and Abel Maldonado (R), plan to introduce a bill allowing companies a sales tax refund on the purchase of certain manufacturing equipment. Details are still being ironed out, but it's a good start, in addition to a few other similar proposals floating in Sacramento this session.

Most states offer some kind of sales tax exemption for manufacturers. With the sunset of the Manufacturers' Investment Credit ("MIC") in 2003, California is currently left with no such benefit.

MIC "In Lieu" Refunds Authorized: In late January, the SBE granted combined sales tax refunds of over $80 million to 18 companies who had taken advantage of a seldom used sales tax statute. This allowed the companies to receive partial sales/use tax refunds in lieu of claiming the California MIC, (a credit claimed against a company's franchise tax) and effectively accelerated their benefits.

States of Affair" reported on the "In- Lieu" in our Autumn 2003 issue when the first of the refunds were allowed. Monika Miles also published an article in Nov/Dec 2003 *Journal of Multistate Taxation and Incentives* outlining the specifics of the benefit.

Labhart Miles Consulting Group, Inc.
1714 Valpico Drive
San Jose, CA 95124

Phone: 408-266-2259
Fax: 408-323-9571
website: www.labhartmiles.com

State Tax Solutions

Our Mission:
To provide our clients with the highest quality, value-added state and local tax consulting services; to make our client, not the fee arrangement, the focus of our every effort.

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Target Your Tax Savings!

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