

LEGISLATIVE DIGEST

[Initiative Ordinance - Business and Tax Regulations Code - Business Tax Changes]

Motion ordering submitted to the voters an Ordinance amending the Business and Tax Regulations Code to: 1) reduce the annual Business Registration Fee for businesses with \$1,000,000 or less in San Francisco gross receipts, 2) increase the small business exemption ceiling for the Gross Receipts Tax to \$1,500,000 and increase the annual Business Registration Fee on businesses benefiting from this increased exemption ceiling, 3) modify the Gross Receipts Tax rates, 4) repeal the Payroll Expense Tax, 5) increase the Gross Receipts Tax on certain taxpayers for 15 years if a court strikes down the Homelessness Gross Receipts Tax Ordinance, 6) impose a new general tax on the gross receipts from the lease of certain commercial space for 15 years if a court strikes down the Early Care and Education Commercial Rents Tax Ordinance, and 7) make other changes to the City's business taxes; and to increase the City's appropriations limit by the total revenues collected under Articles 12-A-1 and 36 of the Business and Tax Regulations Code for four years from November 3, 2020, at an election to be held on November 3, 2020.

Existing Law

The City imposes a number of taxes under the Business and Tax Regulations Code on persons engaged in business within the City. Among these taxes, the registration fee (Article 12), the payroll expense tax (Article 12-A), and the gross receipts tax (Article 12-A-1) are general taxes, the revenues from which go to the General Fund:

- The registration fee ranges between \$75 and \$35,000 (adjusted for inflation), depending on the type of business and the amount of gross receipts attributable to the City. For persons engaged in business as an administrative office, the registration fee ranges between \$15,000 and \$35,000 (adjusted for inflation), depending on the person's payroll expense attributable to the City.
- The payroll expense tax rate is 0.38% of payroll expense attributable to the City, except for persons that pay the administrative office tax. Small businesses with payroll expense attributable to the City not exceeding \$320,000 are exempt from this tax.
- The gross receipts tax rate ranges from 0.075% to 0.65% of gross receipts attributable to the City, depending on the person's type of business activities and amount of taxable gross receipts, except for persons that pay the administrative office tax. Small businesses with gross receipts attributable to the City not exceeding \$1,170,000 are exempt from this tax in tax year 2019, and this amount is adjusted for inflation annually.
- In lieu of payroll expense and gross receipts taxes, persons engaged in business as an administrative office pay the administrative office tax equal to 1.4% of payroll expense attributable to the City.

Certain persons engaged in business within the City also pay special taxes, the revenues from which are dedicated to specific purposes:

- Persons that receive gross receipts from the lease of commercial space in properties in the City pay the Early Care and Education Commercial Rents Tax (Article 21) at a rate of 1% or 3.5% of those receipts, depending on the type of property. This tax is dedicated 15% to the General Fund and 85% to fund early care and education for young children.
- The Homelessness Gross Receipts Tax (Article 28) is imposed on (1) persons that pay the administrative office tax, at a rate of 1.5% of payroll expense attributable to the City and (2) persons with gross receipts attributable to the City exceeding \$50,000,000, at a rate that ranges from 0.175% to 0.69% of gross receipts attributable to the City in excess of \$50,000,000, depending on the person's type of business activities and amount of taxable gross receipts. This tax is dedicated to fund services for homeless people and to prevent homelessness.

Commencing in 2021, Article 30 will impose an additional tax on persons engaged in cannabis business activities in the City equal to 1% to 5% of the gross receipts from those cannabis business activities in excess of \$500,000, depending on the type of cannabis business activities and the amount of gross receipts from those activities attributable to the City. This tax will be deposited into the General Fund.

Amendments to Current Law

Effective beginning in the 2021-2022 fiscal year, the proposed ordinance would reduce the registration fee of most persons with \$1,000,000 or less in gross receipts attributable to the City by approximately 50%, and increase the registration fee of most persons with \$1,000,000.01 to \$1,500,000 in gross receipts attributable to the City who would benefit from the proposed increase in the small business exemption ceiling for the gross receipts tax (described below) by either \$230 or \$245, depending on the person's business activities.

This ordinance would repeal the payroll expense tax beginning with the 2021 tax year.

This ordinance would modify the gross receipts tax rates, effective beginning with the 2021 tax year, and would incrementally increase the rates for certain business activities as the economy improves, to be triggered in the tax year following the August to July period in which the average monthly unemployment rate drops to the benchmark rates of 7% and 4%, as indicated in the following table:

Business Activity	Current Gross Receipts Tax Rates*	Proposed Gross Receipts Tax Rates*		
		General	7% Trigger	4% Trigger
Certain Services	0.075% to 0.160%	0.053% to 0.168%	No Change	0.105% to 0.224%
Retail Trade	0.075% to 0.160%	0.053% to 0.224%	No Change	0.105% to 0.224%
Wholesale Trade	0.075% to 0.160%	0.105% to 0.224%	No Change	No Change
Manufacturing	0.125% to 0.475%	0.088% to 0.499%	No Change	0.175% to 0.665%
Food Services	0.125% to 0.475%	0.088% to 0.665%	No Change	0.175% to 0.665%
Transportation and Warehousing; Biotechnology; Clean Technology	0.125% to 0.475%	0.175% to 0.665%	No Change	No Change
Information	0.125% to 0.475%	0.560% to 0.784%	0.580% to 0.812%	0.600% to 0.840%
Accommodations; Arts, Entertainment and Recreation	0.300% to 0.400%	0.210% to 0.560%	No Change	0.420% to 0.560%
Utilities	0.300% to 0.400%	0.420% to 0.560%	No Change	No Change
Private Education and Health Services; Administrative and Support Services; Miscellaneous Business Activities	0.525% to 0.650%	0.735% to 0.910%	No Change	No Change
Construction	0.300% to 0.450%	0.420% to 0.630%	No Change	No Change
Insurance	0.400% to 0.560%	0.560% to 0.784%	No Change	No Change
Financial Services; Professional, Scientific and Technical Services	0.400% to 0.560%	0.560% to 0.784%	0.580% to 0.812%	0.600% to 0.840%
Real Estate; Rental and Leasing Services	0.285% to 0.300%**	0.399% to 0.420%	No Change	No Change

* The gross receipts tax is generally progressive, with rates that increase by tiers, depending on the amount of gross receipts attributable to the City. The gross receipts tax is expressed as a range of rates from the lowest tier to the highest tier within each business activity.

** The gross receipts tax rate applicable to taxable gross receipts in excess of \$25,000,000 for the business activities of real estate and rental and leasing services will increase to 0.325% beginning in tax year 2021 if this ordinance does not pass.

This ordinance would increase the ceiling for the small business exemption from the gross receipts tax to \$1,500,000 of gross receipts attributable to the City. This ordinance would eliminate the credit for taxpayers that have paid a substantially similar tax to any other taxing jurisdiction on any gross receipts attributed to the City and taxed under Article 12-A-1. The required quarterly payments of gross receipts taxes for the 2021 tax year would be adjusted upward to take into account the repeal of the payroll expense tax.

This ordinance would retain the administrative office tax rate of 1.4% of payroll expense attributable to the City, in addition to the 1.5% rate currently imposed under the Homelessness Gross Receipts Tax. But that rate would be subject to future incremental increases when the economy improves as measured by declines in the average monthly unemployment to the benchmark rates of 7% and 4%, as shown in the following table:

Current Administrative Office Tax Rate*	Proposed Administrative Office Tax Rate*		
	General	7% Trigger	4% Trigger
1.4%	1.4%	1.47%	1.54%

* This rate is in addition to the 1.5% rate currently imposed under the Homelessness Gross Receipts Tax.

If a court strikes down the Homelessness Gross Receipts Tax, this ordinance would increase the gross receipts tax on certain taxpayers for 15 years, beginning with the tax year following the date on which the court’s decision becomes final. For persons that pay the administrative office tax, the administrative office tax rate would be increased by 1.5% of payroll expense attributable to the City on the top of the rate otherwise in effect. For other persons, there would be added to the gross receipts tax rate tiers an additional rate tier for taxable gross receipts over \$50,000,000 at the rate indicated in the following table for each business activity, plus the applicable rate for taxable gross receipts between \$25,000,000.01 and \$50,000,000:

Business Activity	Tax Rate*
Certain Services; Retail Trade; Wholesale Trade	0.175%
Manufacturing; Food Services; Transportation and Warehousing; Biotechnology; Clean Technology; Information	0.500%
Accommodations; Arts, Entertainment and Recreation; Utilities	0.425%
Private Education and Health Services; Administrative and Support Services; Miscellaneous Business Activities	0.690%
Construction	0.475%

Insurance; Financial Services; Professional, Scientific and Technical Services	0.600%
Real Estate; Rental and Leasing Services	0.325%

* This rate would be added to the applicable rate for taxable gross receipts between \$25,000,000.01 and \$50,000,000.

If a court strikes down the Early Care and Education Commercial Rents Tax, this ordinance would add Article 36 to impose a new general tax for 15 years on the gross receipts from the lease of certain commercial space in the City, substantially similar to the existing Early Care and Education Commercial Rents Tax, except that all revenues from the new tax would go to the General Fund.

This ordinance would increase the City's appropriations limit under Article XIII B of the California Constitution by the total revenues collected under Articles 12-A-1 and 36 of the Business and Tax Regulations Code, for four years from November 3, 2020.

This ordinance also would remove provisions that are no longer in effect, update the existing code language to current formatting standards, and make other changes to the City's business taxes.

Background Information

In June 2018, San Francisco voters by simple majority vote approved Proposition C, which imposes the Early Care and Education Commercial Rents Tax. In November 2018, San Francisco voters, also by simple majority vote, approved Proposition C, which imposes the Homelessness Gross Receipts Tax. Separate lawsuits regarding the validity of the Early Care and Education Commercial Rents Tax and the Homelessness Gross Receipts Tax are pending at the Court of Appeal. Pending resolution of those suits, the Controller has impounded the revenues from both the Early Care and Education Commercial Rents Tax and the Homelessness Gross Receipts Tax.

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