

Item 7 Files 11-1102	Department(s): Office of Economic and Workforce Development Treasurer/Tax Collector
EXECUTIVE SUMMARY	
<p style="text-align: center;">Legislative Objectives</p> <ul style="list-style-type: none"> • The proposed ordinance would amend the City’s Business and Tax Regulations Code to establish a Payroll Expense Tax exclusion for San Francisco businesses that hire ex-offenders. The proposed Payroll Expense Tax exclusion would be a two-year pilot program from January 1, 2012 through December 31, 2013. <p style="text-align: center;">Key Points</p> <ul style="list-style-type: none"> • Businesses with an annual payroll of \$250,000 or more currently pay Payroll Expense Taxes to the City of 1.5 percent of the firm’s payroll expenses for work or services performed in San Francisco. • Under the proposed ordinance, a San Francisco business that hires an ex-offender full-time, or 40 hours per week for at least six months, would be allowed to exclude, one-time, \$675,000 from its payroll expenses for the calculation of Payroll Expense Taxes due to the City. Therefore, if a San Francisco business hires an ex-offender full-time, the business’ Payroll Expense Tax would be reduced by \$10,125, equal to 1.5 percent of \$675,000. • A San Francisco business that hires an ex-offender part-time, or at least 20 hours per week for at least six months, would be allowed to exclude, one-time, \$337,500, from its payroll expenses for the calculation of Payroll Expense Taxes due to the City. Therefore, if a San Francisco business hires an ex-offender part-time, the business’ Payroll Expense Tax would be reduced by \$5,062, equal to 1.5 percent of \$337,500. • According to the legislative digest prepared by the City Attorney’s Office, the purpose of the proposed ordinance is to provide San Francisco employers with a meaningful incentive to employ ex-offenders. According to the legislative digest, studies have shown that when an ex-offender finds employment, the likelihood of the ex-offender re-offending is reduced. <p style="text-align: center;">Fiscal Impacts</p> <ul style="list-style-type: none"> • The proposed ordinance would require estimated one-time General Fund expenditures of approximately \$150,000 by the Treasurer/Tax Collector’s Office for the additional costs to retain an outside consultant to make necessary revisions to the Treasurer/Tax Collector’s Office’s existing Payroll Expense Tax documents. • The proposed ordinance would also result in some additional undetermined costs to the Office of Economic and Workforce Development to promote the proposed Payroll Expense Tax exclusion for hiring ex-offenders and to provide prescreening for ex-offenders. • The Budget and Legislative Analyst cannot estimate the amount of the reduced Payroll Expense Tax revenues to the City as a result of the proposed ordinance because it is not known at this time how many San Francisco businesses would hire ex-offenders in order to receive the proposed Payroll Expense Tax exclusion. 	

- The Budget and Legislative Analyst cannot estimate the potential cost savings to the City because the number of ex-offenders hired by San Francisco businesses in order to be eligible to receive the proposed Payroll Expense Tax exclusion is not known, and the potential reduced Sheriff's Department's costs due to reduced re-incarceration of these ex-offenders, is not known.

Policy Considerations

- If the Board of Supervisors approves the proposed ordinance and elects to continue the Payroll Expense Tax exclusion for ex-offenders at the end of the two-year pilot program, the Budget and Legislative Analyst suggests that the City conduct a more in-depth study on the economic and fiscal benefits associated with employing ex-offenders.

Recommendation

- Approval of the proposed ordinance is a policy decision for the Board of Supervisors.

MANDATE STATEMENT

Mandate Statement

In accordance with the City's Business and Tax Regulations Code Section 902.1¹, San Francisco businesses pay Payroll Expense Taxes to the City of 1.5 percent of the firm's payroll expenses for work or services performed in San Francisco. Each San Francisco businesses' tax liability is determined annually based on the payroll expenses of the entity. Under the Business and Tax Regulations Code Section 905-A, San Francisco businesses with payroll expenses of \$250,000 or less are exempt from Payroll Expense Taxes. Provisions of the Business and Tax Regulations Code that provide additional Payroll Expense Tax exclusions include:

- Sections 906.1 and 906.2 provide Payroll Expense Tax exclusions for businesses engaged in certain biotechnology enterprises and clean energy technology, respectively.
- Section 906.3 provides a Payroll Expense Tax exclusion for certain businesses that are located in or relocate to the Central Market Street and Tenderloin Area.
- Section 906.4 provides a Payroll Expense Tax exclusion for that portion of an eligible person's payroll expense that is attributable to Stock-Based Compensation, expiring December, 31, 2017.

Charter Section 2.105 provides that all legislative acts in San Francisco be by ordinance, approved by a majority of the Board of Supervisors.

¹ Business and Tax Regulations Code Section 902.1(a) specifically defines Payroll Expense as compensation paid to individuals including shareholders of a professional corporation or a Limited Liability Company (LLC), for salaries, wages, bonuses, commissions, property issued or transferred in exchange for the performance of services (including but not limited to stock options), compensation for services to owners of pass-through entities, and any other form of compensation, who during any tax year, perform work or render services, in whole or in part in the City.

DETAILS OF PROPOSED LEGISLATION

The proposed ordinance would amend Article 12-A of the City's Business and Tax Regulations Code by adding Section 906.5 to establish a two-year pilot program, implementing a Payroll Expense Tax exclusion for businesses that hire ex-offenders. The proposed ordinance would become effective with the tax year commencing on January 1, 2012, and expire on December 31, 2013.

Purpose of the Proposed Ordinance

According to the legislative digest prepared by the City Attorney's Office, the purpose of the proposed ordinance is to provide San Francisco employers with a meaningful incentive to employ ex-offenders. According to the legislative digest, studies have shown that when an ex-offender finds employment, the likelihood of the ex-offender re-offending is reduced.

Provisions of the Proposed Ordinance

Under the proposed ordinance, a San Francisco business that hires an ex-offender full-time, or 40 hours per week for at least six months, would be allowed to exclude, one-time, \$675,000 from its payroll expenses for the calculation of Payroll Expense Taxes due to the City. Therefore, if a San Francisco business hires an ex-offender full-time, the business' Payroll Expense Tax would be reduced by \$10,125, equal to 1.5 percent of \$675,000.

A San Francisco business that hires an ex-offender part-time, or at least 20 hours per week for at least six months, would be allowed to exclude, one-time, \$337,500 from its payroll expenses for the calculation of Payroll Expense Taxes due to the City. Therefore, if a San Francisco business hires an ex-offender part-time, the business' Payroll Expense Tax would be reduced by \$5,062, equal to 1.5 percent of \$337,500.

Therefore, to qualify for the Payroll Expense Tax exclusion, businesses must incur payroll expenses of at least \$675,000 per year to hire an ex-offender full time and \$337,500 per year to hire an ex-offender part time.

In order to be eligible for the Payroll Expense Tax exclusion, businesses must (a) complete and submit an initial application to the Mayor's Office of Economic and Workforce Development (OEWD) as prescribed by OEWD; (b) file with OEWD an affidavit to establish entitlement to the Payroll Expense Tax exclusion by January 31 of each year, that must state that each ex-offender who the applicant has hired is not displacing another existing employee; (c) maintain records and documentation in a manner acceptable to the Treasurer/Tax Collector's Office that objectively substantiates the claimed Payroll Expense Tax exclusion; (d) provide all records and documentation to the Treasurer/Tax Collector's Office upon request; and (e) file an annual Payroll Expense Tax Return with the Treasurer/Tax Collector's Office regardless of the amount of tax liability shown on the return after claiming the Payroll Expense Tax exclusion.

Under the proposed ordinance, the Treasurer/Tax Collector's Office would be responsible for adopting rules and regulations for implementing the proposed Payroll Expense Tax exclusion for businesses that hire ex-offenders. The Treasurer/Tax Collector's Office would also be

responsible for (a) verifying all exclusion claims; and (b) submitting an annual report to the Board of Supervisors for each year of the exclusion that includes both the (i) number of exclusions claimed and (ii) aggregate dollar value of the reduced Payroll Expense Taxes due to the City as a result of the exclusions.

Under the proposed ordinance, OEWD would be responsible for (a) conducting on-going outreach and marketing efforts regarding the proposed Payroll Expense Tax exclusion, to inform business owners, ex-offenders, and those who assist ex-offenders in finding employment; (b) submitting an annual report to the Board of Supervisors for each year of the proposed Payroll Expense Tax exclusion that includes (i) the number of businesses that have applied for the exclusion, (ii) the number of businesses that have received the exclusion, and (iii) the number of ex-offenders who have found employment as a result of the exclusion; and (c) coordinating with any and all City and County of San Francisco agencies whose mission includes (i) helping ex-offenders to reenter society, or (ii) administering programs available to ex-offenders who are reentering society.

FISCAL ANALYSIS

Prospective Businesses and Payroll Tax Impacts

As noted above, under the proposed ordinance, a San Francisco business that hires an ex-offender full-time would be allowed to exclude \$675,000 per year from its payroll expenses for the calculation of Payroll Expense Taxes due to the City. Therefore, if a San Francisco business hires an ex-offender full-time, the business' Payroll Expense Tax would be reduced by \$10,125 per year, equal to 1.5 percent of \$675,000.

A San Francisco business that hires an ex-offender part-time would be allowed to exclude \$337,500 per year from its payroll expenses for the calculation of Payroll Expense Taxes due to the City. Therefore, if a San Francisco business hires an ex-offender part-time, the business' Payroll Expense Tax would be reduced by \$5,062 per year, equal to 1.5 percent of \$337,500.

To receive a Payroll Expense Tax exclusion for more than one ex-offender, the firm must have at least an additional payroll expense of (a) \$675,000 per full-time ex-offender in order to obtain an additional \$10,125 reduction in Payroll Expense Taxes due to the City and (b) \$377,500 per part-time ex-offender in order to obtain an additional \$5,062 reduction in Payroll Expense Taxes due to the City.

According to Mr. Greg Kato, Policy and Legislative Manager with the Treasurer/Tax Collector's Office, only approximately 5,000 businesses in the City currently report more than \$675,000 in annual payroll expense, which is the minimum annual payroll expense for a business to receive the full exclusion for one ex-offender employee.

According to Ms. Jennifer Matz, Director of the Mayor's Office of Economic and Workforce Development (OEWD), as of the writing of this report, OEWD cannot identify prospective San Francisco businesses that would participate in the proposed Payroll Expense Tax exclusion for

hiring ex-offenders. According to Mr. Kato, the Treasurer/Tax Collector's Office does not have information on how many businesses currently employ, or plan to employ, ex-offenders. Therefore, the Treasurer/Tax Collector's Office cannot estimate how many businesses would qualify for the proposed Payroll Expense Tax exclusion for hiring ex-offenders.

Because the City does not have information on the number of San Francisco businesses that would participate in the Payroll Expense Tax exclusion for hiring ex-offenders, the Budget and Legislative Analyst cannot estimate the reduction in Payroll Expense Tax revenues due to the City. A program implemented by the City of Philadelphia in 2007 provides a \$10,000 one-time tax credit to Philadelphia businesses that hire ex-offenders and provide tuition support or vocational training. The City of Philadelphia reports 12 businesses have applied for the one-time payroll tax credit, totaling \$120,000.

Potential Cost Savings

According to Ms. Maureen Gannon, Sheriff's Department Chief Financial Officer, the annual cost to San Francisco of a prisoner in county jail is \$46,720 (\$128 per day x 365 days). However, because the number of ex-offenders that would be hired by San Francisco businesses, in order to be eligible to receive the proposed Payroll Expense Tax exclusion is not known, and the potential reduced Sheriff's Department's costs due to reduced re-incarceration of these ex-offenders, is not known, the Budget and Legislative Analyst cannot estimate the potential cost savings to the City.

Administrative Impacts and Costs

The Mayor's Office of Economic and Workforce Development has pledged to work with City agencies that work with ex-offenders, such as the Adult Probation Department and the Public Defender's Office, as well as conduct outreach to local businesses that may benefit from the Payroll Expense Tax exclusion. Ms. Matz states that OEWD would incur some additional costs to promote the proposed Payroll Expense Tax exclusion for hiring ex-offenders and to provide prescreening for ex-offenders. Ms. Matz does not have specific estimates of such additional costs at this time.

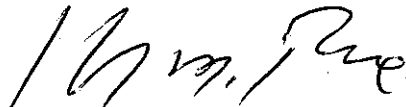
Under the proposed ordinance, each business would be required to file an annual Payroll Expense Tax return with the Treasurer/Tax Collector's Office regardless of the amount of the business's tax liability, after claiming the proposed Payroll Expense Tax exclusion. Mr. Kato states that the Treasurer/Tax Collector's Office would incur an initial one-time General Fund expenditure of approximately \$150,000 for the additional costs to retain an outside consultant to make necessary revisions to the Treasurer/Tax Collector's Office's existing Payroll Expense Tax documents.

POLICY CONSIDERATIONS**In-Depth Study of the Economic and Fiscal Benefits of Employing Ex-Offenders in San Francisco is Necessary**

The proposed ordinance would establish a two-year pilot program to allow San Francisco businesses to receive a Payroll Expense Tax exclusion for hiring ex-offenders. If the Board of Supervisors approves the proposed ordinance and elects to continue the Payroll Expense Tax exclusion for ex-offenders at the end of the two-year pilot program, the Budget and Legislative Analyst suggests that the City conduct a more in-depth study on the economic and fiscal benefits associated with employing ex-offenders. In 2011, the city of Philadelphia produced a similar study, the *Economic Benefits of Employing Formerly Incarcerated Individuals in Philadelphia*, prepared by the Economy League of Greater Philadelphia.

RECOMMENDATION

Approval of the proposed ordinance is policy decision for the Board of Supervisors.



Harvey M. Rose

cc: Supervisor Chu
Supervisor Mirkarimi
Supervisor Kim
President Chiu
Supervisor Avalos
Supervisor Campos
Supervisor Cohen
Supervisor Elsbernd
Supervisor Farrell
Supervisor Mar
Supervisor Wiener
Clerk of the Board
Cheryl Adams
Controller
Rick Wilson