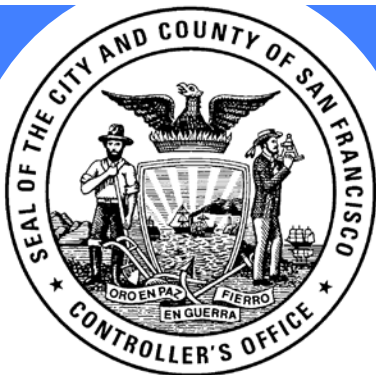


# Overview of Revised Business Tax Proposals



**CITY & COUNTY OF SAN FRANCISCO**

Office of the Controller

July 16, 2020

## Overview

In June, two modifications to the City's business tax were introduced through the Board legislative process, one by Mayor Breed and the other by President Yee with Supervisors Fewer, Haney, and Peskin.

This overview compares the two measures pending in committee today, including proposed amendments to them.

Two other measures were submitted directly to the Department of Elections, one by the Board sponsors and the other by the Mayor. They are not included in this comparison.

## Key Features of the Two Measures

1. Both measures unlock revenue collected from Big and Baby C through voter-adoption of a backstop tax that would go into effect only if the City loses the litigation on those taxes.
2. Both measures complete the retirement of the payroll tax and replace it with a revenue-neutral increase to gross receipts tax rates.
3. Both measures provide permanent tax relief for small businesses and temporary relief for targeted industries. The form of this relief varies between the two measures.
4. Both measures equalize rates for the information and professional services sectors in 2021.
5. Both measure increases rates on certain sectors, although the timing, level, and breadth of those increases varies.

## Today's Amendments to BOS Measure

1. Increases small business exemption to \$2.0 million
2. Expands industries subject to temporary tax relief
  - Adds hospitality, food services, arts, entertainment, and recreation
3. Reduces level of ultimate tax rate increases and delays them
  - Ultimate rate increases reduced from 30% to 15-20%, varying by industry
  - Phases increases between 2022 and 2024, rather than full increase in 2021
  - Adds trigger to delay 2023 and 2024 increases if receipts don't recover
4. Extends duration of backstop tax from 10 to 20 years
5. Merges Charter baseline changes for the backstop tax into the measure

## Big & Baby C Backstop Tax Feature

1. Many businesses are currently paying Big C and Baby C taxes, but these funds are impounded and cannot be spent by the City because of pending litigation.
2. Both measures create a “backstop” tax that would increase revenues to the General Fund that could be appropriated to refund claims and provide some ongoing revenues in the event the City loses the litigation. This would permit the Controller to release currently impounded funds.
3. The Mayor’s proposal enacts a 15-year backstop tax. With today’s amendments, the Board’s backstop tax would extend for 20 years.
4. The Charter amendment, combined into the Board’s measure in the amendments today, excludes the revenue from the backstop tax for baseline calculations, similar to the current status of Big C and Baby C taxes. This increases revenue available to pay refunds and to support these services, should the lose the litigation.

## Payroll Tax Repeal

1. In both proposals, the payroll tax will be repealed in 2021, and most tax-paying businesses will pay only the gross receipts tax.
2. To offset the lost revenue from the payroll Tax, current gross receipts rates would increase by 40%. This is a revenue-neutral swap.

## Information Sector

1. Both proposals would increase the gross receipts tax rates on the Information sector to equalize them with the rates paid by schedule 6 industries: Financial Services, Professional Services, and Insurance. Apportionment rules would not change.

## Small Business Tax and Fee Reductions

1. Both measures reduce registration fees for businesses with \$1 million or less in San Francisco gross receipts.
2. Both measures increase the small business exemption (the level under which businesses are not subject to the tax) beginning in 2021:
  - The Mayor's proposal increases the exemption to \$1.5 million, exempting an additional 1,800 businesses from the tax.
  - The Board's amended version increases the exemption to \$2.0 million, exempting an additional 3,000 businesses.

## Temporary Tax Reductions

1. Both measures provide temporary tax relief for certain cost-sensitive and impacted industries.
2. With amendments to the Board's versions, both measures apply to manufacturing, retail, other services, hospitality, food services, arts, entertainment, and recreation sectors.
3. For these sectors, the Board's version provides a 50% reduction for adjusted rates on the first \$25 million of a business's receipts for tax years 2021 and 2022, and then a 25% for 2023.
4. The Mayor's version applies similar but not identical rate reductions, with economic triggers rather than specific dates determining their duration.



## Future Rate Increases

1. Both measures provide future tax rate increases for certain sectors, although the rate of increase, the timing of them, and their application across sectors vary.
2. The Mayor's measure proposes a phased ultimate increase for professional services, information, financial services, and administrative offices of 10%, in two 5% stepped increases that would be enacted when unemployment drops below specified levels.
3. The Board's measure, as amended, proposes a phased ultimate increase for a broader set of sectors of between 15% and 20% depending on the sector. These increases would occur in three stepped increases in 2022, 2023, and 2024. Increases in 2023 and 2024 would be deferred by one year if specified gross receipt conditions are not met.
4. Rates for the Board version are included in this presentation's appendix.

## Revenue and Spending Impacts

The revenue and spending benefits to the City vary between the two measures, but share the following components:

- **Shorter-term.** The backstop tax feature in both measures would permit the City to spend currently-assessed taxes of approximately \$1.5 billion through fiscal year 2022-23, comprised of approximately \$1.2 billion for childcare and homeless services and \$300 million in General Fund repayments.
- **Longer-term.** On full phase-in, the rate restructuring in the two measures would generate additional ongoing revenue each year. The Mayor's proposed measure would generate approximately \$20 million on full phase-in while the Board's amended version would generate approximately \$100 million.
- **Other benefits.** Beyond the estimates above, the City would gain other financial benefits, including but not limited to avoided revenue losses from expected shifts in the tax base and ongoing revenue and spending benefits from the backstop tax, for both the General Fund and childcare and homeless services.

## Questions or Comments?

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## Appendix: Board-Version Amended Rate Changes by Industry (slide 8 detail)

	<u>2022</u>	<u>2023</u>	<u>2024</u>
Accommodations	No Change	No Change	No Change
Activity Not Listed Above	10.00%	15.00%	20.00%
Administrative and Support Services	5.00%	10.00%	15.00%
AOT	5.00%	10.00%	15.00%
Arts, Entertainment, and Recreation	No Change	No Change	No Change
Biotechnology	5.00%	10.00%	15.00%
Certain Services	No Change	No Change	No Change
Clean Technology	No Change	No Change	No Change
Construction	No Change	No Change	No Change
Financial Services	10.00%	15.00%	20.00%
Food Services	No Change	No Change	No Change
Information	10.00%	15.00%	20.00%
Insurance	5.00%	10.00%	15.00%
Manufacturing	No Change	No Change	No Change
Private Education and Health Services	5.00%	10.00%	15.00%
Professional, Scientific, and Technical Services	10.00%	15.00%	20.00%
Real Estate and Rental and Leasing Services	5.00%	10.00%	15.00%
Retail Trade	No Change	No Change	No Change
Transportation and Warehousing	No Change	No Change	No Change
Utilities	5.00%	10.00%	15.00%
Wholesale Trade	No Change	No Change	No Change

*\* Rate increases in 2023 and 2024 subject to one-year delay if specified economic conditions are not met.*