FILE NO.

LEGISLATIVE DIGEST

[Initiative Ordinance – Business and Tax Regulations Code – Enact Gross Receipts Tax and Phase Out Payroll Expense Tax]

Ordinance amending the Business and Tax Regulations Code to: 1) enact a new Article 12-A-1 (Gross Receipts Tax Ordinance) to impose a gross receipts tax and an administrative office tax on persons engaging in business activities in San Francisco; 2) amend Article 12-A (Payroll Expense Tax Ordinance) to reduce business payroll expense tax rates based on the amount of gross receipts tax collected under Article 12-A-1 (Gross Receipts Tax Ordinance); 3) amend Article 12 (Business Registration Ordinance) to establish business registration fees based on gross receipts and amend the current business registration fees to generate approximately $28.5 million in estimated additional revenue; 4) amend Article 12-A (Payroll Expense Tax Ordinance) to add a sunset date to the surplus business tax revenue credit; and 5) amend Article 6 (Common Administrative Provisions) to establish requirements for filing a tax return under Article 12-A-1 (Gross Receipts Tax Ordinance), establish penalties for non-filing, and amend the requirements for filing payroll expense tax returns and penalties for non-filing to conform to the new gross receipts tax

Existing Law

The City and County of San Francisco currently imposes a tax on the payroll expense of persons who conduct business in the City. The tax is levied at a rate of 1.5 percent against a business's taxable payroll expense, which includes all compensation a person pays to individuals for services performed in the City. The City exempts small businesses with less than $250,000 in payroll expense.

Amendments to Current Law

The legislation phases in a gross receipts tax gradually, over a five-year period that commences with tax year 2014. The phase-in period allows businesses time to adjust to the gross receipts tax. It also minimizes risk of revenue uncertainty to the City, and to business taxpayers as a whole. Also beginning in tax year 2014, the payroll expense tax will be phased out in increments consistent with the phase in of the gross receipts tax, and is expected to be phased out completely in tax year 2018. If the gross receipts tax generates revenue in excess of that expected during the phase-in process, the payroll expense tax will be phased out early and final gross receipts tax rates will be permanently established at less than the maximum rates authorized by this Ordinance. If, on the other hand, gross receipts tax revenues are less than expected, then the payroll expense tax will not be fully phased out, and a reduced payroll expense tax rate will remain at the end of the process. Beginning tax year 2014, a business whose predominant activity in the City is providing administrative services for itself or a related entity will continue to pay a tax based on its payroll expense instead of on its gross receipts. All tax proceeds would be deposited in the General Fund and could be expended for any purpose of the City.

Section 2 provides that the Ordinance will be submitted to qualified electors at the November 6, 2012 general election.

Section 3 enacts new Article 12-A-1, the Gross Receipts Tax Ordinance, as specified. The proposed Gross Receipts Tax Ordinance would impose a tax for the privilege of engaging in a business in the City that is measured by the taxpayer's gross receipts from business activities that are attributable to the City. The rate of the gross receipts tax is dependent upon a business's activities and the rates are progressive within each industry group. A business predominantly engaged in the City in providing administrative services for itself or a related entity would pay a fixed rate of tax measured by its payroll expense. Businesses with less than $1 million in gross receipts would be exempt from the gross receipts tax. The $1 million threshold is indexed for inflation. The gross receipts tax is to be phased in over a five-year period and during that period, the City's payroll expense tax will be phased out. The value of certain exclusions under the current payroll expense tax are carried forward into the gross receipts tax.

Section 4 provides that all sections of this Ordinance are operative beginning tax year 2014, except for the amendments to the Business Registration Ordinance, which are operative on the effective date of this Ordinance.

Section 5 amends the Business Registration Ordinance under Article 12 to establish business registration fees for 2014-2015 based on payroll expense, to establish business registration fees for registration years beginning after June 30, 2015 based on gross receipts to generate an additional $28.5 million in revenue, and to index the business registration fees for inflation. It also amends current business registration fees to add a penalty for failure to register business locations and fictitious business names with the Tax Collector, and to add a new fee for registering more than 15 fictitious business names.

Section 6 amends the Payroll Expense Tax Ordinance under Article 12-A to conform the payroll expense tax rates to the phase in of the Gross Receipts Tax Ordinance and provide a sunset date for the existing surplus business tax revenue credit.

Section 7 amends the Common Administrative Provisions set forth in Article 6 of the Business and Tax Regulations Code. The amendments to Article 6 amend return and payment requirements and otherwise conform the administrative provisions to the provisions of the Gross Receipts Tax Ordinance and the amendments to the Payroll Expense Tax Ordinance.

Section 8 provides that the effective date of this legislation is 10 days after the date the official vote count is declared by the Board of Supervisors.

Background Information

San Francisco is the only major city in California that levies its entire business tax on payroll expense. This payroll-based tax raises an affected business's cost of hiring a worker in San Francisco, and thereby discourages job creation. Instituting a tiered rate structure under which a business is taxed based on its gross receipts will better distribute the tax burden among the City's businesses.

A gross receipts tax is the most common business tax base among California's largest cities. Replacing the payroll expense tax in San Francisco can be expected to stimulate employment in the City, as well as broadening and stabilizing the tax base.