



AGENDA REPORT

FINANCE DEPARTMENT

DATE: August 5, 2020

TO: Mayor Butt and Members of the City Council

FROM: LaShonda White, Acting Deputy City Manager for Internal Services
Belinda Brown, Finance Director
Antonio Banuelos, Accounting Manager
James Atencio, Senior Assistant City Attorney

SUBJECT: CONSIDERATION OF GROSS RECEIPTS BUSINESS TAX BALLOT
MEASURE FOR NOVEMBER 3, 2020 ELECTION

STATEMENT OF THE ISSUE:

Staff is requesting that the City Council consider placing a measure on the November 3, 2020 ballot changing the Business License Tax calculation methodology to be based on gross receipts in the City of Richmond instead of number of employees.

RECOMMENDED ACTION:

REVIEW the draft measure for the November 3, 2020 ballot which would amend the City's business tax rate structure to authorize the City to tax businesses based on a range of .06% to 5.00% of gross receipts rather than rates based on the number of employees and either: (1) ADOPT a resolution placing the measure on the November 3, 2020 ballot; or (2) PROVIDE DIRECTION to staff on further revisions to the draft measure and continue engagement with the business community with the intent to place the measure on the ballot at a future election.

FINANCIAL IMPACT OF RECOMMENDATION:

The new methodology would charge the highest rates on businesses with the most gross revenue, with exemptions for specific businesses, as identified in the ordinance. If the measure passes, it would provide an estimated \$3.2 million annually in new revenue to the City, based on historical sales tax and rental property data. Staff projects that the City would incur one time implementation costs as well as annual costs for ongoing

staffing needs generated by the ordinance. New revenue would not be received by the City until FY2021-22.

There is a cost of approximately \$8,000 - \$10,000 per 10 pages of printed material to put this measure on the ballot. The ballot measure costs could come from the City Clerk's election budget.

DISCUSSION:

On December 17, 2019, the Mayor brought an item to the City Council, directing City staff to explore potential revenue enhancement and cost-recovery measures. Staff brought a comprehensive revenue enhancement matrix to Council for review and discussion during the FY 2020-21 budget cycle and the proposed ballot measure is one such opportunity.

On July 21, 2020, the proposed ballot measure item was presented to the City Council. Council directed staff to reach out to the local business community prior to the next council meeting on July 28, 2020. On July 28, 2020, Council reviewed an updated draft measure for the November 3, 2020 ballot which would amend the City's business tax rate structure to authorize the City to tax businesses based on a range from 0.075% to 1.395% of gross receipts instead of charging based on the number of employees (not including firearms and cannabis). After discussion and hearing from the business community, Council directed staff to bring back the ordinance during a special Council meeting, with a progressive schedule based on the Berkeley model, tailored to the economics of the City of Richmond.

Partnership with Lift Up Richmond – Revenue Ballot Measures

During the FY 2020-21 budget development process, the City asked for union support in finding ways to increase revenue and help address the City's structurally unbalanced budget. As a result, a coalition called Lift Up Richmond¹ was created and began to explore the feasibility of placing measures on the November 2020 ballot that would increase revenue. Lift Up Richmond hired FM3 Research to conduct polling of 411 potential Richmond voters between June 16 – 23, 2020. Participants were asked questions about their likelihood of voting for three measures: gross receipts, vacant parcel tax and documentary transfer tax.

All of the ballot measures proposed and tested in the poll would generate new revenue for the city to support and protect services for Richmond youth, libraries, parks, community centers, emergency response, and other city services that may see cuts due to a structural budget deficit compounded by COVID-19 related revenue shortfalls. Although all three revenue measures polled well, a decision was made to focus on the gross receipts measure in the November 2020 election because the parcel tax would

¹ The Lift Up Richmond coalition consists of SEIU Local 1021, Richmond Police Officers Association (RPOA), IAFF Local 188, IFPTE Local 21, RYSE, Alliance of Californians for Community Empowerment (ACCE), Asian Pacific Environmental Network (APEN), and many more community and labor advocates.

require 2/3 voter approval to pass and the transfer tax had the lowest approval and revenue projections.

Proposed Ballot Measure Language

The official ballot question for the measure is proposed to read as follows:

“To maintain the quality of life in Richmond by providing essential City services, including 911 emergency response, pothole/street repair, homeless and youth services and other general services, shall an ordinance amending the City business tax structure to use a range from 0.06% to 5.00%, charging the highest rates on cannabis businesses and those with high gross revenue and the lowest rates for small businesses, providing approximately \$6.2 million annually until ended by voters, be adopted?”

Gross Receipts Model

The current ordinance, as proposed, was initially based on the ordinance which Oakland is currently studying and is scheduled for the November 2022 ballot. However, after additional research, input from the business community, and City Council direction, City staff updated the ordinance to better meet the needs of Richmond (Attachment 2). As written, Richmond’s proposed measure would generate an estimated \$3.2 million annually in additional revenue.

Currently, the business license tax in most cases is based on the number of employees. The base rate is \$234.10 per year and goes up per each employee a business has working in Richmond (the first 25 employees are charged at \$46.80 per employee, and employees above 25 are charged at a rate of \$40.10 per employee). The cannabis industry (at 5%) and movie theaters (at 0.3% for revenues over \$20,000) are currently based on gross receipts.

The new model would calculate the business license tax based on the amount of gross receipts (total amount of money received in connection with any sale) in Richmond by the business and then charging a specific percentage based on the type of business and the amount of revenue generated.

The key components of the proposed ordinance include:

- Lower charge for small businesses - With the current ordinance, all businesses pay the base rate of \$234.10 and the tax only goes up if they have employees. With this proposed ordinance, small businesses or any business generating less than \$250,000 in gross receipts, would only have to pay \$200. This does not apply to rental properties. This would allow these businesses to still pay less than the current business license rate but would increase the revenue collected by the City. Any business has the option of paying on gross receipts even if the total due is less than \$200.
- Different rates are applicable to different business categories (see ordinance).
- Within the business categories, the rates are progressive meaning that the higher the dollars in sales, the higher the rate.

- Businesses will be allowed to self-report information (under penalty of perjury), but the City has the ability to audit the information provided.
- Liens may be placed on the business for unpaid business tax.
- Specific exemptions are included in the ordinance.

The ordinance, as prepared, currently includes the rates as recommended per Option 1. The ordinance includes the following exemptions and City Council may add additional exemptions:

- Non-profit educational institutions
- Religious Institutions
- New affordable housing development
- Buildings rented by the City
- Child day care

Options for consideration

Based on Council direction from the July 28, 2020 meeting, staff was directed to bring back an ordinance with a progressive schedule based on the Berkeley model, tailored to the economics of the City of Richmond. Staff is bringing forth five (5) different options. It is important to note that the rates included in any of the options can be modified up or down prior to adoption on August 5, 2020, or rates can be reduced after the ballot measure is passed.

Option 1 – RECOMMENDATION: Berkeley Rate as Floor and 1% Rental Rate

Option 1 below, which is staff’s recommendation, uses the Berkeley rate as a floor/base and includes a flat 1.00% rate with a .50% rate for property owners subject to rent control.

Industry	Recommendation - Potential Proposed Richmond Rates (Berkeley Rates as Floor & 1% Rental Rates)				
	\$0-\$1 Million	\$1M-\$2.5M	\$2.5M-\$25M	\$25M-\$50M	\$50M+
Retail Sales	0.12%	0.16%	0.20%	0.24%	0.32%
Grocers	0.06%	0.10%	0.13%	0.15%	0.20%
Automobile Sales, Manufacturing	0.12%	0.22%	0.31%	0.41%	0.50%
Recreation and Entertainment	0.45%	0.46%	0.47%	0.48%	0.50%
Hotel/motel	0.18%	0.28%	0.38%	0.48%	0.50%
Construction contractor	0.18%	0.21%	0.24%	0.27%	0.30%
Business and personal services	0.18%	0.27%	0.36%	0.50%	0.54%
Professional/semi-professional service	0.36%	0.41%	0.45%	0.50%	0.68%
Administrative headquarters (payroll based, not gross receipts)	0.12%	0.15%	0.19%	0.22%	0.24%
Miscellaneous	0.24%	0.31%	0.38%	0.45%	0.48%
Residential Rentals	1.00% with 50% discount for properties subject to rent control (.50%)				
Commercial Rentals	1.00%				
Firearms Ammunition	2.40%				
Taxi and limousine service	\$75 for each ambulance or limousine and \$180 for each taxicab permit				
Transportation, trucking	Tax based on current employee total				
Cannabis (Medical/Non-Medical)	5.00%				

This proposed rate structure is estimated to bring in approximately \$6.2 million in total revenue (\$3.2 in new revenue).

Residential Rental Property Table

Staff spoke with the Association of United Housing Providers and the Contra Costa Association of Realtors regarding the impact of the proposed rental fees on both residential and commercial property owners. We discussed various options for consideration including if the structure should be tiered or flat, or if the rates should be based on gross receipts or number of units. The current rates for different cities include:

- Richmond: \$234 per location
- Berkeley: 1.081% and 2.88% (based on # of units)
- Oakland: 1.395% (flat)
- San Francisco: .285%, .3% and .6% (tiered model based on gross receipts)

Staff is recommending a semi-tiered model with a flat rate charged to the property owners based on gross receipts (similar to Oakland’s current model) but that provides a 50% discount to property owners that have units subject to rent control. This model is administratively feasible to implement, and provides a substantial break to property owners that are subject to rent control.

This proposed residential rental rate structure is estimated to provide the City with an additional \$1.4 million over our current revenue of \$1.4 million (shown as #6 in table below). A similar revenue increase of \$1.3 million could also be reached by instituting a flat .75% rate across the board, with no discounts for properties subject to rent control (shown as #2 in table below). Council can chose between either option, if the estimated revenue target is desired, or any other rate structure. Council will have the ability, after additional analysis and feedback, to lower these rates, if deemed necessary.

	<u>New Total Projections:</u>	<u>Est. Total BL Revenue</u>	<u>Current BL Rev Collected</u>	<u>Difference</u>
1	Flat 0.50%	\$1,800,000	\$1,400,000.00	\$ 400,000
2	Flat 0.75%	2,700,000	1,400,000.00	1,300,000
3	Flat 1.00%	3,600,000	1,400,000.00	2,200,000
4	Flat 1.50%	5,400,000	1,400,000.00	4,000,000
	<u>Using SF Model with 50% discount for those with Rent Control:</u>			
5	0.375%/0.75%	1,900,000	1,400,000.00	500,000
6	0.50%/1.00%	2,800,000	1,400,000.00	1,400,000
7	0.75%/1.50%	4,300,000	1,400,000.00	2,900,000

Option 2 - Berkeley Rates as Floor/Base and 1.5% Rental Rate

Staff used the Berkeley rates as a floor or base, and increased the rates as the tiers increased. The residential rental rate is set at 1.5% with the 50% discount to property owners that have units subject to rent control. The commercial rental rate is set at 1%. This proposed rate structure is estimated to bring in approximately \$7.7 million in total revenue (\$4.7 million in new revenue).

Industry	Potential Proposed Richmond Rates (Berkeley Rates as Floor & 1.5% Rental Rates)				
	\$0-\$1 Million	\$1M-\$2.5M	\$2.5M-\$25M	\$25M-\$50M	\$50M+
Retail Sales	0.12%	0.16%	0.20%	0.24%	0.32%
Grocers	0.06%	0.10%	0.13%	0.15%	0.20%
Automobile Sales, Manufacturing	0.12%	0.22%	0.31%	0.41%	0.50%
Recreation and Entertainment	0.45%	0.46%	0.47%	0.48%	0.50%
Hotel/motel	0.18%	0.28%	0.38%	0.48%	0.50%
Construction contractor	0.18%	0.21%	0.24%	0.27%	0.30%
Business and personal services	0.18%	0.27%	0.36%	0.50%	0.54%
Professional/semi-professional service	0.36%	0.41%	0.45%	0.50%	0.68%
Administrative headquarters (payroll based, not gross receipts)	0.12%	0.15%	0.19%	0.22%	0.24%
Miscellaneous	0.24%	0.31%	0.38%	0.45%	0.48%
Residential Rentals	1.50% with 50% discount for properties subject to rent control (.75%)				
Commercial Rentals	1.00%				
Firearms Ammunition	2.40%				
Taxi and limousine service	\$75 for each ambulance or limousine and \$180 for each taxicab permit				
Transportation, trucking	Tax based on current employee total				
Cannabis (Medical/Non-Medical)	5.00%				

Option 3 - Berkeley Rates as Midpoint and 1% Rental Rate

Staff used the Berkeley rates as the midpoint, and decreased the rates for the tiers less than \$2.5 million and increased the rates as the tiers increased over \$25 million. The residential rental rate is set at 1.0% with the 50% discount to property owners that have units subject to rent control. The commercial rental rate is set at 1%. This proposed rate structure is estimated to bring in approximately \$5 million in revenue (\$2 million in new revenue).

Industry	Potential Proposed Richmond Rates (Berkeley Rates as Midpoint & 1% Rental Rates)				
	\$0-\$1 Million	\$1M-\$2.5M	\$2.5M-\$25M	\$25M-\$50M	\$50M+
Retail Sales	0.07%	0.10%	0.12%	0.14%	0.19%
Grocers	0.03%	0.05%	0.06%	0.07%	0.10%
Automobile Sales, Manufacturing	0.05%	0.08%	0.12%	0.16%	0.19%
Recreation and Entertainment	0.43%	0.44%	0.45%	0.46%	0.48%
Hotel/motel	0.09%	0.13%	0.18%	0.23%	0.24%
Construction contractor	0.14%	0.16%	0.18%	0.20%	0.23%
Business and personal services	0.09%	0.14%	0.18%	0.25%	0.27%
Professional/semi-professional service	0.29%	0.32%	0.36%	0.40%	0.54%
Administrative headquarters (payroll based, not gross receipts)	0.08%	0.10%	0.12%	0.14%	0.15%
Miscellaneous	0.15%	0.20%	0.24%	0.28%	0.31%
Residential Rentals	1.00% with 50% discount for properties subject to rent control (.50%)				
Commercial Rentals	1.00%				
Firearms Ammunition	2.40%				
Taxi and limousine service	\$75 for each ambulance or limousine and \$180 for each taxicab permit				
Transportation, trucking	Tax based on current employee total				
Cannabis (Medical/Non-Medical)	5.00%				

Option 4 – Berkeley Rates as Ceiling and .75% Rental Rate

Staff used the Berkeley rates as a ceiling, and decreased the rates as the tiers increased. The residential rental rate is set at .75% with the 50% discount to property owners that have units subject to rent control. The commercial rental rate is set at 1%. This proposed rate structure is estimated to bring in approximately \$3.4 million in revenue (\$400,000 in new revenue).

Industry	Potential Proposed Richmond Rates (Berkeley Rates as Ceiling & .75% Rental Rates)				
	\$0-\$1 Million	\$1M-\$2.5M	\$2.5M-\$25M	\$25M-\$50M	\$50M+
Retail Sales	0.05%	0.06%	0.08%	0.09%	0.12%
Grocers	0.02%	0.03%	0.04%	0.05%	0.06%
Automobile Sales, Manufacturing	0.03%	0.05%	0.07%	0.10%	0.12%
Recreation and Entertainment	0.41%	0.41%	0.42%	0.43%	0.45%
Hotel/motel	0.06%	0.10%	0.14%	0.17%	0.18%
Construction contractor	0.11%	0.13%	0.14%	0.16%	0.18%
Business and personal services	0.06%	0.09%	0.12%	0.17%	0.18%
Professional/semi-professional service	0.19%	0.22%	0.24%	0.26%	0.36%
Administrative headquarters (payroll based, not gross receipts)	0.06%	0.08%	0.09%	0.11%	0.12%
Miscellaneous	0.12%	0.15%	0.19%	0.22%	0.24%
Residential Rentals	.75% with 50% discount for properties subject to rent control (.375%)				
Commercial Rentals	1.00%				
Firearms Ammunition	15.00%				
Taxi and limousine service	\$75 for each ambulance or limousine and \$180 for each taxicab permit				
Transportation, trucking	Tax based on current employee total				
Cannabis (Medical/Non-Medical)	5.00%				

Option 5 – Oakland’s Proposed Rates

Staff used the Oakland rates, that is currently being discussed and is planned for the November 2022 ballot. The residential rental rate is set between 1.081 to 2.880%. The commercial rental rate is set at 1%.

Industry	Proposed Oakland Rate with Berkely Rental Rates (1.081% - 2.880%)				
	\$0-\$1 Million	\$1M-\$2.5M	\$2.5M-\$25M	\$25M-\$50M	\$50M+
Retail Sales	0.075%	0.10%	0.125%	0.15%	0.20%
Grocers	0.060%	0.10%	0.125%	0.15%	0.20%
Automobile Sales, Manufacturing	0.125%	0.225%	0.325%	0.425%	0.525%
Recreation and Entertainment	0.45%	0.46%	0.47%	0.48%	0.50%
Hotel/motel	0.18%	0.28%	0.38%	0.48%	0.50%
Media firms	0.18%	0.28%	0.38%	0.48%	0.50%
Public utility	0.18%	0.28%	0.38%	0.48%	0.50%
Construction contractor	0.30%	0.35%	0.40%	0.45%	0.50%
Business and personal services	0.20%	0.30%	0.40%	0.55%	0.60%
Professional/semi-professional service	0.40%	0.45%	0.50%	0.55%	0.75%
Administrative headquarters (payroll based, not gross receipts)	0.35%	0.45%	0.55%	0.65%	0.70%
Miscellaneous	0.35%	0.45%	0.55%	0.65%	0.70%
Residential Rentals	1.081%-2.880%				
Commercial Rentals	1.081%				
Firearms Ammunition	2.40%				
Taxi and limousine service	\$75 for each ambulance or limousine and \$180 for each taxicab permit				
Transportation, trucking	Tax based on current employee total				
Cannabis (Medical/Non-Medical)	5%				

Impact on Residential Rental Providers

If there is a desire to increase the revenue, then staff could adopt the City of Berkeley’s model for the taxation of rental properties. The Berkeley model charges 1.081% for the first four rental units and 2.881% for 5 units and above. This proposed tiered system, although giving small property owners a discount, could potentially yield an additional \$4.2 million per year. Staff shared this idea with the business community and were informed that this rate was too high and would be extremely detrimental to small housing providers (under 10 units). City staff included this rate in the option 5 – Oakland model – as the rates align with Oakland’s higher rates.

Potentially impacted residential rental property owners shared that the tiered and lower rates used by San Francisco would be more palatable (tiered model based on gross receipts - .285%, .3% and .6%). The impact of adopting the Berkeley model (1.081% to 2.880%) for residential property owners, would significantly increase the expenses that property owners are responsible to pay to the City. It is also important to note that the City currently charges property owners of rental units the following:

- Current business license
- Rent control fees
- Rental inspection fee
- Rent moratorium (many rental property owners are not currently receiving rent)
- Fire inspection fees (in some cases)
- Property taxes (depending on the outcome of the proposed Community and Schools ballot measure, some property owners may have sustainably higher property taxes)
- Sewer fee increases

Along the same lines, other businesses pay or have to adhere to the following:

- Current business license
- Property taxes
- Utility User Taxes
- 1% for public art on private projects
- Inclusionary housing ordinance(ranging from 12.5% - 25% of housing units should be available for low income household or pay or in-lieu fee)
- Impact fees (i.e. park and library fees)
- Various planning fees (comprehensive planning fee, design review fee, CEQA)
- Local employment (25% requirement)
- Business opportunity (25% local and small business)
- Ban the box
- Living wage and minimum wage
- Zoning ordinance

Business Community Outreach and Feedback

Per City Council direction, staff reached out to the business community to garner their input in this process:

- Staff is connecting with various City departments that have connections to the Richmond business community and requesting feedback on outreach and the ordinance
- The proposed draft ordinance has been posted in the Finance Department section of the City webpage
- Meetings with representatives and members from the Council of Industries, Richmond Chamber of Commerce, Richmond Main Street, Association of United Richmond Housing Providers, and Contra Costa Association of Realtors
- Hosted two virtual business community meetings on Tuesday, July 28th at 10:00pm and Monday, August 3rd at 5:30pm
- Outreached via various methods and to business organizations
- Received numerous emails and engaged in telephone calls with impacted stakeholders and included recommendations into the proposed ordinance

Based on staff's interaction with the business community, staff would like to highlight the following feedback:

- Language is too complicated and additional clarification is needed
- Process feels rushed
- Bad timing due to COVID-19 impacts
- Don't mind paying their "fair share" but the City has to take into consideration the current fees paid by business to the City and the state of the economy
- Lack of authentic engagement and input
- Establish a committee and consider special election or Nov. 2022
- Like the Berkeley model as ceiling
- Possibility of phasing in the impact of the tax increase
- Staff should consider including 1-10 units as mom & pop property owners under the "small business" classification

- Concerned that council will not reduce rates or make other changes once approved by voters

Implementation Considerations for Any New Business License Model

- Implementation Date – Per the ordinance, council has the ability to push the start date back if additional time is needed for implementation.
- Outreach and Education – The City will need to provide information on the impact of the ordinance on those most impacted by its implementation.
- Consistent Business License Period – Currently, the majority of the business license accounts expire on December 31st. The City will need to transition those businesses that do not expire on December 31st to this new format. One option to implement this is by prorating their 2021 business tax obligation. For example, a business with a license that expires in March would only pay 75% of the Business License Tax due. Once that payment is received, their new expiration date will be December 31. The new amounts due will be solely based on amounts of revenue generated and reported to the Internal Revenue Service and Franchise Tax Board.
- Staffing and tracking needs – If approved, the implementation of this measure will be labor intensive for Finance staff both at the outset and on an ongoing basis. Staff will need to return to City Council to discuss the need for additional staffing, as well as the need for a comprehensive database for tracking compliance.
- Enhanced Revenue Collection Enforcement – The new ordinance contains language to allow staff to both lien and then levy unpaid business license tax and have it collected through the Contra Costa County property tax assessment.

Next Steps

Based on a majority vote, the City Council has the flexibility to: (1) defer implementation, (2) reduce the rates, and (3) add exemptions. If desired, Council could direct staff to continue conversations with the business community and place the gross receipts tax on the ballot for an upcoming special election in either March 2021 or June 2021. The estimated cost to the City would be between \$75,000 and \$150,000. It is important to note that the off-cycle elections do not garner the same level of voter turnout as during a presidential election cycle.

If approved by City Council and passed by the voters, the new progressive business license tax would take effect July 1, 2021 (with an option by Council to defer implementation, if needed). Therefore, the City would not receive any new revenue until FY2021-22. The City needs to transition all business to an expiration date of December 31. This will allow both businesses and staff to accurately compute the amount due each year. The City will continue receiving business tax revenue in FY2020-21 but only based on the number of employees. The actual business tax rate changes will not start

until customers with a license expiration date of December 31, 2021 start paying the tax for 2022.

Ballot measure timeline:

- Last day to place a measure on the ballot August 7, 2020
- Last day to amend or withdraw a measure August 12, 2020
- Impartial Analyses Due August 14, 2020
- Last day to file Primary Arguments August 19, 2020
- Election Day November 3, 2020

ATTACHMENTS:

Attachment 1 – Gross Receipts Tax Resolution

Attachment 2 – Gross Receipts Tax Ordinance