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June 26, 2020

The Honorable Mayor London N. Breed, Board of Supervisors President Norman Yee,
and City Controller Ben Rosenfield
San Francisco City Hall
1 Dr. Carlton B. Goodlett Place
San Francisco, CA 94102

Re: Business and Tax Regulations Code

Dear Mayor Breed, Board President Yee, and City Controller Rosenfield,

On behalf of the San Francisco Chamber of Commerce and the thousands of businesses we represent, I write to you regarding the City's upcoming proposed business tax overhaul. Over 80% of our members at the San Francisco Chamber are small businesses, and a majority of our member businesses are owned by people of color and women. We are proud that our businesses, ranging from cannabis dispensaries, tourist attractions, hotels, technology innovators, and neighborhood restaurants, represent and contribute to the heart and diversity of San Francisco.

The businesses of San Francisco and their employees make up a critical portion of the City's budget through their tax dollars. With this in mind, the **San Francisco Chamber of Commerce and our members must oppose the ballot measures increasing business taxes proposed last Tuesday.**

Our businesses and their hundreds of thousands of employees are deeply concerned about the health and well-being of San Francisco - we are ready to work to find a way to raise revenue responsibly to help protect critical City services. However, the tax increases proposed come exactly at the wrong time for our economy. It will hurt our small, local businesses and worsen the unemployment crisis.

An overhaul of the business tax structure should be thoughtful and deliberate. It can have profound impacts on our local economy. If done badly, it can punish small businesses, deepen unemployment, and create further economic inequality. In 2012, it took City leaders, stakeholders, and the business community over nine months to plan our initial overhaul of the business tax structure. We now attempt to do a business tax overhaul in nine weeks.

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In a recent survey conducted by the San Francisco Chamber of Commerce, approximately 70% of large and small businesses said that the overall City tax burden and future potential business tax measures play a major role in deciding whether to continue to hire in San Francisco or relocate jobs elsewhere.

San Francisco has already seen anchor businesses move across the bridge and out of the state. As these businesses leave, they take their jobs and tax revenue with them. Business taxes are the second-largest source of revenue for the City's general fund, bringing in $1 billion annually. We are concerned for the loss of tax revenue in our City budget if businesses continue to leave San Francisco in larger numbers.

Beyond the usual high cost of doing business, we are now in a global pandemic. Our survey of small business members during the first three weeks of the pandemic reported that 47% had either lost 100% of their sales or closed their businesses entirely. Transaction data shows that the retail, restaurant, and accommodation industries have seen a 95% drop in activity since March.

There are more San Franciscans out of work now than at any time in recent history, including the Great Recession of 2008. More than 140,000 residents have filed unemployment claims. Several major employers have allowed their workforces to remain remote through 2021. These employment trends have downstream impacts on our small businesses. Small businesses have lost thousands of customers overnight, and it is not clear when those customers will return. Introducing new business taxes when San Francisco has not even fully reopened the economy threatens our already fragile small business community.

The proposed business tax increases will drive large employers and their tax revenue out of San Francisco, but ultimately small and mid-sized businesses will be impacted the most. Those local businesses will not have the ability to relocate or avoid the taxes, and will bear the brunt of the tax increase. Businesses such as grocery wholesalers, accommodations, and retailers are prime examples. These industries generate high gross receipts with a high volume of sales, but with very low profit margins. They have also seen a sharp decline in business due to the COVID-19 pandemic and are struggling to recover. Without careful consideration, the transition from payroll tax to gross receipts tax will disproportionately impact small and mid-sized businesses and put these essential industries at risk of closing their doors.

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While we cannot support the business tax increases, we believe that if City leaders are going to move forward with a business tax overhaul, the following technical amendments should be considered and included. These technical amendments come from the Tax Working Group hosted by the San Francisco Chamber of Commerce over the past several weeks.

1. **Life Science Research and Development Dollars**.
   Research and development stage biotechnology companies do not have gross receipts as a result of sales. Though the companies may receive funding from various sources for research and development, those companies often do not have a product on the market.

   While there is an existing exemption of pre-commercial funding for life science companies, we are requesting a modification to bring parity for other sources of funding as a result of equity exchange. Whereas pre-commercial investments such as venture capital are currently not taxed, other forms of funding that life science companies receive during R&D and clinical trial phases are taxed. Thus, we are seeking to equalize the tax code by adding these other sources of pre-commercial funding to the category of what is not included in gross receipts.

   "Gross receipts" should not include any amounts received:
   a. *as a grant from a non-profit entity, or*
   b. *by a biotechnology, manufacturing, or clean technology business, as referenced in Section 953.2, where such amounts*
      i. *do not result from the commercial sale of a product;*
      ii. *are received from third parties as up-front payments, milestone payments, cost or expense reimbursements, or other payments related to or result from research or development activities for investigational products (including manufacturing of investigational products evaluated in research and development activities including clinical trial supplies); and*
      iii. *are related to a research and/or development contract, license agreement, intercompany agreements, collaboration agreement, joint venture arrangement or similar agreement, in each case, where intellectual property rights or an option to such rights are, or have been, licensed, granted or otherwise transferred to the payor.*

2. **Amendment for Payment Processors**
   When a transaction is made online or in-person, there are multiple fees collected by a payment processor in addition to its own fees, which include bank fees and credit card fees that are ultimately passed on to various financial institutions. Payment processing companies are currently forced to calculate these pass-through fees as their own gross receipts. Those companies only keep a fraction of the gross receipts collected from payment processing, yet pay the San Francisco business tax on the entire amount of gross receipts collected. This can also cause those dollars to be taxed twice - once as the fees are collected by the payment processor, and again when the fees are passed onto the bank or credit card company.

   We would ask for an amendment that would clarify that payment processors would not have to calculate funds that they are simply passing through to another financial institution as part of their total gross receipts.

   Gross receipts, as defined in Section 952.3, generated from the processing of payments shall be reduced by any credit card, banking, or other payment processing-related fees associated with generation of gross receipts.

3. **Amendment for Real Estate Brokerages**
   During a real estate transaction, real estate brokers often collect the entire commission from the transaction and then pass-through the appropriate funds to their independent real estate agents. These brokerages only keep a fraction of the entire commission, but pay the SF business tax on the entire amount of gross receipts collected. This also causes those dollars to be taxed twice - once when the entire commission is collected by the brokerage, and again then the commission is passed onto the real estate agent, who is taxed on it as an independent contractor.

   We would ask for an amendment that would clarify that real estate brokerages would not have to calculate funds that they are simply passing through to their independent real estate agents as part of their total gross receipts.

4. **Backstop Tax for Homelessness Gross Receipts Tax and Commercial Rents Tax**
   The revisions to Section 953.7(d) in the Mayor and the Supervisors' gross receipts tax proposals seem to say that the backstop for the homelessness gross receipts tax would apply to all of the taxpayer's real estate gross receipts over $50 million, including both rental receipts and receipts from real estate services.

   However, Section 2805(c) of the existing Homelessness Gross Receipts Tax (passed in November 2018) says it would not apply to gross receipts subject to the commercial rent tax (passed in June 2018).

   We think that any backstop tax created by a November 2020 ballot measure should reflect the same exemptions as the original Homelessness Gross Receipts Tax, and should not have rental receipts to be subject to both the backstop Commercial Rents Tax and the backstop Homelessness Gross Receipts Tax.

   Section 953.7 should specify that gross receipts that are subject to the existing commercial rents tax under Article 21 or the newly proposed commercial rents tax under Article 36 are not included in gross receipts under Section 957.3(d).

5. **Clarification on Information Services Rates in the Supervisors Proposal**
   It is our understanding that the tax rate increase in Information Services is meant to reflect a 40% increase for the elimination of the payroll tax and another 30% for increased revenue. In Section 953.2(a)(1)(D), the starting rates for the Information category are .125%, .205%, .37% and 0.475%; and these rates increase to 0.68%, 0.782%, 0.867% and 0.952% in the Supervisors tax proposal. The written rates seem substantially higher than the 40% and 30% tax increase outlined. We would like clarification on why the tax rates for Information Services may be higher than the public policy description outlined, or if there is another principle being used to calculate the category tax rate.

The San Francisco Chamber of Commerce's goal is to create a progressive economy that supports all residents. Our members want to support reforms that put our City and its residents first.

Our local businesses provide salaries, healthcare, and benefits to hundreds of thousands of people in San Francisco. During this critical time, it is important to recognize that a job with benefits is the best and most sustainable way to ensure our residents have high-quality healthcare. Stabilizing and creating jobs in San Francisco must be our top priority.

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We are in the midst of a major public health crisis and at the start of a recession that may last several years. Our economic landscape is shifting permanently and these changes will have a profound impact on our City, small businesses, and residents. Our small businesses and workers need predictability and stability from their local government.

This is the time for long-term economic planning and recovery, not short-term attempts to fill in a growing budget deficit. We hope that City leaders will partner with the business community to pursue responsible policies that will allow San Francisco to survive this pandemic, and rebuild a progressive economy.

Respectfully,

Rodney Fong
CEO & President
San Francisco Chamber of Commerce