



Proposition C: San Francisco Gross Receipts Tax Increase

CALTAX RECOMMENDATION: VOTE NO ON PROPOSITION C

The California Taxpayers Association urges San Francisco residents to vote “no” on Proposition C on the November ballot. The measure includes flawed tax policies that would increase the cost of living and doing business in San Francisco, and is being used by the San Francisco government in an attempt to circumvent the state constitution.

DIGEST

This local initiative would impose an additional gross receipts tax (GRT), on top of San Francisco's existing GRT, for businesses with annual receipts of \$50 million or more. For businesses not subject to the existing GRT, but subject to San Francisco's payroll tax, Proposition C would impose an additional payroll tax of 1.5 percent. Many of the increased costs on employers likely would be passed along to consumers in the form of higher retail prices for products and services used by San Franciscans, or would cause employers to reduce wages or job opportunities. The payroll tax increase would create a new disincentive for employers to hire in San Francisco, thereby limiting job opportunities for San Franciscans, including those who are trying to escape homelessness or are at risk of becoming homeless.

MAJOR PROVISIONS

Tax Provisions

- **Additional Gross Receipts Tax.** The initiative imposes an additional annual GRT on any person engaged in business in San Francisco who receives or is a member of a combined group that receives \$50 million or more in total taxable gross receipts in a tax year. The portion of receipts over \$50 million is subject to tax. The tax rate would range from 0.175 percent to 0.69 percent, depending upon the business' activities.
- **Payroll Tax.** For businesses not subject to the existing GRT, but instead subject to San Francisco's payroll tax, the initiative imposes an additional tax of 1.5 percent on payroll expenses.
- **Tax Collector Authorized to Determine Gross Receipts.** The office of the San Francisco tax collector may use its discretion to establish a person or combined group's

gross receipts within San Francisco, or reallocate receipts among related entities to determine taxable receipts occurring in San Francisco.

- **Exemption.** Legal entities exempt from income and franchise taxes under state and federal law are exempt from the proposed GRT. Also exempt are businesses with receipts from warehouse, commercial and industrial leases that already pay the additional GRT approved by voters in June 2018.

Spending Provisions

- **Intent.** The measure expresses intent to house at least 4,000 homeless people and expand shelter beds by 1,000, provide legal assistance to residents, and subsidize rents within five years.
- **Administrative Costs.** The local government would be authorized to spend up to 3 percent of the revenue for administrative costs.
- **Ballot-Box Budgeting.** After paying for administrative costs, government oversight of expenditures and refunds of overpayments, the revenue generated from the new tax would be earmarked for specific purposes:
 - 50 percent – Mayor’s Office of Housing and Community Development for more programs related to homelessness.
 - 10 percent – Short-term shelters, bathrooms, handwashing stations and showers.
 - 15 percent – Mayor’s Office of Housing and Community Development for more services for people “at risk of becoming homeless.”
 - 25 percent – Department of Public Health for more mental health programs.

FISCAL IMPACT

According to San Francisco’s Office of Economic and Workforce Development, the tax would cost San Francisco employers subject to the GRT approximately \$280 million to \$300 million annually.

POLICY CONSIDERATIONS

Gross receipts taxes lack transparency, fairness and competitive neutrality, and should not be imposed. This tax seeks to make San Francisco’s existing gross receipts tax more targeted and even less competitive.

San Francisco already is a high-cost city for businesses and residents, and by increasing the costs, Proposition C would encourage employers to consider moving jobs and investments to other cities or states where their operational costs would be considerably lower.

Additional considerations:

- **Special Taxes Require a Two-Thirds Vote.** This is a special tax that should have a two-thirds vote requirement, not a simple majority threshold. San Francisco officials are attempting to strip residents of their constitutional protections.
- **Double Taxation.** San Francisco already imposes a gross receipts tax. This initiative would impose an additional tax on the same receipts already subject to tax.
- **Distorts Business Decisions.** This tax would negatively influence business decisions, including location, operations, and movement of goods and supplies. Gross receipts taxes effectively create “tax pyramiding” by taxing all levels of production of goods, products and services.
- **Significant Tax Burden on New Businesses.** This tax places a significantly greater tax burden on start-up businesses, businesses with low margins, and unprofitable firms. Generally, a GRT is more difficult to pass on to consumers, leading to lower wages and fewer employment opportunities. GRTs also have a significant impact on businesses that are not vertically integrated.

CONSTITUTIONAL VIOLATION

This measure – a special tax that earmarks funds for a specific program – was placed on the ballot by homeless housing advocates through the initiative process. California’s constitution states that special taxes such as this can be imposed only if approved by at least two-thirds of the electorate. Despite this constitutional requirement, San Francisco officials issued an opinion that only a majority vote of the electorate is needed to approve this measure.

In October 2017, the San Francisco city attorney opined that a measure imposing a special tax placed on the ballot through the initiative process is not subject to the constitution’s vote requirements, citing a decision by the California Supreme Court in *California Cannabis Coalition v. City of Upland*. In that case, the court found that a citizens’ initiative is not subject to the same election timing rules as a measure placed on the ballot by a local governing body. The opinion did not specifically mention vote requirements for local taxes.

San Francisco officials followed the city attorney’s erroneous analysis in June, and deemed two special taxes to have passed even though neither received at least two-thirds of the vote. Taxpayers are challenging the constitutionality of those taxes, and litigation is pending.