County Of San Benito

Business Tax Analysis and Ordinance Review
Report Date: July 15, 2018

DRAFT – V1.1

Prepared By:

Business License Tax Analysis and Ordinance Review

Project Overview

The County of San Benito has contracted with the HdL Companies to analyze the current ordinances and tax structures as they relate to business tax and make certain recommendations and analysis to accomplish the specific goals of the review. While the County has existing tax codes related to business tax, the codes are not currently in effect and have not been charged or tracked by the County.

Specific Goals

The County has identified the following key items that will be addressed in this report.

1. Review current ordinances for any items that may be carried over including classifications, definitions, and overall structure.
2. Develop options for implementing a new business tax and create options for multiple tax structures for review.

Data

HdL has compiled data from the County, State, City, and other 3rd party sources for use in the analysis and estimates contained within the report. As the data may have come from 3rd parties, the data cannot be certified by HdL and should be treated as estimates and not actual values.

Report Sections

The report is divided into three sections designed to simplify the review process. The first section will provide background, data analysis, and other comparative information for reference and use in recommendations and impact sections. The second section will cover the review of the current ordinance and identify potential changes that may facilitate the County's stated goals as well as enhance operations for the County. The final section will cover proposed rate modifications and the potential impact of those changes. Additional items requested by the County, and information or recommendations not covered elsewhere in the report, can be found in the additional information section at the end of this report.

SECTION 1 – County of San Benito & Surrounding Jurisdictions

County of San Benito Business License Tax Background

The County had a business license tax in the past, however while the code still exists, it is currently not being assessed. The tax was a hybrid of flat fee plus a variable rate depending on classification of the business. Data from the old business license tax was not available for use in this review, requiring the use of estimates for the analysis of options. Revenues from the old program are estimated to have been in excess of $200K, and primarily came from the business tax related to mining operations.

In conducting analysis of the County and similar jurisdictions it is important to note that traditionally, counties do not have strong business tax ordinances. Business licenses in California typically fall in to one of two categories, revenue generating or regulatory. Counties by far fall in to the regulatory category and typically have little revenues from business license and taxes.

Revenue vs Regulatory

Regulatory licenses, as are predominant in most counties, are designed to regulate business activity and provide approvals for a business to operate at a particular location. They exercise control over the activity, rather than the taxation of the activity. Fees for regulatory licenses are usually tied to a cost basis and tied in to a master fee schedule or similar instrument. This typically means a jurisdiction is only allowed to charge as much as the program costs to administer.

Revenue licenses are true taxes and by contrast, typically are not an approval or license to operate like their regulatory counterparts. Most jurisdictions that have revenue generating licenses, also have regulatory licenses and permits, to address the control over certain activities such as massage and taxi cabs. The County's existing code language is a hybrid of revenue and regulatory, though the revenue piece, as previously stated, is not currently active.

Comparative Jurisdictions

HdL has conducted a review of multiple jurisdictions where business licenses are assessed, to provide background of how cities and counties are taxing their businesses and identify common taxation practices. Because counties typically don't have a tax based license, HdL has cited two of the Cities from within the county for use in analysis and drawing comparisons. Additionally, neighboring counties were reviewed, but provided little benefit for comparative analysis due to business make-up and varying business license structures. The regulatory nature of many counties prevents direct comparisons on revenue and taxation structures.
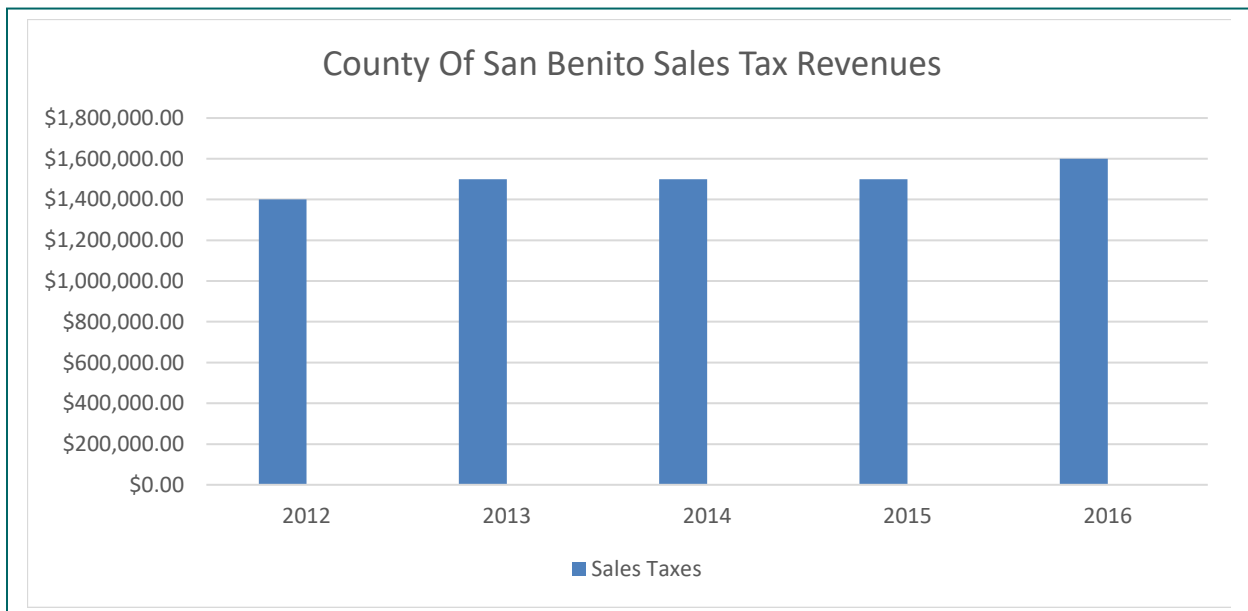
County of San Benito Buisiness Analysis

County Of San Benito - Estimated Business Make Up By Primary Type

- 32.1%
- 10.7%
- 14.3%
- 7.1%
- 35.7%

■ 1. Retail / Misc   ■ 2. Services   ■ 3. Professionals   ■ 4. Rental Properties   ■ 5. Contractors

County Of San Benito Sales Tax Revenues
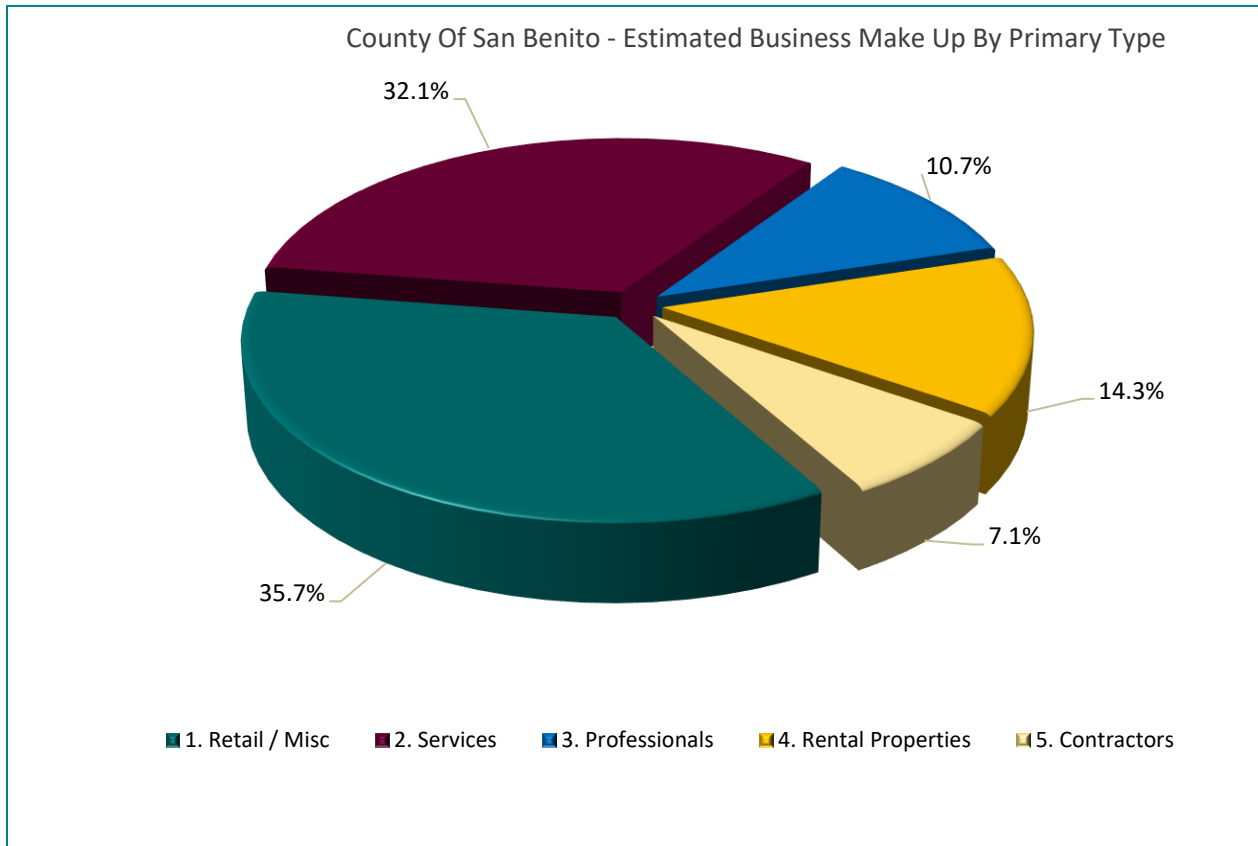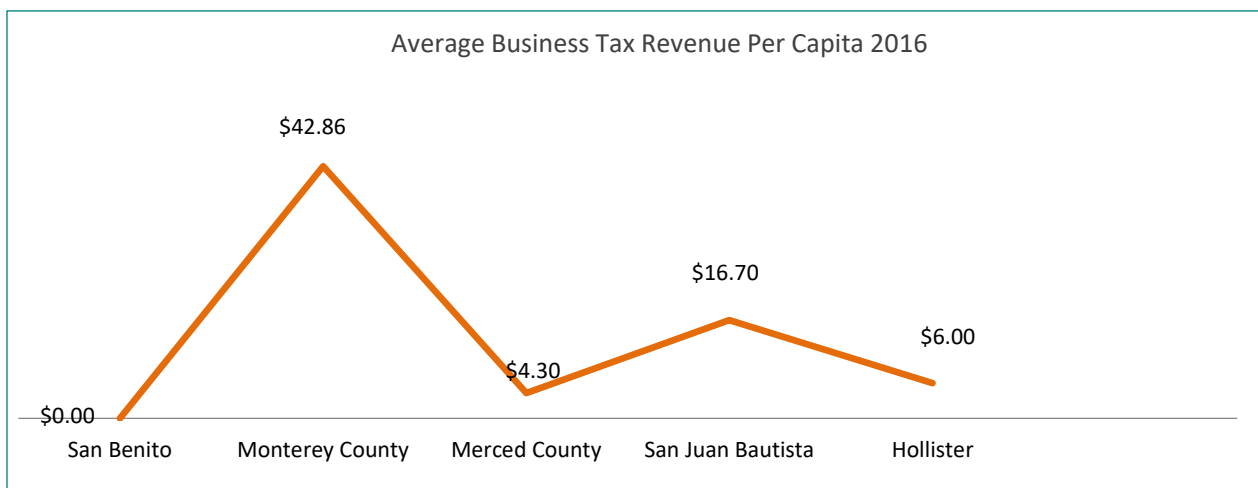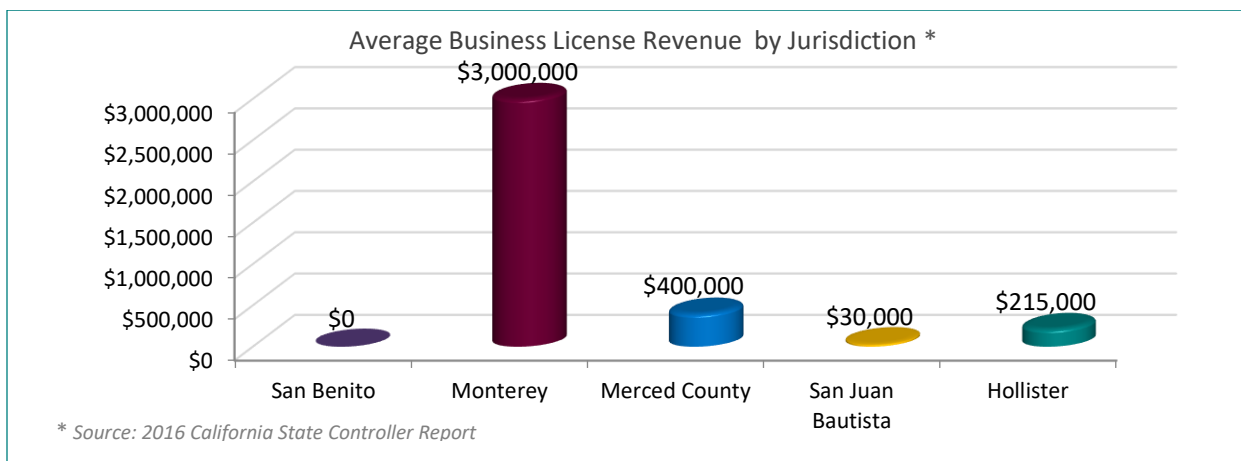

■ Sales Taxes

Table 1 – County of San Benito: Existing Business Tax Rate Schedule (Not in Use)

Classification	Rate Type	License Fee
(A) Retail / Wholesale / Misc,	Flat + Emps	$99.00 + 2.20 per employee
(B) Services / Property Rental & Entertainment	Flat + Emps	$99.00 + $4.5 per employee
(C) Professionals	Flat + Emps	$99.00 + $6.50 per employee
(D) Itinerant Vendors	Flat + Emps	$25.00 + $0.55 per Employee
(E) Mining Operations	Flat + Tonage	**$99.00 + $0.05 per Ton**

Similar and Surrounding Jurisdictions

Average 2016 Population by Jurisdiction

Jurisdiction	Population
Hollister	36,000
San Juan Batista	1,800
Merced County	93,000
Monterey County	70,000
COSB	19,000

Average Business License Revenue by Jurisdiction *

Jurisdiction	Revenue
San Benito	$0
Monterey	$3,000,000
Merced County	$400,000
San Juan Bautista	$30,000
Hollister	$215,000

Source: 2016 California State Controller Report

Average Business Tax Revenue Per Capita 2016

Jurisdiction	Revenue Per Capita
San Benito	$0.00
Monterey County	$42.86
Merced County	$4.30
San Juan Bautista	$16.70
Hollister	$6.00

SECTION 2 – Ordinance Modification Options

*PENDING *

This section will contain a line-by-line review of the existing code related to business tax should the County elect to move forward with any of the options outlined in the report. Depending on the option selected, HdL will work with the County to identify potential improvements and modernizations to the code to ensure efficient operations, create a business friendly filing process, and ensure compliance with state and federal laws.

SECTION 3 – Tax Model Options & Analysis

The County has requested that HdL conduct an analysis of the County business inventory and propose structures as they relate to business license taxation. For this section, HdL prepared summaries of each classification of business activity and to the extent data was available, provided a breakout of the number of businesses and their potential contribution to the total tax pool.

In this section HdL has provided options for implementing a variety of tax structures. Using the data compiled on current business activities, models were developed to estimate potential fiscal impacts to the County as well as how those changes may have an effect on the business community.

Data Variables – Grouping by General Type of Business

The County currently has a number of "classifications" that spans across multiple categories. This structure assigns a specific fee to each type of business, listing five different types of businesses and their corresponding fees. While those categories are outlined in the code, the basic fee structures are closely aligned. For the purpose of the analyzing and comparing the options in this section, HdL has compiled data on the business community and estimated the distribution of the community in to these categories.

Grouping	Business Count
Retail / Misc	500
Services	550
Professionals	150
Rental Properties / Entertainment	100
Contractors / Itinerants	100

Data Variables – Mining Activities

HdL has assumed the tonnage calculations and potential revenues for use in calculating potential tax amounts for mining business classifications. HdL used the numbers that were being generated by the prior code as a baseline and allowed for a 30% increase over the numbers to address increase operations.

Option 1 – Existing Categories and Rates With Simple Increases

The County may elect to not modify the existing structure, and continue with the structure currently codified. In addition to keeping the same rates, HdL has shown examples of simple increases to the fee amounts for each category. Keeping the current structure in place would eliminate the need to create different categories and allow for a much simpler implementation for the County.

The County could choose to implement the current numbers, adjust each category separately, increase the rates on a select group, or apply a standard rate increase across the board. An example of an across the board % increase is indicated in the following Option 1 table. **Option 1 – Table A**

Rate Classes Unchanged (with % Fee Increase)

Fee Amount Paid	Number of Accts	Est Current Structure Revenues	20% Increase	40 % Increase	60% Increase
Retail\ Wholesale\ Misc.	500	$55,000.00	$66,000.00	$77,000.00	$88,000.00
Services / Property Rental & Entertainment	650	$74,000.00	$88,800.00	$103,600.00	$118,400.00
Professionals	150	$18,000.00	$21,600.00	$25,200.00	$28,800.00
Itinerant Vendors	100	$4,000.00	$4,800.00	$5,600.00	$6,400.00
Mining Operations	5	$227,000.00	$272,400.00	$317,800.00	$363,200.00
TOTALS >	1,400	$378,000.00	$453,600.00	$529,200.00	$604,800.00

Option 1 – Highlights and Impact Review

As indicated in the Table (A) above, a simple increase in each rate type amount could keep the existing structures in place while yielding various revenues to the County. The County can replace any of the sample % increases with varying degrees of increase or could elect to only apply the increases to certain categories. For example, increasing the rates on manufacturing and residential property rental by 60%, while increasing others rates by 20% or not at all.

This option provides the County with the simplest method of increasing and the most accurate to forecast. Additionally, for those flat fee categories, the County has a standard CPI adjustment to those appropriate categories to ensure the rates stay current over the course of time.

Should the County wish to see specific calculations or examples of specific category rate increases, HdL will provide the calculations and attach as an addendum to this report.

Option 2 -Replace Multiple Categories with Single Gross Receipts Tax

Taxing gross receipts is a common model for California business license. A variety of models are commonly used including a scale method or the use of a standard rate multiplier to determine the tax amount owed. This model can be implemented as a standard rate applying to any business or one that can vary by business class. For example, many jurisdictions elect to charge $1 per thousand dollars of gross receipts (0.001 x Gross) for a retail business, while charging a rate of $2 per thousand dollars of gross receipts (0.002 x Gross) for service or professional businesses.

Because the rate method can result in $0.00 returns or negligible amounts, most jurisdictions have a minimum tax or other method of ensuring a base fee. Another option is to create a base tax plus gross receipts rate. This allows for a minimum fee for businesses that generate gross receipts in excess of the base amount.

The "rate" method of taxing on gross receipts provides an even distribution of the effective tax rate because all businesses subjected to the tax will pay the same rate. This method also provides the simplest method of calculation due to every business using a single multiplier.

Option 2 – Background

Due to the lack of information available on current gross receipts for all County businesses, HdL is not able to accurately predict the impact of changing the structure to a single gross receipts model. HdL was able to use averages for those businesses where gross receipts reporting was available; however, direct comparisons are not available on a County wide basis and certain information may overlap between categories. It is important to note that HdL has used multiple assumptions as outlined in the options below that should not be relied upon for actual budgeting and are meant to provide a baseline of the possible impact.

Option 2 – Data Analysis & Variables

HdL has prepared key data elements for use in estimating the gross receipts tax on businesses where information was otherwise not available.   The following information was used as a basis for the tax tables and models in subsequent options below.

Combined Gross Estimates

Number of Records	Business Tax Total Taxable Gross Receipts
1,400	$230,000,000.00

Option 2 – Single Gross Receipts Rate

Option 2 reflects the potential revenues for converting the whole County to a single rate type gross receipts model. This would eliminate the current structure of mixed classes with fixed fees, whereby each business would pay based on the gross receipts attributed within the County.

Potential Tax Structure

Tax Basis	Tax Rate
Registration Tax	$100.00 + Annual CPI
Gross Receipts	$1 per thousand dollars of Gross (0.001 x Gross)

Option 2 Estimates Table

The table below indicates the potential revenues from implementing a gross receipts tax with two options, $1 / thousand, and $1.50 / thousand. Information for the estimates comes from the data in the section above.

Gross Receipts	Number of Accts	Taxable Gross Receipts	Tax Amount (.001)	Tax Amount (.0015)
General / Retail				
Registration Tax	1,400	Flat Fee	$140,000.00	$140,000.00
Gross Receipts Tax		$230M	$230,000.00	$345,000.00
		TOTALS>	$370,000.00	$495,000.00

Option 2– Highlights and Impact Review

Option 2 shows the most potential for revenue while keeping the tax structure simple. This model creates equity in the tax base by applying the same effective rate for all businesses across the board, rather than using complicated business categories creating potential inequities.

Using the 1 Mil (.001 rate) as our baseline, we can see that revenues are similar to the estimates from option 1 which uses the existing categories in the code. This rate structure may provide similar revenues to the County, but likely spreads the tax burden out by potentially reducing liability for smaller business and shifts it to those higher grossing entities.

Option 3 – Classification Based Rates / Hybrid Measurements

Similar to the County's current method, Model 3 as indicated below would create varying rate multipliers depending on business classifications. The County could for example, choose to implement a rate for the retail/wholesale/Misc. business activities at a base rate of .001. This recognizes higher costs of goods sold and lower profit margins for these types of business as well as their contribution to other County revenues such as sales tax. Conversely, the County could consider implementing a higher rate for professionals and property rental. This model affords the most flexibility for increasing revenues while accommodating certain business categories.

For this model, mining operations are kept under a similar approach to taxing tonnage rather than gross receipts. Each category could be assigned its own unique tax measurement, allowing a hybrid of employees, gross receipts, tonnage, flat fees and other tax rates. This provides the most flexibility for the County to adjust rates based on business activity.

Tax Structure

Tax Rate	Categories	Tax Rate
Registration Tax	General / Retail	$100 Flat
Gross Receipts Tax	General / Retail	0.001 X Gross
Registration Tax	Property Rentals	$100 Flat
Gross Receipts Tax	Property Rentals	0.002 X Gross
Registration Tax	Mining Operations	$100 Flat
Tonnage Removed	Mining Operations	$0.05 per Ton
Registration Tax	Service / Professionals	$100 Flat
Gross Receipts Tax	Service / Professionals	0.003 X Gross

Estimates Table

Using the varying structures above, the table below indicates potential revenues from one possible classification model based on the estimated business data. Because actual distribution of gross receipts is not available for all classifications, HdL has used a series of estimates to categorize businesses and the potential gross receipts for each category.

Gross Receipts	Number of Accts	Taxable Measure	Tax Rate	Tax Amount
General / Retail				
Registration Tax	600	Fixed	$100 /Flat	$60,000.00
Gross Receipts Tax	600	$200M	.001	$200,000.00
Rental Units (Com & Res)				
Registration Tax	100	Fixed	$100 /Flat	$10,000.00
Gross Receipts Tax	100	$2M	.002	$4,000.00
Service / Professionals				
Registration Tax	700	Fixed	$100 /Flat	$70,000.00
Gross Receipts Tax	700	$28M	.003	$84,000.00
Mining Operations				
Registration Tax	4	Fixed	$100 Flat	$400.00
Gross Tons	4	4.5M Tons	.05	$227.000.00
			TOTALS>	$428.400.00

Option s– Highlights and Impact Review

This option has the benefit of spreading varying tax rates across multiple business types. The County has the option of modifying the rates and reassigning business types to different categories. The model above includes basic rate increases for standard categories but can be further expanded or contracted to accommodate a different method of the County's choosing.

Additional Models

The County has various options should it elect to move forward with a hybrid gross receipts based tax. For example, a model could be designed to implement fixed fee structures, while moving certain categories over to a simplified gross receipts tax. In this method Rentals could be taxed by number of units, while all other businesses are lumped in as gross receipts based model, or vice versa.

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The County could also elect to implemental a scale model using expanding ranges, implementing caps, or by additional rates and classifications. Removing the registration tax and including a minimum range could also simplify the process and equalize the tax.

County of San Benito

Rate Comparison Chart

Sample Business	San Benito Current Rates	Hollister	Monterey County	San Juan Bautista	San Benito Option 1:	San Benito Option 2:	San Benito Option 3:	San Benito Option 4
Small Craft Business $25,000								
Restaurant – $100,000 Gross								
Big Retailer – $2,500,000 Gross								
Hotel / Rental Property $2M Gross / 80 Units								
Doctors Office- $250,000 Gross								
Professional Firm- $1,500,000 Gross								
Small Contractor – $50,000 Gross								
Contracting Firm– $500,000 Gross								

Additional Information

Ordinance Review

A review of the ordinance sections related to business tax is still pending. The recommended changes will provide technical recommendations based on the information available and direction provided by the County. Should the County elect to move forward with specific changes, HdL recommends the office of the County Attorney or their designee review each proposed change and craft language that accomplishes the County's final objectives.

Voter & Additional Approvals

Some of the changes may or may not require voter or additional approval. The County should review each change and determine which changes can be made via powers granted to the collector or other County staff members and which changes will require additional processes.

Additional Support

While HdL is not able to provide specific legal advice, HdL will work with the County's designee to assist in crafting the final changes as well as provide advice and additional analysis should the County elect to move forward with modification of its ordinances. Should the County wish to contract out legal services, HdL can provide references for firms that specialize in local government ordinances.

Comparative Jurisdictions

The analysis of surrounding jurisdictions was conducted to provide background of the overall structure and taxes imposed by neighboring cities. This information can be valuable and may be considered by the County when making its final determinations to ensure that changes made to the tax structure remain competitive with other cities.

Additional Cities / Counties

HdL selected cities from surrounding jurisdictions that were similar in size or tax structure. Should the County wish to expand the analysis to additional jurisdictions, HdL can provide further details as an addendum to this report.

Rate Structure Modification

The primary focus of the rate analysis and change review was the current fee structure. Options indicated in this report represent a few of the potential structures available for the County's consideration. Additionally, each proposed structure has the flexibility to be modified with rates that may be more in line with the County's ultimate goals. HdL will work with the County to craft any additional classifications or structures that the County feels may be worth considering.