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Multistate Tax
EXTERNAL ALERT

Local Business Tax Update

January 29, 2013

Overview

This External Alert summarizes various local business tax developments, including:

- The upcoming transition in San Francisco from the Payroll Expense Tax to a gross receipts tax
- An update regarding the ongoing reform of the Los Angeles Business Tax
- Notice of a pending ballot measure that would increase the sales tax rate in Los Angeles
- Voluntary disclosure considerations in the City of Portland now that the city's tax amnesty period has ended
- An update on the City of Portland and Multnomah County's position regarding whether taxpayers may elect to apply the Multistate Tax Compact apportionment provisions
- A court ruling precluding the levy of City of Birmingham business license tax on legal services performed outside Birmingham

San Francisco, California

San Francisco Approves Proposition E, Gross Receipts Tax – The voters of San Francisco recently approved Proposition E, a gross receipts tax that will be phased in over five years beginning in 2014.[1] This gross receipts tax will gradually replace the existing 1.5% payroll expense tax, which will be phased out by 2018 other than as applied to administrative offices. During the five-year phase-in period, taxpayers will pay both the payroll tax and gross receipts tax. As with the current payroll tax, the new gross receipts tax is imposed at the entity level on persons "engaging in business" within San Francisco. Each separate business activity is assigned to one of seven industry classifications,[2] which determine the applicable tax rates, apportionment methodology and, in certain cases, special industry-related rules.[3]

Receipts received from a related entity that is part of the same combined unitary group for California income tax purposes are excluded. Gross receipts are then apportioned based on the location of the property, payroll, or the benefit received - or some combination of these factors.[4] There are a number of exemptions and exclusions from the gross receipts tax such as for small businesses with San Francisco gross receipts under $1 million.[5]

[1] Proposition E, San Francisco Gross Receipts Tax Ordinance Article 12-A-1 ("Gross Receipts Tax Ordinance"), approved by voters on November 6, 2012.
[2] Gross Receipts Tax Ordinance §§ 953.1 to 953-7 and 952.4. The business activities are based on definitions and descriptions from the North American Industry Classification System ("NAICS"). The NAICS code is used by the federal government to classify business establishments.
[3] Additionally, there are special rules for businesses with activities that may be described in more than one industry classification. Gross Receipts Tax Ordinance § 953.9.
[4] Gross Receipts Tax Ordinance § 956.
[5] For more information on San Francisco's Gross Receipts Tax, see our External Tax Alert dated January 22, 2013, accessible at:
http://www.deloitte.com/assets/Dcom-UnitedStates/Local%20Assets/Documents/Tax/us_tax_multistate_CA_San%20Francisco_Alert_1-22-2013.pdf.

Los Angeles, California

Recently Published Article: "Open for Business" Updated: Los Angeles Pioneers Local Tax Reforms in a Challenging Economic Environment – Read our updated discussion regarding Los Angeles business tax reform efforts. Our article is accessible at:
http://www.deloitte.com/view/en_US/us/Services/tax/Multistate-Tax/b3a94c603422b310VgnVCM3000003456f70aRCRD.htm.

Extension of Los Angeles New Business Tax Holiday – An extension of the existing "new business" tax holiday was enacted on November 20, 2012. Prior to the extension, new businesses commencing activities in the Los Angeles between January 1, 2010, and December 31, 2012, were exempt from the Los Angeles business tax for the first three filing years. The amendment to the ordinance extends the three-year tax exemption to new businesses commencing activities in Los Angeles after December 31, 2012, and on or before December 31, 2015.[6]

Reevaluation of the Radio and Television Broadcasting Classification – On November 20, 2012, the Los Angeles City Council's Jobs Committee approved a motion instructing the Office of Economic Analysis, with the assistance of the Office of Finance, to review the potential impact on the radio and television broadcasting industry of certain revisions to the Los Angeles tax structure. Taxpayers in this industry are currently taxed under Los Angeles Municipal Code §21.45 at a rate of $1.27 per $1,000 of gross receipts. The exact apportionment methodology for such taxpayers is unclear, although Section 21.45 suggests that a fair apportionment should be used, based on some form of cost allocation or apportionment, similar to that used for businesses classified as Professions & Occupations under City Clerk's Ruling 15. The Jobs Committee's motion notes that the broadcasting industry generates revenue through both local and national advertising, and that some activities occurring within and outside Los Angeles may not be fairly apportioned for Los Angeles Business Tax purposes under the current provisions. Among the suggested revisions to Section 21.45 are a maximum tax, a minimum tax, and various alternative apportionment/allocation methodologies. In addition, the motion instructs the city to continue to meet with the Motion Picture Association of America to assist in evaluating the impact of the potential alternatives being considered for Radio and Television Broadcasters.

Sales Tax Rate Increase on 2013 Ballot – On November 20, 2012, after a second vote, the Los Angeles City Council approved a measure to be placed on the March 5, 2013 ballot that would increase the sales tax rate in Los Angeles by .5%. The ballot measure was first approved on November 13, 2012, by the City Council, but a second vote was required because the initial vote was not unanimous. The sales tax increase will be used to fund various services and will replace other proposed revenue raisers, such as the local transfer tax on home sales. The current sales tax rate in Los Angeles is 9%[7] and if this ballot measure is adopted, the sales tax in Los Angeles would increase to 9.5%.

City of Portland and Multnomah County, Oregon

Tax Amnesty Period Has Closed – The Portland Revenue Bureau (the "Bureau") recently concluded a "one time only" business tax amnesty program for the City of Portland Business License Tax and the Multnomah County Business Income Tax. The amnesty program, which ran from May 15, 2012, to July 16, 2012, granted a full penalty waiver and an annual interest rate reduction to 5% (from 10%) for business taxpayers without a tax account and registered business taxpayers that had not filed returns in recent years.

In the post-amnesty period, the Bureau is taking the position that any taxpayer that could have taken advantage of the tax amnesty, but did not do so, will not be allowed to take advantage of the "Voluntary Compliance Policy."[8] Businesses that are required to register and file with the

[6] The ordinance also contains language that would allow Los Angeles to suspend the exemption in the event of a drastic decline in General Fund revenue due to an economic downturn, a natural disaster, a legal judgment, or other situations likely to put the city in severe financial distress .

[7] The rate increased from 8.75% to 9% on January 1, 2013 as a result of the passage of California Proposition 30.

[8] In general, qualified participants in the City's Voluntary Compliance program may choose one of two options:

1. Report and pay all taxes due, plus interest for all years of unreported business activity. Upon receipt of returns, taxes and interest, all penalties will be waived upon written request; or

City/County but reasonably believed that they were exempt from the Portland City/Multnomah County business taxes may still be eligible for the Voluntary Compliance program.[9] However, if the City/County can prove that notification was sent to a business for a return and/or payment due, the business may not take advantage of the Voluntary Compliance Policy and the business will be liable for all outstanding filings and payments due.

MTC Election Appears to be Unavailable for City of Portland and Multnomah County Income Taxes – The recent decision from the California Court of Appeal on October 2, 2012, *Gillette v. California Franchise Tax Board,*[10] provided that California - a full member of the Multistate Tax Compact ("MTC") during the tax years that were before the court – could not preclude a taxpayer from electing the apportionment provisions of the Compact, notably application of an equally-weighted, three-factor apportionment formula, despite the fact that California had enacted statutory language requiring application of a different apportionment formula.[11] The City of Portland, which administers both the City and County income taxes, has stated informally that it will not recognize an MTC election because neither the City nor the County is a member of the MTC. While the City and County tax codes each generally conform to the Oregon corporate tax statutes, this conformity does not extend to apportionment, where the City and County have adopted different apportionment rules.

Birmingham, Alabama

Ruling Limits City Business License Taxes on Legal Services – On December 26, 2012, a County Circuit Court judge ruled in favor of a law firm taxpayer, effectively precluding the City of Birmingham from taxing gross receipts earned by the taxpayer from legal services performed outside the city limits. The taxpayer had argued that the license tax ordinance limits the tax to only legal services performed within the city and to suggest otherwise would be unconstitutional because the tax would not then be fairly apportioned. While the instant case pertains to lawyers, similar litigation is pending involving service professionals from a variety of other industries, including engineers, accountants, physicians, and consultants.

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2. Report and pay all taxes, interest and penalties for the current year plus three prior years only (penalties will be limited to 25% of the taxes and/or fees due each year). The "current year" is the most recent return that would have been required to be filed as determined by the Bureau.

City of Portland Voluntary Compliance Policy (July 8, 2009).

[9] *See*, **http://www.portlandonline.com/omf/index.cfm?c=59798.**

[10] *The Gillette Company, et al. v. California Franchise Tax Board*, 209 Cal. App. 4th 938 (Oct. 2, 2012); petition for review granted, 2013 Cal. LEXIS 282 (Jan. 16, 2013).

[11] For further details regarding the *Gillette* decision, please see our External Tax Alerts dated October 4, 2012, accessible at: **http://www.deloitte.com/assets/Dcom-UnitedStates/Local%20Assets/Documents/Tax/us_tax_multistate_CA_Alert_10-04-2012.pdf**; July 27, 2012, accessible at: **http://www.deloitte.com/assets/Dcom-UnitedStates/Local%20Assets/Documents/us_tax_multistate_CA_MTC_Alert_7-26-2012.pdf**; and January 22, 2013, accessible at: **http://www.deloitte.com/assets/Dcom-UnitedStates/Local%20Assets/Documents/Tax/us_tax_multistate_CA_Alert_1-22-2013.pdf.**

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