COUNCIL AGENDA: 10-23-12
ITEM: 3.7

CITY OF SAN JOSE
CAPITAL OF SILICON VALLEY

Memorandum

TO: HONORABLE MAYOR AND CITY COUNCIL

FROM: Julia H. Cooper
Jennifer A. Maguire

SUBJECT: SEE BELOW

DATE: October 9, 2012

Approved

Date 10/9/12

SUBJECT: BUSINESS TAX AND BUSINESS IMPROVEMENT DISTRICTS ASSESSMENT AMNESTY PROGRAMS

RECOMMENDATION

(a) Approve an ordinance authorizing the Director of Finance to administer a Business Tax Amnesty Program which forgives taxpayers who pay certain past due business taxes from liability for the remaining past due business taxes, interest, and penalties; and,

(b) Approve an ordinance authorizing a Business Improvement District Assessment Amnesty Program for the Downtown and Japantown Business Improvement Districts to run concurrently with the Business Tax Amnesty Program.

(c) Adopt the following 2012-2013 Appropriation Ordinance and Funding Sources Resolution Amendments in the General Fund:

1. Increase the revenue estimate for Business Tax by $300,000; and
2. Increase the Finance Department Non-Personal/Equipment appropriation by $300,000.

OUTCOME

To encourage San José business owners and self-employed individuals with income reported on Federal Form Schedule C, Profit or Loss from Business, to 1) pay past due Business Tax and Business Improvement District ("BID") assessments; 2) increase current and future Business Tax and BID assessment revenues and to capture the appropriate number of businesses and self-employed individuals conducting business in San José; and 3) educate businesses regarding the availability of the Business Tax Hardship Exemption Fee that allows businesses that generate less than approximately $22,000 per year to pay a lower fee.

BACKGROUND

Business Tax Amnesty Program in 2006

In August 2006, the Finance Department administered a 60-day Business Tax Amnesty Program ("Amnesty Program"), including a BID Assessment Amnesty Program, generating approximately $1,300,000 in additional revenue from approximately 5,300 taxpayers. Outreach included the mailing of approximately 26,000 direct mail lead and delinquent account letters as well as advertising the Amnesty Program. The advertising campaign included the following: the three BID Associations[1], Mercury News, Tri-County Apartment Association, San José Silicon Valley Chamber of Commerce, Hispanic Chamber of Commerce, Vietnamese Chamber of Commerce and KLIV Radio Station.

The accomplishments of the 2006 Business Tax and BID Amnesty Programs were more notable than the previous two amnesty programs (1987 and 1998) due to the direct mail approach utilized. The strategic plan relied heavily on the City's telephone and website technology to handle customer inquiries. The telephone system received approximately 11,700 calls of which 8,700 were answered by staff and recorded messages. A total of 8,300 customers visited the Business Tax and BID Amnesty Program website and downloaded 8,100 forms.

Business Tax Data Leads

The City and the California Franchise Tax Board ("FTB") have participated in the exchange of data through a reciprocal agreement. The City data helps the FTB identify businesses and self-employed individuals who may not have filed required business entity and/or individual income tax returns. In turn, the FTB data helps the City identify businesses and self-employed individuals who may not have complied with the City's Business Tax requirements. As a result of the City receiving this shared data, the Finance Department anticipates sending out approximately 40,000 direct mail notices. The Finance Department believes that the prolonged economic downturn and lack of awareness of tax requirements by individuals with income reported on the Schedule C have resulted in an increased number of non-compliant businesses and individuals. A Business Tax and BID Amnesty Program will generate one-time and ongoing revenue to the General Fund. The Amnesty Program will also educate more businesses and individuals about the City requirements and bring them into compliance prior to implementing a more automated registration and payment system in 2013.

[1] Willow Glen BID ceased to exist in December 2009 following Council adoption of Willow Glen Community Benefit and Improvement District in December 2008.

ANALYSIS

Business Tax and BID Amnesty Terms

The proposed Business Tax and BID Amnesty Programs cover the period from January 1, 2009 through December 31, 2012, capping the maximum amount of unpaid Business Tax and assessment liabilities at three prior tax years, plus the current tax year. The proposed period during which a business owner may file a request for amnesty is recommended to commence on December 1, 2012 and to end on March 29, 2013.

The BID Amnesty Program will include assessments owed to the City's two Business Improvement Districts (Japantown and Downtown). All proceeds derived from the BID Amnesty Program will benefit the respective Business Improvement Districts.

During the amnesty period, the Director of Finance will be authorized to waive all interest and penalties for the affected tax periods (January 1, 2009 through December 31, 2012) for never registered and delinquent taxpayers (except for taxpayers against whom a civil or criminal action for Business Tax liability was commenced prior to December 1, 2012). The same parameters are applicable for the unpaid BID assessments.

Business Tax Owed

The City's general Business Tax is based on the number of employees. For most businesses the annual tax is $150 for up to eight employees. The additional tax increments are $18 per person over eight employees with a maximum tax of $25,000. Currently 50% of San José businesses that pay the Business Tax are in the category of eight or fewer employees. Staff believes a majority of the businesses ultimately participating in the Amnesty Program will fall into the eight or fewer employee category or qualify for the Business Tax Hardship Exemption Fee. The Business Tax Hardship Exemption Fee ("Exemption Fee") is available to sole proprietorships and corporations that are owned by one person, husband/wife or domestic partner ownership structures that have a) no employees and b) annual gross receipts at or below less than twice the poverty level which changes year to year[2]. The term "poverty level" means the income amount established by the U.S. Department of Health and Human Services as the poverty guideline for a single person multiplied by two (2) for the calendar year in which the business tax is due. For businesses that qualify for the Exemption Fee, the current annual rate is $38.

The Business Tax statute of limitations for the collection of unpaid taxes is three prior years plus the current year. As displayed in the chart below, without the Amnesty Program, a typical business with eight or fewer employees that failed to pay the business tax over the previous three years would owe a total of $864. However, the Amnesty Program reduces the amount a business would owe to $600; the penalties and interest of $264 would be waived.

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[2] Historic poverty levels for the income tax reporting year: 2012 - $22,340; 2011 - $21,780; 2010 - $21,660; 2009 - $21,660.

Typical Business Tax Owed

Categories	Tax	Penalties	Interest	Without Amnesty	With Amnesty
3 Prior Years + Current Year	$600.00	$75.00	$189.00	$864.00	$600.00
2 Prior Years + Current Year	450.00	75.00	106.31	631.31	450.00
1 Prior Year + Current Year	300.00	75.00	38.81	413.81	300.00
Current Year	150.00	75.00	27.00	252.00	150.00

In addition, if the business is a sole proprietorship and qualifies for the Exemption Fee, instead of paying the $864, the business would pay $148 for the current and prior three tax years.

Business Tax Hardship Exemption Fee Owed

Categories	Fee*	Penalties	Interest	Without Amnesty	With Amnesty
3 Prior Years + Current Year	$148.00			$148.00	$148.00
2 Prior Years + Current Year	110.00			110.00	110.00
1 Prior Year + Current Year	75.00			75.00	75.00
Current Year	38.00			38.00	38.00

* FY 12-13: $38, FY 11-12: $37, FY 10-11: $35, FY 09-10:$38

The Director of Finance will encourage payment of outstanding tax liabilities and assessments in full. However, an installment payment plan will be afforded to businesses owing more than one year of outstanding Business Tax or assessment greater than $200. Payment plans will be available on an as necessary basis for businesses owing more than $200 with the installment payment plan requiring that one-third of the outstanding tax or assessment be paid immediately. If a business owner does not comply with the terms of the payment plan, the unpaid tax or assessment including penalties and interest retroactive to the date the tax or assessment was originally owed will become due and payable immediately.

Outreach

The Business Tax Amnesty Program will require outreach to the business community through a variety of mediums, including advertisements in print media, public service announcements through radio stations, and direct-mailing of approximately 40,000 notices informing never-registered and delinquent taxpayers. Staff will also provide additional outreach to organizations and associations, such as the Santa Clara County Association of Realtors, California Apartment Association (Tri-County Division), San José Silicon Valley Chamber of Commerce, Hispanic Chamber of Commerce Silicon Valley, Greater San José Hispanic Chamber of Commerce, Vietnamese American Chamber of Commerce, Black Chamber of Silicon Valley, Silicon Valley Leadership Group, Silicon Valley SCORE, Silicon Valley Small Business Development Centers of Northern California, neighborhood business associations, local CPA firms and title companies

requesting assistance to communicate the amnesty programs to their members and clients. Staff is exploring the feasibility to conduct several community meetings to educate businesses regarding the Amnesty Program as well as work with the businesses to determine if they qualify for the Business Tax Hardship Exemption Fee in lieu of paying the Business Tax.

Amnesty Program Administrative Expenses

In order to facilitate this comprehensive program in an efficient manner, the Finance Department will hire temporary staff to process Business Tax Registration Forms and payments and will pay for advertising and mailing to support this program at an estimated cost of $300,000. Staff anticipates that the additional revenue generated by the Amnesty Program will cover these additional costs.

EVALUATION AND FOLLOW-UP

It is anticipated that budget adjustments will be brought forward later in 2012-2013 to recognize the additional revenue generated by the Amnesty Programs over the $300,000 that is recommended in this memorandum to cover the program costs. The year-end adjustments will be based on the actual results after the close of the amnesty period. It is likely that these funds will be recommended for use as part of the 2013-2014 budget process. The ongoing impacts associated with these programs will also be incorporated into the 2013-2014 budget development process. In addition, the Finance Department will proactively pursue compliance from businesses and individuals who failed to take advantage of the Amnesty Program.

POLICY ALTERNATIVES

Alternative #1: Do not offer the Business Amnesty Program
Pros: Generates additional General Fund revenue from those businesses that were not in compliance by imposing and collecting penalties and interest.
Cons: Potentially increases the number of taxpayers failing or evading payment of the Business Tax and BID Fees.
Reason for not recommending: An Amnesty Program encourages the payment of Business Tax without the additional cost of penalties and interest as well as avoiding potential legal action. The Amnesty Program, while encouraging businesses to come forth and pay a reduced amount, also becomes a source of ongoing revenue generation through future billing.

PUBLIC OUTREACH/INTEREST

☐ **Criterion 1**: Requires Council action on the use of public funds equal to $1 million or greater. **(Required: Website Posting)**

☒ **Criterion 2:** Adoption of a new or revised policy that may have implications for public health, safety, quality of life, or financial/economic vitality of the City. **(Required: E-mail and Website Posting)**

☐ **Criterion 3:** Consideration of proposed changes to service delivery, programs, staffing that may have impacts to community services and have been identified by staff, Council or a Community group that requires special outreach. **(Required: E-mail, Website Posting, Community Meetings, Notice in appropriate newspapers)**

This memorandum will be posted on the City's website for the October 23, 2012 Council agenda. In addition, the business community will be informed about the upcoming Business Tax and BID Amnesty Programs through news releases, print media advertisements, and public service announcements.

COORDINATION

This memorandum was coordinated with the City Manager's Office, Office of Economic Development, City Attorney's Office and representatives of the Business Improvement Districts.

COST SUMMARY/IMPLICATIONS

An increase to the Finance Department's Non-Personal/Equipment appropriation in the amount of $300,000, offset by additional Business Tax revenue, is requested to cover the cost of administering the Amnesty Program, including expenses associated with advertising, mailing of notices, supplies and temporary staffing. Staff expects the Amnesty Program to generate revenue in excess of that amount based on the results of the last Business Tax Amnesty Program in 2006 that generated revenue of $1,300,000. As discussed above, it is anticipated that budget adjustments will be brought forward during 2012-2013 to recognize the additional revenue generated by the Amnesty Program over the $300,000 that is recommended in this memorandum to cover the program costs. The year-end adjustments will be based on the actual results after the close of the amnesty period. It is likely that these funds will be recommended for use as part of the 2013-2014 budget process.

Further, the City will identify new business owners who are expected to pay the annual Business Tax and assessment after the conclusion of the amnesty contributing to ongoing additional Business Tax and assessment revenue. The ongoing revenues will also be considered in the development of the 2013-2014 Budget.

BUDGET REFERENCE

Fund #	Appn. #	Appn. Name	RC#	Total Appn.	2012-2013 Proposed Budget	Last Budget Action (Date, Ord No.)
001	0492	Non-Personal/ Equipment	000150	$968,232	VIII-108	06/19/2012; 29102

CEQA

Not a Project; File No. PP10-068, Municipal Code or Policy.

/s/
JULIA H. COOPER
Acting Director, Finance

JENNIFER A. MAGUIRE
Budget Director

For questions, please contact Wendy Sollazzi, Division Manager, at (408) 535-7005.

I hereby certify that there will be available for appropriation in the General Fund in the Fiscal Year 2012-2013, monies in excess of those heretofore appropriated there from, said excess being at least $300,000.

JENNIFER A. MAGUIRE
Budget Director