



DATE: May 20, 2024

TO: Mayor and Members of the City Council

VIA: Stefan Chatwin, City Manager

FROM: Marlene Subhashini, Assistant City Manager  
Sofia Mangalam, Community Development Director  
Waqas Hassan, Assistant Finance Director  
Priscilla Schaus, Communications Director/City Clerk

DEPARTMENT: City Manager, Community Development, Finance

SUBJECT: REPORT ON BUSINESS LICENSE TAX UPDATE

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## RECOMMENDATION

It is recommended that the City Council, by Minute Order:

1. Receive and accept this report on a potential update to the City's Business License Tax (BLT); and
2. Review and discuss the proposed models related to the BLT update and provide policy direction on:
  - a. The preferred Business License Tax model;
  - b. Whether to consider phasing the maximum tax cap increase over a three (3) year period for the preferred model;
  - c. Whether to keep or eliminate the current Foster City Municipal Code (FCMC) exemption provision related to multiple corporate entities; and
  - d. Whether to proceed with a potential ballot measure to increase the Business License Tax for the November 2024 General Election.

## EXECUTIVE SUMMARY

The City's Five-Year Financial Plan indicates an ongoing structural deficit over the next five years, meaning, annual ongoing expenditures will exceed ongoing revenues. In other

words, there are insufficient revenues to pay for the cost of operations and services provided to the community. In recognition of the fiscal challenges facing the City and the City's commitment to provide uninterrupted services to the community, the City Council directed staff to consider an update to the City's BLT as a potential revenue enhancement option in 2022. Although progress was made on the BLT update in 2022, those efforts were put on hold. In 2023, one of the goals that the City Council adopted at its Vision & Policy Summit was to *"Identify new revenue sources and strengthen existing resources to ensure Foster City finances are more resilient to economic fluctuations and support city services."* Under this goal, two (2) measures/initiatives were identified including:

- Initiate and engage in ongoing dialogue with City businesses to build strong relationships and assess their needs and understand their perspectives on a BLT ballot measure.
- Research BLT methodologies and consider feasibility of various methodologies (e.g., gross receipts, square footage, employee count) with presentation to Council in January 2024.

The City Council reaffirmed this initiative as a key priority at its 2024 Vision & Policy Summit. A project team comprising of staff from the City Manager's Office, Community Development Department, Finance, Communications/City Clerk and Consultants were assembled to begin work on this initiative. Staff presented reports to Council on October 16, 2023 ([link](#)), December 18, 2023 ([link](#)) and February 05, 2024 ([link](#)), where staff outlined the strategy for amending the BLT Ordinance, discussed steps leading to the potential ballot measure in the November 2024 General Election, provided preliminary analysis of the City's current BLT structure, shared pros and cons of the various BLT structures and provided a comparison to other cities' BLT structure.

Following the Council meetings, the project team began to explore potential BLT models that could generate additional revenue while meeting the City's goals. To understand the impact of the potential BLT models on businesses and assess the support for a BLT update, the project team began a robust engagement effort with the community, the Chamber, the businesses and key stakeholders utilizing surveys, one-on-one and group meetings, social media and direct outreach efforts to share information on the City services, City budget, the proposed BLT models and gather feedback. During this time, a public opinion survey and a fiscal sustainability survey was administered to understand the community's needs and perspectives on the potential BLT ballot measure for the November 2024 General Election.

In this staff report, staff will present the potential BLT models and share feedback received from the various outreach/engagement efforts from the community and businesses for Council consideration. Staff would like to seek Council direction on the preferred model and other policy direction before proceeding with continued outreach and engagement efforts and a potential ballot measure for the November 2024 General Election. It is important to note that with all the potential models that will be presented, approximately 78% of Foster City businesses, which includes 1,287 small businesses, would see no change in their annual BLT. Of the 78%, approximately 8% will see a positive impact in

that they'll be paying less than what they currently pay. This was in response to the initial feedback that staff received to ensure that small businesses are not impacted.

**BACKGROUND**

The City of Foster City's BLT Ordinance was enacted in 1972, shortly after the City's incorporation. The City of Foster City requires all businesses operating within the City of Foster City to obtain a business license and pay associated taxes in accordance with Title 5 – Business Licenses and Regulation of the Foster City Municipal Code (FCMC). It wasn't until four decades later (in 2013) that the BLT Ordinance was amended and a ballot measure (Measure U) to increase the BLT was approved by the Foster City voters. Chapters 5.04 to 5.40 of FCMC Title 5 outline the provisions of the City's current BLT. All businesses, trades, professions, and occupations specified in the code are subject to a BLT when there is sufficient evidence that business is being conducted in the City. Nonprofit Organizations as defined under Section 501(c)(3) of the United States Internal Revenue Code and Farmers Markets approved by the city are exempt from BLT.

The model which the City follows is based on a gross receipts model with a single tax rate of \$0.75 per \$1000 of gross receipts, utilizes a minimum tax of \$100 (\$200 for general contractors) and a maximum tax (\$28,597 based on FY 2023 licensing period). *Under the current structure, a business has to gross more than approximately \$33 million to hit the gross receipts cap and pay the maximum tax.* Generally, single-rate gross receipt tax structures allow the City to capture all gross receipts generated locally and tie the City to the economic growth of the business community. This model has growth potential, yet is also equitable to businesses during economic downturns, which also means there may be significant revenue volatility during periods of expansion and contraction (gross receipts are self-reported by each business). As noted earlier, in 2022, the City began exploring an update to its BLT by increasing the gross receipts cap while maintaining the same tax rate.

Table 1 below shows a comparison of the original 1972 BLT Ordinance, the 2013 BLT Ordinance Amendment and the 2022 BLT Proposed Ordinance Amendment.

	1972 Original Business License Tax Ordinance	2013 Business License Tax Ordinance Amendment	2022 Proposed Business License Tax Ordinance Amendment
<b>Scope</b>	All forms of entities conducting business in Foster City (non-profits excluded)	All forms of entities conducting business in Foster City. Farmers Markets excluded in addition to non-profits	<b>NO CHANGE</b>
<b>Tax Rate</b>	\$0.75 per \$1,000 of gross receipts (or 0.075%)	<b>NO CHANGE</b>	<b>NO CHANGE</b>
<b>Gross Receipts Cap</b>	\$5 million	\$30 million adjusted over three (3) years:	<b>Scenario #1 \$300 million Scenario #2 \$400 million</b>

		2014 - \$10 million 2015 - \$20 million / 2016 - \$30 million /	<b>Scenario #3 \$500 million</b> <b>Scenario #4 \$1 billion</b>
<b>Minimum Tax</b>	\$25 / \$50 for General Contractors	Phased in over 3 years: \$50 in 2014; \$75 in 2015; \$100 in 2016;  All Rates – Double for General Contractors	<b>NO CHANGE</b>
<b>Maximum Tax</b>	\$3,750 based on a \$5 million cap	\$22,500 (based on \$30 million cap in 2013) \$26,985 (based on 2022 \$35.98M cap)	<b>Scenario #1 \$225,000</b> <b>Scenario #2 \$300,000</b> <b>Scenario #3 \$375,000</b> <b>Scenario #4 \$750,000</b>
<b>Future Increases</b>	None	Gross Receipts Cap will increase based on SF Bay Area CPI-U Rate October-to-October	<b>NO CHANGE</b>
<b>Cap on Corporate Entities</b>	Each corporate entity is considered a separate business and requires a separate business license	The number of corporate entities conducting business at same location is limited to (3) entities with the highest gross receipts	<b>NO CHANGE</b>
<b>Effective Date</b>	<b>1972</b>	<b>January 1, 2014</b>	<b>January 1, 2023</b> (if passed)

As noted earlier, the BLT update efforts in 2022 were paused to allow staff to engage with the business stakeholders, research various BLT methodologies and their feasibility. Staff resumed this effort in 2023. At the October 16, 2023 Council Meeting, staff provided a preliminary report on the approach to amending the BLT Ordinance, and steps leading up to adding a ballot measure during the November 2024 General Election. The Council received the report and provided direction to staff to continue the work on placing the potential BLT update on the ballot for the November 2024 General Election. At the December 18, 2023 Council Meeting, staff provided an update on progress on amending the BLT including an update on the consultant selection for BLT tax study (HdL Companies), public outreach/community engagement services (Grassroots Lab) and polling/survey services (FM3 Research). Specifically, the City commissioned HdL to review the administrative efficiency of the current structures, to review options for improving the BLT structure, if any, and to investigate the possibilities for additional revenue generation.

At the February 5, 2024 Council Meeting, the project team presented an informational report on the preliminary analysis of the City’s current BLT structure, shared pros and cons of the various BLT structures, provided a comparison to other cities’ BLT structure and possibilities to modernize the City’s current BLT. A memo summarizing preliminary findings was provided and attached to the February 5, 2024 staff report.

## ANALYSIS

### **I. General Overview of Business License Tax**

Business License Tax, also referred to as “BLT” has become a common and important revenue source for many cities. It is an annual tax charged to anyone doing business in a city. The measure of how much taxable activity is occurring within the City (or subject to the City’s taxation powers), is referred to as “measure of the tax.” In most cases, BLT uses proxies for the measure of taxable activity. Those proxies fall into the three significant alternatives for measuring taxable activity: inputs (employee count, square footage based), flat taxes, payroll taxes and outputs or gross receipts or a combination of these. Approaches used by cities vary and can depend on a number of variables.

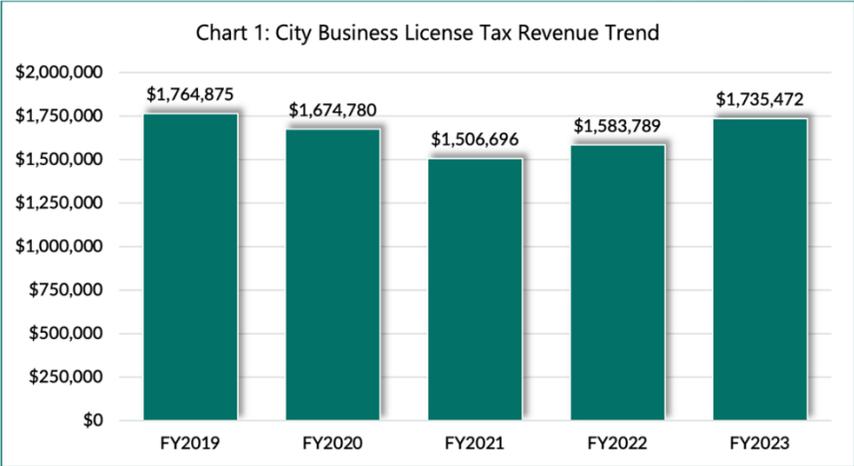
Table 2 below summarizes the key points of comparison (pros and cons) for the various BLT Methodologies/Types of Measurements.

Measure Type	Measure	Pros	Cons
Input	Per Employee	<ul style="list-style-type: none"> <li>▪ Maybe less volatile than gross receipts.</li> <li>▪ Easy to calculate and administer.</li> <li>▪ Larger businesses with more employees pay more-aligning tax contributions with their use of city resources and services.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Higher burden on businesses with more labor inputs (like restaurants) that have already seen their costs of goods sold increase.</li> <li>▪ Doesn't capture per-employee productivity gains from technology.</li> <li>▪ A per-employee tax measure tends to place a heavier burden on smaller businesses than larger businesses.</li> <li>▪ Rise in remote or hybrid work could increase volatility and reduce the usefulness of this measure of tax.</li> </ul>
Input	Square Footage	<ul style="list-style-type: none"> <li>▪ Fixed amount for calculation.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Can be challenging to calculate as certain spaces need to be discounted, tenant improvements take place changing square footage data, etc.</li> <li>▪ Would require City to maintain a database of square footage for each business and keep it up to date.</li> <li>▪ Tends to miss the business activity occurring at other than floor level.</li> </ul>

			<ul style="list-style-type: none"> <li>▪ Is limited to only businesses with a physical location in the city, reducing the taxable business activity/tax base.</li> <li>▪ Rise in remote or hybrid work could increase volatility and reduce the usefulness of this measure of tax.</li> <li>▪ Can be perceived as double taxation as property taxes are assessed on property values based on square footage.</li> <li>▪ It can disproportionately affect businesses that require large physical footprint due to the nature of their business even though the business itself may generate limited revenue.</li> </ul>
Input	Unit	<ul style="list-style-type: none"> <li>▪ The units of input may already be tracked.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Does require pro-ration and may only have a weak relation to the amount of business activity.</li> </ul>
Flat	Flat Fee/Flat Tax	<ul style="list-style-type: none"> <li>▪ Easy to calculate.</li> <li>▪ Predictable and consistent.</li> </ul>	<ul style="list-style-type: none"> <li>▪ No clear relationship to the amount of taxable business activity.</li> <li>▪ Not proportional to the amount of business conducted</li> </ul>
Output	Gross Receipts	<ul style="list-style-type: none"> <li>▪ Closer relationship to the amount of business activity since it captures the output of the taxable business activity.</li> <li>▪ Proportional to the amount of business conducted.</li> <li>▪ Has potential for capturing revenue from economic growth</li> </ul>	<ul style="list-style-type: none"> <li>▪ Increase in the volatility of revenues since they are linked to the outputs of the business activities.</li> <li>▪ In some cases, may be harder to calculate.</li> <li>▪ Under State law, it cannot be based on net income.</li> <li>▪ Exposes City revenues to fluctuations in gross receipts based on the economy.</li> <li>▪ May concentrate revenue in the highest-grossing businesses.</li> </ul>

## II. Current Business License Tax Structure (Single Rate Gross Receipts Tax)

The City has approximately 1,651 businesses contributing to the BLT. Since FY 2019, BLT revenue has averaged approximately \$1,653,122. As seen in the chart below, the City's BLT revenue has remained flat with a dip during the pandemic. Although revenue has since recovered, it has remained steady.



Source: HdL

The City’s current BLT structure includes a gross receipts component consisting of a single (gross receipts) tax rate of \$0.75 or 75 cents per \$1,000 with a minimum tax of \$100 (\$200 for contractors) and a maximum tax based on the cap (\$28,597 based on FY 2023 licensing period). The gross receipts cap is adjusted annually for inflation based on the local Consumer Price Index (CPI).

Table 3: City Current Tax Structure

Category	Minimum Tax	Gross Receipt Rate	Maximum Tax	Business Count	Total Reported <sup>4</sup> Gross Receipts	Tax Collected
General Contractor	\$200	\$0.75 per thousand	\$28,597	449	\$204,000,000	\$203,000
All Other Businesses	\$100			1,202	\$59,895,000,000	\$1,448,000
Totals				1,651	\$60,099,000,000	\$1,651,000

The single rate gross receipt tax of \$0.75 has remained the same since the City’s BLT Ordinance was first adopted in 1972. The single tax rate applies to all businesses regardless of the amount of taxable gross receipts they report. Generally, single rate gross receipt tax structures allow the City to capture all gross generated locally and ties BLT revenue to the economic growth of the business community. However, two factors reduce the amount of tax revenue generated from the reported gross receipts. The first factor is the cap. Businesses paying the maximum tax amount often report gross receipts that are significantly higher than the amount of the cap (in some cases, hundred times more than the amount of the cap). The second factor is the tax limit on the number of multiple corporate entities. The City’s current Ordinance limits the tax on multiple corporate entities conducting business at the same location to three (3) entities with the highest gross receipts (FCMC Section 5.24.020). This exemption allowed otherwise taxable entities to claim millions of dollars in BLT exemptions.

**III. Foster City’s Business License Tax Structure Comparison to Other Cities**

a. Jurisdictions Comparison

Foster City is heavily dependent on the business service industry, which includes businesses such as research & development, warehousing, and technology. Professional, Business, and Personal Service make up approximately 50% of the tax base in Foster City. Service businesses, unlike retail, are limited in the way they contribute to the tax base since they tend not to contribute to sales tax.

The table below illustrates, in descending order based on business license tax revenue, key features of each jurisdiction, namely population, estimated number businesses, and business license tax revenue. The revenue trend diagrams indicate the lowest revenue (red) and highest (green) between FY2018 and FY2022.

Jurisdiction Name	Population	Median Household Income	Est. Annual Businesses	State Report Revenue (FY2022)	Tax Schedules (General)	Latest Code Updated	Revenue Trend FY2018 - FY2022
Richmond <sup>5</sup>	116,448	\$79,478	5,190	\$8,491,418	Gross Receipts with Measure	2022	
San Mateo	105,661	\$133,612	7,070	\$6,639,151	Gross Receipts / Flat Rate	1984	
Daly City	104,901	\$105,374	3,780	\$5,710,745	Gross Receipts	2004	
Hayward	162,954	\$98,837	8,717	\$3,170,501	Gross Receipts / Hybrid	1978	
South San Francisco	66,105	\$112,818	6,490	\$2,741,082	Employee Based	2008	
San Bruno	43,908	\$117,747	4,171	\$2,277,785	Flat Rate with Gross Receipt Measure	1999	
Union City <sup>6</sup>	70,143	\$127,828	3,650	\$1,787,652	Multiple Tax Types	1990	
Sausalito	7,269	\$140,417	2,737	\$1,649,760	Gross Receipts	2018	
Foster City	33,805	\$173,721	1,651	\$1,583,789	Gross Receipts / Capped	2013	
San Carlos	30,722	\$204,570	3,420	\$1,110,893	Employee Based	2017	
Belmont <sup>7</sup>	28,335	\$178,125	2,015	\$1,068,168	Employee Based	1990	
Burlingame	31,386	\$150,182	4,170	\$889,658	Flat Rate with Gross Receipts Measures	2022	

<sup>5</sup>Richmond adopted a new gross receipt tax structure in 2020 – Measure U.

<sup>6</sup>Union City is currently considering modernizing their business license tax.

<sup>7</sup>Belmont is currently considering modernizing their business license tax.

b. Business License Tax Revenue Per Capita

BLT revenue per capita is arguably one of the most important statistics that help determine how well a city’s business license tax structure produces revenue, given the population size. Additionally, revenue per business shows how productive a tax is once

the number of businesses is controlled for. These measures allow us to compare cities of varying populations and business communities.

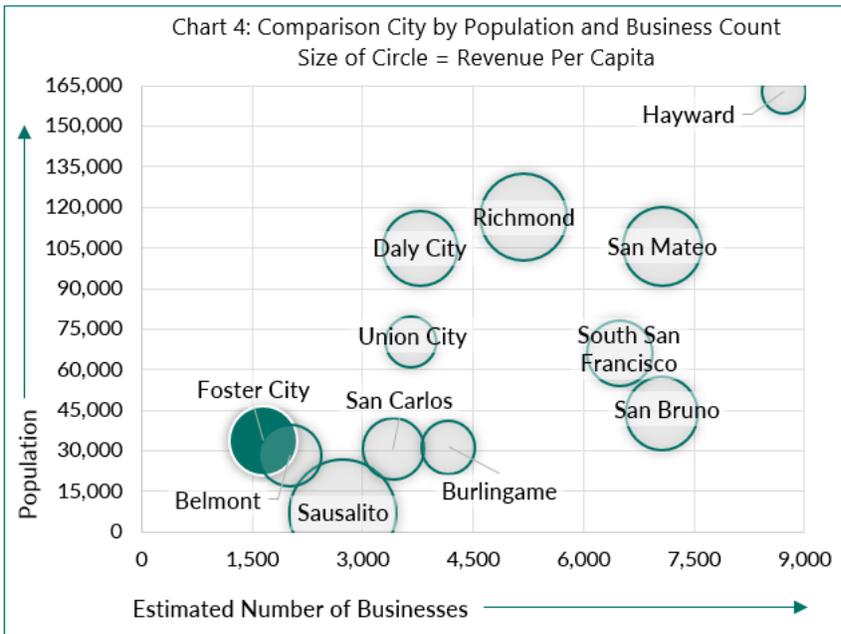


Table 3:  
Revenue Per Capita Comparison

City	Revenue Per Capita
Sausalito <sup>8</sup>	\$226.96
Richmond	\$72.92
San Mateo	\$62.83
Daly City	\$54.44
San Bruno	\$51.88
Foster City	\$46.85
South San Francisco	\$41.47
Belmont	\$37.70
San Carlos	\$36.16
Burlingame	\$28.35
Union City	\$25.49
Hayward	\$19.46

Source: HdL

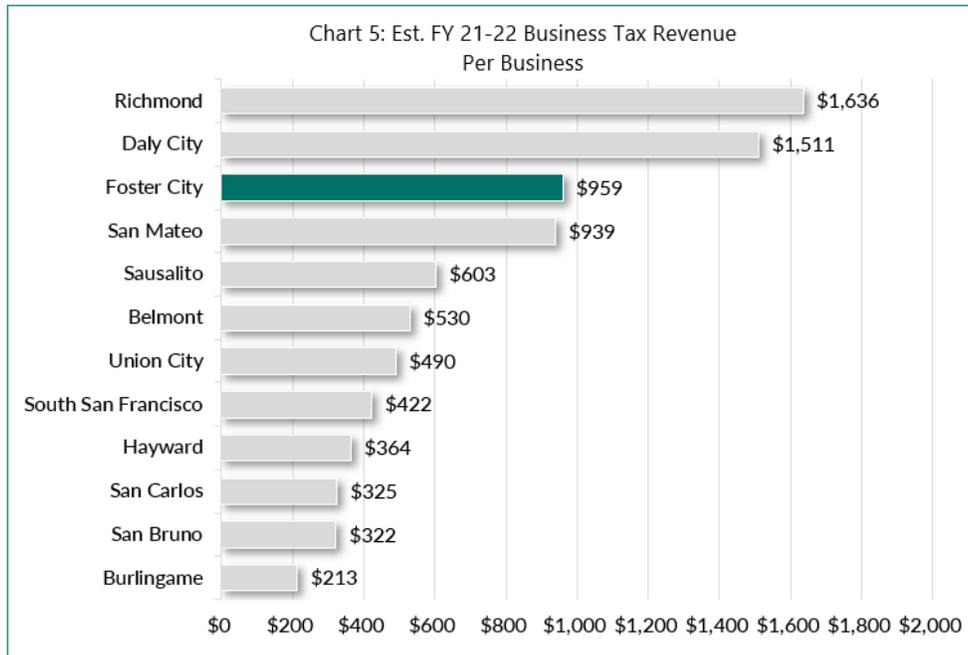
Foster City has an effective tax gross receipt rate of \$0.75 per thousand. Despite this favorable structure, the City’s cap means that not all of the gross receipts from large businesses in the City contribute to the total revenue. The City has several businesses that generate very large amounts of reported gross receipts. HdL’s initial analysis indicates that this cap is one of the main reason Foster City’s tax structure is less productive per capita than some other cities with a gross receipts structure.

Richmond passed a new measure in 2020 to a progressive gross receipts model (Measure U). The tax rates range from 0.075% to 1.395% of gross receipts. Other interesting comparisons are Daly City and San Mateo. Daly City’s tax structure is \$1.10 per thousand dollars with a \$100 minimum, while a portion of San Mateo’s businesses pay about \$0.57 per \$1,000 (for gross receipts over \$100,000). Both outproduce Foster City per capita. Please note that Sausalito was included because it adopted a change to its gross receipts structure in 2019 that provides an instructive comparison.

c. Business License Tax Revenue Per Business

When we account for the number of businesses in each City (by dividing revenues by the number of businesses), which yields a per-business measure of the tax, Foster City is in the top three cities in the comparison set for generating business license tax per business. Nevertheless, Richmond and Daly City also show that this category may have room for

growth. The Chart below shows estimated FY 21-22 Business Tax Revenue Per Business.



Source: HdL

d. Current Rate Comparison based on Sample Businesses

The Tables below show a comparison of tax from certain hypothetical businesses across these cities to show how the differing tax structures would produce different revenues.

Current Rate Comparison Based on Sample Businesses

Sample Business	Gross Receipts/ Employee/Units	Foster City	Belmont	Burlingame	Daly City	Hayward	Richmond
Outside Sub-Contractor	\$6,000 / 1 Emp	\$100	\$376	\$200	\$110	\$53	\$11
Home-Based Cottage Food / Retail	\$22,000 / 1 Emp	\$100	\$376	\$200	\$110	\$16	\$26
General Contractor - Remodeling	\$85,000 / 3 Emp	\$200	\$446	\$200	\$110	\$53	\$153
Business Service	\$450,000 / 5 Emp	\$338	\$516	\$300	\$385	\$120	\$810
Engineering Firm	\$500,000 / 5 Emp	\$375	\$516	\$300	\$440	\$632	\$1,550
Restaurant Chain	\$625,000 / 50 Emp	\$469	\$1,391	\$300	\$578	\$167	\$750
Family Dentistry	\$2,000,000 / 10 Emp	\$1,500	\$691	\$750	\$2,090	\$2,627	\$7,700
Apartment Complex	\$5,000,000 / 20 Emp / 150 Units	\$3,750	\$5,500	\$750	\$5,390	Repealed	\$144,000
Large Retailer - Grocery Store	\$20,000,000 / 300 Emp	\$15,000	\$10,841	\$750	\$21,890	\$5,399	\$24,850
Business Services - Large Firm	\$350,000,000 / 400 Emp	\$28,597	\$14,341	\$750	\$384,890	\$94,499	\$1,831,850
		\$50,429	\$34,994	\$4,500	\$415,993	\$103,566	\$2,011,700

Sample Business	Gross Receipts/ Employee/Units	Foster City	San Bruno	San Carlos	San Mateo	Sausalito	Union City
Outside Sub-Contractor	\$6,000 / 1 Emp	\$100	\$75	\$253	\$40	\$125	\$167
Home-Based Cottage Food / Retail	\$22,000 / 1 Emp	\$100	\$100	\$253	\$25	\$125	\$167
General Contractor - Remodeling	\$85,000 / 3 Emp	\$200	\$100	\$253	\$100	\$170	\$340
Business Service	\$450,000 / 5 Emp	\$338	\$478	\$271	\$366	\$1,350	\$194
Engineering Firm	\$500,000 / 5 Emp	\$375	\$530	\$321	\$394	\$1,500	\$279
Restaurant Chain	\$625,000 / 50 Emp	\$469	\$630	\$966	\$466	\$625	\$269
Family Dentistry	\$2,000,000 / 10 Emp	\$1,500	\$1,480	\$446	\$1,249	\$6,000	\$279
Apartment Complex	\$5,000,000 / 20 Emp / 150 Units	\$3,750	\$3,130	\$796	\$2,959	\$10,000	\$2,150
Large Retailer - Grocery Store	\$20,000,000 / 300 Emp	\$15,000	\$8,080	\$3,055	\$11,509	\$20,000	\$8,600
Business Services - Large Firm	\$350,000,000 / 400 Emp	\$28,597	\$116,980	\$3,055	\$199,609	\$1,050,000	\$150,500
		\$50,429	\$131,583	\$9,669	\$216,717	\$1,089,895	\$162,945

Source: HdL

When compared to some other cities in the region, Foster City is currently imposing a lower tax than about half of the comparison cities. The key driver of that difference is the City's cap on taxable gross receipts (as seen in the tax comparison for the Business Services-Large Firm category in the above tables).

#### IV. Foster City's Proposed Business License Tax Structure and Measure

Based on the analysis of the City's current business license tax structure and comparison to other cities, staff requested HdL to explore BLT models and options for modernizing the City's BLT structure. Using the data from the analysis of the current structure and comparison to other cities, HdL developed five models and estimated the fiscal impact of each, discussed benefits and impacts of each of these models. It is important to note that a discount factor is applied to all these models to account for fluctuations in gross receipts generated in the City and other uncertainties in the modeling. The initial models that were developed are discussed in detail below.

##### Model 1: Increase In Current Maximum Tax (Cap)

This model retains the existing structure and tax rate while modifying/increasing the tax cap. A simple increase to the business license tax cap could keep the existing structures in place while yielding higher revenues to the City. The drawback of Model 1 is that simply increasing the business license cap rate increases the effective rate for the largest business, but it also makes the revenues more dependent on the largest businesses. And, instead of being a more general tax modernization, it focuses only on the largest businesses.

### Model 2: Gross Receipts Tax – Single Gross Receipts Rate

Model 2 changes the existing single-rate gross-receipts model to a more effective tax rate. The “single rate” method of taxing on gross receipts provides an even distribution of the effective tax rate. All businesses subject to the tax will pay the same rate. This model implements \$1,000,000 maximum tax so only a few businesses would reach the gross receipts limits. This allows the City to get closer to total taxation of gross receipts generated in the City. Model 2 expands revenue while keeping the tax structure simple and easy to understand for businesses while asking larger businesses to pay a proportionally equivalent share. This model would raise the tax rate for mid-sized businesses and would lower the tax rate for those paying the minimum tax to \$25 to provide some tax relief for very small businesses when compared to the City’s current structure.

### Model 3: Gross Receipts Tax – Classifications-Based Rate

Model 3 would create different rates for different business classifications. The City might choose to implement a rate for the retail and wholesale business activities that recognize the higher costs of goods sold, lower profit margins, and their contribution to other City revenues such as collecting and remitting sales tax. At the same time, the City could consider implementing a higher rate for professionals due to the nature of their business model. This model offers the most flexibility for increasing revenues while accommodating certain business categories. Model 3 is tailored to shifting more of the tax to property rentals and professional services and spreads the tax burden across multiple business types. The model retains most of the administrative efficiencies of Model 2 by having a simple structure of just six categories.

### Model 4: Tiered Gross Receipts

This model attempts to mitigate the regressivity in the City’s business license tax structure with a gross receipts measure that increases the share that large businesses pay and provides lower taxes for small businesses. The model removes or increases the cap, creates a lower minimum, and uses different tax structures to test different configurations of the tiered approach. Under this model, businesses making less than \$100,000 pay less tax because of the decreased minimum tax. Overall, the number of businesses that would see an increase in tax owed is less than 30% of businesses.

### Model 5: Uniform Employee Tax Rate

This model switches the tax base away from gross receipt model to an alternative tax structure – a uniform employee tax rate. This model is simple – allows the City to implement a structure without a cap. Unlike gross receipts, City wide employee count may have less volatility—although the rise in remote or hybrid work could increase volatility and reduce the usefulness of this measure of the tax. This model is a useful comparison to the gross-receipts models. It would produce about the same amount of revenue as the current model.

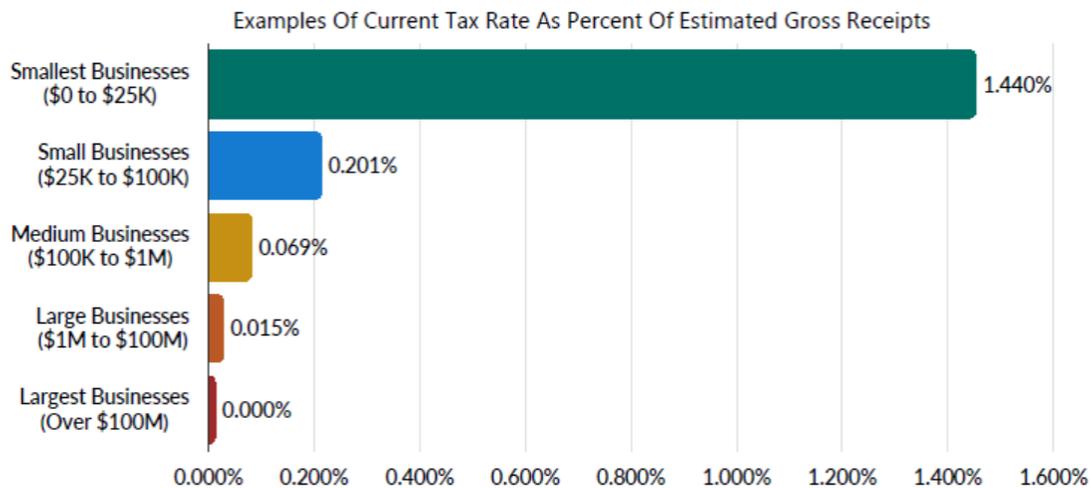
For additional information and revenue estimates for each of the above models, refer to Attachment 1 – Business Tax Analysis prepared by HdL Companies (pages 11-20).

Note: Staff did initially discuss a square-footage model with HdL, but the data was hard to obtain, and the model would have the side-effect of only taxing businesses with an office in the City, thus giving an advantage to businesses that come in from outside the City to do business. As noted in an earlier section of the report, the disadvantages of this model outweighed its benefits.

## STAFF COMMENTS

In analyzing the current BLT model and researching the BLT structure used in other cities, staff came to the following conclusion:

- The gross receipts model is becoming increasingly popular and is the preferred model due to its relatively simple tax structure that allows for adaptability.
- The current fixed gross receipts tax rate of \$0.75 per thousand, which has remained the same since 1972, is regressive in nature. A regressive gross receipts tax requires all businesses to pay at the same BLT rate regardless of the value of the taxable gross receipts that each individual business reports. In other words, businesses that report lower taxable gross receipts pay a disproportionate share of the BLT burden when compared to larger businesses. As illustrated in the graphic below, the larger businesses (in red) are paying proportionally less than the small businesses (green) and medium businesses (yellow) based on estimated gross receipts.



- The business tax base is unique in Foster City given that approximately 70% of the businesses are small businesses (reporting less than approximately \$133,000 in gross receipts annually) and a very small percentage (less than 5%) of the businesses report extremely high gross receipts.

- The City's current tax limit exemption on the number of multiple corporate entities to three (3) entities does not benefit the City's tax structure.
- The business license tax applies to taxable activity namely, conducting businesses in the City. If a business is doing business both inside and outside the City, that business can request apportionment so that it is reporting the gross receipts that appropriately reflect the amount of taxable activity attributable to the City. The city's current Ordinance language allows for this, and the intent is to continue allowing businesses to apply for apportionment in the modernized code.

The five early models discussed above provided a starting point for discussion for staff. While all the models demonstrated revenue growth potential, the impact of the specific rates and the increased tax burden on businesses, the current rate for business license tax, the administration of the BLT and alignment with the City's goals were taken into consideration as staff review the various options. While narrowing down to a preferred model (Model 4), the following objectives were taken into consideration:

- Minimal to no impact on small businesses.
- A modern progressive rate structure that is equitable and fair.
- A modest increase to the gross receipt rate for middle to large businesses.
- Creating tiers so that medium to large businesses pay a lower rate (share of the overall BLT) than the largest businesses.
- A new increased maximum for large businesses.
- Potential to generate additional revenue to support core City services.

The tiered rate structure (Model 4) involves a tax rate that increases (or progresses) as taxable gross receipts increase. It imposes a lower tax rate on businesses that report lower taxable gross receipts and a higher tax rate on those businesses that report higher taxable gross receipts. A progressive tiered rate structure group businesses into different tiers with varying tax rates that is proportional to the range of taxable gross receipts within that tier.

#### MODEL 4 – TIERED GROSS RECEIPTS

Staff requested HdL to provide variations of Model 4 - Tiered Gross Receipts Structure with varying tiered rates (modest to slightly larger increase for the middle tiers and a much larger increase for the topmost tier), maintaining the minimum tax of \$100 for small businesses, a maximum tax cap of either \$250,000 or \$500,000 and overall revenue generation potential (in the \$2 to \$3 million range). In the Model 4 variations presented below, businesses will pay \$100 for the first \$250,000 of gross receipts. Businesses making an excess of \$25 million will pay on gross receipts until they reach the maximum tax imposed by the City (\$250,000 or \$500,000).

**Model 4X-1 – Estimated Additional Revenue Potential - \$2.36 million**

Model 4X-1: Gross Receipts \$1.25 to \$3.00 with \$250K Cap

Measure Index	Gross Receipts Range	Gross Receipt Rate	Minimum Tax	Number of Businesses	Model 4X-1 Revenue
1	\$0 to \$250,000	\$0.00	\$100.00	1,287	\$128,700
2	\$250,000 to \$4,400,000	+\$1.25 per \$1,000	\$100.00	276	\$324,366
3	\$4,400,000 to \$8,500,000	+\$1.54 per \$1,000	\$5,287.50	39	\$299,118
4	\$8,500,000 to \$12,650,000	+\$1.83 per \$1,000	\$11,608.33	14	\$220,531
5	\$12,650,000 to \$16,750,000	+\$2.13 per \$1,000	\$19,216.67	11	\$257,834
6	\$16,750,000 to \$20,900,000	+\$2.42 per \$1,000	\$27,929.17	3	\$91,134
7	\$20,900,000 to \$25,000,000	+\$2.71 per \$1,000	\$37,958.33	1	\$44,047
8	Gross Receipts Over \$25,000,000	+\$3.00 per \$1,000 (Max \$250,000)	\$49,062.50	20	\$2,728,446
				1,651	\$4,094,176

**Model 4X-2 – Estimated Additional Revenue Potential - \$1.46 million**

Model 4X-2: Gross Receipts \$0.75 to \$3.00 with \$250K Cap

Measure Index	Gross Receipts Range	Gross Receipt Rate	Minimum Tax	Number of Businesses	Model 4X-2 Revenue
1	\$0 to \$250,000	\$0.00	\$100	1,287	\$128,700
2	\$250,000 to \$4,400,000	+\$0.75 per \$1,000	\$100	276	\$205,660
3	\$4,400,000 to \$8,500,000	+\$0.88 per \$1,000	\$3,213	39	\$178,018
4	\$8,500,000 to \$12,650,000	+\$1.00 per \$1,000	\$6,800	14	\$126,844
5	\$12,650,000 to \$16,750,000	+\$1.13 per \$1,000	\$10,950	11	\$145,041
6	\$16,750,000 to \$20,900,000	+\$1.25 per \$1,000	\$15,563	3	\$50,488
7	\$20,900,000 to \$25,000,000	+\$1.38 per \$1,000	\$20,750	1	\$23,841
8	Gross Receipts Over \$25,000,000	+\$3.00 per \$1,000 (Max \$250,000)	\$26,388	20	\$2,342,971
				1,651	\$3,201,563

**Example:**

If a company reports \$50,000,000 in annual gross receipts, their annual maximum business license tax will be as follows:

Model 4X-1 would be  $\$49,062.50 + \$75,000 = \$124,062.50$

Model 4X-2 would be  $\$26,388 + \$75,000 = \$101,388.00$

**Model 4Y-1 – Gross Receipts \$1.25 to \$3.50 with \$500K Cap**

Model 4Y-1: Gross Receipts \$1.25 to \$3.00 with \$500K Cap

Measure Index	Gross Receipts Range	Gross Receipt Rate	Minimum Tax	Number of Businesses	Model 4Y-1 Revenue
1	\$0 to \$250,000	\$0.00	\$100	1,287	\$128,700
2	\$250,000 to \$4,400,000	+\$1.25 per \$1,000	\$100	276	\$324,366
3	\$4,400,000 to \$8,500,000	+\$1.50 per \$1,000	\$5,288	39	\$296,607
4	\$8,500,000 to \$12,650,000	+\$1.75 per \$1,000	\$11,438	14	\$215,502
5	\$12,650,000 to \$16,750,000	+\$2.00 per \$1,000	\$18,700	11	\$249,418
6	\$16,750,000 to \$20,900,000	+\$2.25 per \$1,000	\$26,900	3	\$87,540
7	\$20,900,000 to \$25,000,000	+\$2.50 per \$1,000	\$36,238	1	\$41,858
8	Gross Receipts Over \$25,000,000	+\$3.50 per \$1,000 (Max \$500,000)	\$46,488	20	\$3,625,401
				1,651	\$4,969,392

**Model 4Y-2 – Estimated Additional Revenue Potential - \$2.93 million**

Model 4Y-2: Gross Receipts \$0.75 to \$3.50 with \$500K Cap

Measure Index	Gross Receipts Range	Gross Receipt Rate	Minimum Tax	Number of Businesses	Model 4Y-2 Revenue
1	\$0 to \$250,000	\$0.00	\$100.00	1,287	\$128,700
2	\$250,000 to \$4,400,000	\$0.75 per \$1,000	\$100.00	276	\$205,660
3	\$4,400,000 to \$8,500,000	\$1.21 per \$1,000	\$3,212.50	39	\$198,105
4	\$8,500,000 to \$12,650,000	\$1.67 per \$1,000	\$8,166.67	14	\$167,073
5	\$12,650,000 to \$16,750,000	\$2.13 per \$1,000	\$15,083.33	11	\$212,367
6	\$16,750,000 to \$20,900,000	\$2.58 per \$1,000	\$23,795.83	3	\$79,241
7	\$20,900,000 to \$25,000,000	\$3.04 per \$1,000	\$34,516.67	1	\$41,354
8	Gross Receipts Over \$25,000,000	\$3.50 per \$1,000 (Max \$500,000)	\$46,987.50	20	\$3,633,901
				1,651	\$4,666,401

**Example:**

If a company reports \$50,000,000 in annual gross receipts, their annual maximum business license tax will be as follows:

Model 4Y-1 would be \$46,488 + \$87,500 = \$133,988.00

Model 4Y-2 would be \$46,987.50 + \$87,500 = \$134,487.50

Overall Gross Receipts Taxed Per Model and Tax Cap

Categories	4X-1 - \$250K	4X-2 - \$250K	4Y-1 - \$500K	4Y-2 - \$500K
Model Maximum Tax Limit	\$250,000	\$250,000	\$500,000	\$500,000
Taxable Gross Receipt of the 1st 7 Tiers	\$25,000,000	\$25,000,000	\$25,000,000	\$25,000,000
Gross Receipt Taxed at Final Tier	\$66,979,167	\$74,537,500	\$129,575,000	\$129,432,143
<b>Total Gross Receipt Taxed</b>	<b>\$91,979,167</b>	<b>\$99,537,500</b>	<b>\$154,575,000</b>	<b>\$154,432,143</b>
<b>Estimated Additional Revenue for the model</b>	<b>\$2.36 million</b>	<b>\$1.46 million</b>	<b>\$3.23 million</b>	<b>\$2.93 million</b>

Current Rate Comparison Based on Sample Businesses

Sample Business	Gross Receipts/ Employee/Units	Foster City	Model 4X-1 \$250k	Model 4X-2 \$250K	Model 4Y-1 \$500K	Model 4Y-2 \$500K	Belmont	Burlingame	Daly City
Restaurant Chain	\$625,000 / 50 Emp	\$469	\$569	\$381	\$569	\$381	\$1,391	\$300	\$578
Large Retailer - Grocery Store	\$20,000,000 / 300 Emp	\$15,000	\$31,992	\$19,625	\$34,213	\$32,192	\$10,841	\$750	\$21,890
Business Services - Large Firm	\$350,000,000 / 400 Emp	\$28,597	\$250,000	\$250,000	\$500,000	\$500,000	\$14,341	\$750	\$384,890
		\$44,066	<b>\$282,561</b>	\$270,006	\$534,782	<b>\$532,573</b>	\$26,573	\$1,800	\$407,358

Sample Business	Gross Receipts/ Employee/Units	Foster City	Model 4X-1 \$250k	Model 4X-2 \$250K	Model 4Y-1 \$500K	Model 4Y-2 \$500K	Hayward	Richmond	San Bruno
Restaurant Chain	\$625,000 / 50 Emp	\$469	\$569	\$381	\$569	\$381	\$167	\$750	\$630
Large Retailer - Grocery Store	\$20,000,000 / 300 Emp	\$15,000	\$31,992	\$19,625	\$34,213	\$32,192	\$5,399	\$24,850	\$8,080
Business Services - Large Firm	\$350,000,000 / 400 Emp	\$28,597	\$250,000	\$250,000	\$500,000	\$500,000	\$94,499	\$1,831,850	\$116,980
		\$44,066	<b>\$282,561</b>	\$270,006	\$534,782	<b>\$532,573</b>	\$100,065	\$1,857,450	\$125,690

Sample Business	Gross Receipts/ Employee/Units	Foster City	Model 4X-1 \$250k	Model 4X-2 \$250K	Model 4Y-1 \$500K	Model 4Y-2 \$500K	San Carlos	San Mateo	Sausalito	Union City
Restaurant Chain	\$625,000 / 50 Emp	\$469	\$569	\$381	\$569	\$381	\$966	\$466	\$625	\$269
Large Retailer - Grocery Store	\$20,000,000 / 300 Emp	\$15,000	\$31,992	\$19,625	\$34,213	\$32,192	\$3,055	\$11,509	\$20,000	\$8,600
Business Services - Large Firm	\$350,000,000 / 400 Emp	\$28,597	\$250,000	\$250,000	\$500,000	\$500,000	\$3,055	\$199,609	\$1,050,000	\$150,500
		\$44,066	<b>\$282,561</b>	\$270,006	\$534,782	<b>\$532,573</b>	\$7,076	\$211,584	\$1,070,625	\$159,369

In the four variations of Model 4 provided above, it can be seen that Model 4X-2 which generates the lowest amount of additional revenue (\$1.46 million) is what would also have the least impact on businesses. Model 4X-2 includes: a modest increase for the medium sized businesses (a gradual increase from the current 0.75 tax rate); a significant impact on the largest grossing businesses that currently pay a maximum tax of approx. \$29,397 as of 2024 will see a 9x increase with a \$250K max tax cap or a 17x increase with a \$500K max tax cap; and a reasonable rate for businesses like restaurants and large retailer/grocery stores.

Based on the information provided above and the community feedback provided (see below section), staff has the following policy direction questions for the City Council:

- a. The preferred Business License Tax model;
- b. Whether to consider phasing the maximum tax cap over a three (3) year period for the preferred model;

- c. Whether to keep or eliminate the current FCMC exemption provision related to multiple corporate entities; and
- d. Whether to proceed with a potential ballot measure to increase the Business License Tax for the November 2024 General Election.

## STAKEHOLDER OUTREACH AND ENGAGEMENT

BLT stakeholder outreach and engagement efforts to date include:

- Social media: Feb: 27 (boosted); March: 4, 6, 19 & 29; April: 4, 17 & 30; May: 6 & 13, additional posts forthcoming through the end of the month.
- Public Polling/Voter Survey: March 2024
- Fiscal Sustainability Survey: February 27 through the end of May
- Newsletter: 3/14, 3/28 & 5/9
- Mayoral Minute: 5/9
- Website: Published 2/22 and FAQs added ([Link](#))
- Business appointment scheduler added 4/18 – Multiple time slots offered on City website for businesses to schedule an appointment and offer both in-person and virtual options.
- Direct email:
  - Community organizations: 4/18, follow up 5/1
  - Businesses: 4/18 (top 20 large employers)
  - 4/24 – 4/25 (additional large employers)
  - 5/1 (follow up to top 20 plus other larger employers)
  - 5/3 (all business license holders – approx. 1300 emails)
  - 5/13 (follow up email to all business license holders + large employers)
- Press release: 5/9
- Recology mailer: 2/28, 5/30 (forthcoming)
- Digital marquee, FCTV + posting boards: 5/13
- Printed flyers (council chambers, city hall lobby, library, levee kiosks): 5/13
- Planned Town Hall Meetings (May 29<sup>th</sup> & May 30<sup>th</sup>)

### 1. Public Polling/Voter Survey

In March 2024, FM3 completed 343 interviews with randomly selected, likely November 2024 voters in Foster City in order to assess the viability of a potential ballot measure to modernize the city's BLT. Interviews were conducted online and via telephone. Results of the polling/voter survey are included in Attachment 2.

### 2. Fiscal Sustainability Survey

The City promoted a Fiscal Sustainability Survey asking the community to identify their priorities on public safety, parks, infrastructure, and more. The Survey was released on February 27. The survey is ongoing and will be open through the end of May. To date, 138 respondents have responded to the survey. The results of the survey are included in Attachment 3.

### 3. Business Stakeholder Outreach

The City conducted in-person and virtual outreach to various sized businesses. Some of these meetings were convened in collaboration with the Foster City Chamber of Commerce. Staff also set up a website allowing individual businesses to schedule briefings with City staff and consultants. Feedback has ranged. Some participants have expressed their understanding of the fiscal challenges facing the City, and even their openness to an updated BLT structure. Larger firms with potentially higher rates have naturally raised concerns about the increase in tax and additional questions about the impact and structure of the potential changes. Firms that are the most impacted (subject to the maximum tax) expressed concerns about their current tax increasing 9 to 18 times with the \$250K and \$500K cap respectively. Outreach is slated to expand to residents and the business community in the coming weeks. Depending on the direction received at the May 20<sup>th</sup> meeting, the City will host two Townhall Meetings and will be increasing distribution of information on both the potential BLT update as well as the City's fiscal condition.

Feedback/Questions received from Businesses include the following:

- Concerns about the tax increases faced by the multiple entities under the same management in Foster City.
  - Suggested limiting taxing multiple entities to avoid paying separately for each entity.
- Questions regarding apportionment. There is language in the existing ordinance regarding apportionment, but some have said they may scrutinize these provisions more closely the higher the levy rises. Some have cautioned they believe the bulk of their receipts/operations are located outside of the City and would impact how they report gross receipts moving forward.
- Smaller business owners have characterized efforts to reduce the relative share of BLT paid by small firms as “fair”, and others even expressed a willingness to pay modest increases to support the City.
- Concerns about the proposed tax increase, questioning how it would address the identified budget deficits, and if the City will continue to move the goal post on businesses by looking at future BLT increases.
- Concerns about the exponential increase affecting the largest firms with consideration to a phased approach (even for \$250k maximum tax model).
- The increase to the maximum tax is unreasonable.
- Questions about how the city is funding the remaining gap in the budget.
- Sourcing receipts gets complicated, and predictability is important.
- If the City has considered the fiscal impact if one or more large businesses leave the City and take their business to a more tax-friendly city.
- If the City has considered the loss of sales tax revenue that may potentially be lost if the large businesses leave the City.
- How the revenue numbers were taken into consideration for various models.

- Almost all the stakeholders emphasized that they are sympathetic and supportive towards the city's financial constraints.
- Some small business owners noted that they would not mind paying \$200 instead of the minimum \$100 tax.
- A small business owner expressed concern about being double taxed, paying for taxes in other places for the same earnings.
- Some small business owners were perplexed with the models presented by staff that showed zero increase to their tax structure as they received certain messages showing that City is increasing taxes ranging from 9x to 17x.
- The idea of modernization of tax structure sounds reasonable, large businesses should pay their fair share.
- If City has taken into considered impact fees, permit fees, and property tax that a large business pays i.e. the cost of doing business in the City.
- Some business owners expressed appreciation for all the facilities that the City offers and noted that the proposed increase in tax is completely understandable and is supportive of the same.
- Question regarding the potential impact of city business license fees updates on utility providers.

#### One-on-one outreach meetings held to date:

- Wednesday, May 1, 2024, 2:00 pm in-person meeting (Gilead)
- Thursday, May 9, 2024, 10:00 am virtual meeting (Chamber, multiple businesses)
- Thursday, May 9, 2024, 1:00 pm virtual meeting (Visa)
- Thursday, May 9, 2024, 2:00 pm in-person meeting (Chambers, multiple businesses)
- Wednesday, May 15, 2:00 pm virtual meeting (Cowan Capital)
- Wednesday, May 15, 1:00 pm virtual meeting (PG&E)
- Wednesday, May 15, 1:00 pm virtual group meeting (Chambers, multiple businesses)
- Thursday, May 16, 2024, 2:00pm virtual meeting (Bailard)
- Thursday, May 16, 2024, 10:00 am virtual meeting (Zoox)
- Thursday, May 16, 2024, 11:00 am virtual meeting (Sycomp)

#### NEXT STEPS – ACTIONS REQUIRED AND ELECTION OVERVIEW

The City's current BLT is considered a general tax because funds generated from the tax are considered general fund revenues that can be used for any governmental purpose. A potential ballot measure to increase the BLT that utilizes funds generated from the tax in same manner would also be a general tax that would require a 2/3rd majority vote of the City Council (4 out of 5 Councilmembers) to be placed on the ballot and a simple majority vote (50% + 1) of the voters to pass. By law, a general tax may only be placed on the ballot when there is a City Council election, except in cases of emergency declared by a unanimous vote of the City Council. California Constitution Article XIII C Section 2(b)

governs this requirement, which restricts the placement of such a measure during such election years.

### Calling for Election and Consolidation of Election

A separate resolution is necessary to call for the election and place the measure on the ballot for the November 5, 2024, General Municipal Election. The County of San Mateo's deadline for the City to call an election and request consolidation for the election is July 3, 2024. Per the Elections Code, if the City Council wants to place a measure on the November 5th ballot, the Council must also adopt a resolution placing any such measures on the ballot and submit it to the County of San Mateo Board of Supervisors and Assessor County Clerk-Recorder Elections' Office no later than 5:00 PM on August 9, 2024. The resolution would contain the wording of the measure as it would appear on the ballot and request its consolidation with the November 5, 2024, General Election. At the meeting placing a potential measure on the ballot, the City Council would also establish Argument and Rebuttal deadlines that correspond to the deadlines set by the County. Based on the direction received at the May 20<sup>th</sup> Council Meeting, staff anticipates returning to the City Council to adopt a resolution to call the election and potentially placing a measure on the ballot in June 2024.

### California Environmental Quality Act

This activity is not a project under California Environmental Quality Act (CEQA) as defined in CEQA Guidelines, section 15378, because it has no potential for resulting in either a direct or reasonably foreseeable indirect physical change in the environment.

### FISCAL IMPACT

If approved by voters, an increase to the business license tax could potentially generate additional revenue in the amount of \$1.46 million to \$3.23 million depending on Council's preferred model.

### CITY COUNCIL VISION, MISSION, AND VALUE/PRIORITY AREA

Smart Planning, Development, and the Local Economy

### ATTACHMENTS:

Attachment 1 – Business Tax Analysis prepared by HdL Companies

Attachment 2 – Public Polling/Voter Survey by FM3 Research

Attachment 3 – Fiscal Sustainability Survey Results (to date)

Attachment 4 – Stakeholder Meeting PowerPoint Presentation

## PAST MEETING LINKS

- March 7, 2022 (Item 8.3) – [Mar 07, 2022 City Council Regular Meeting - Foster City, CA \(swagit.com\)](#)
- April 4, 2022 (Item 7.2) – [Apr 04, 2022 City Council Regular Meeting - Foster City, CA \(swagit.com\)](#)
- June 6, 2022 (Item 8.2) – [Jun 06, 2022 City Council Regular Meeting - Foster City, CA \(swagit.com\)](#)
- October 16, 2023 (Item 8.2) – [Oct 16, 2023 City Council Regular Meeting - Foster City, CA \(swagit.com\)](#)
- December 18, 2023 (Item 6.14) – [Dec 18, 2023 City Council Regular Meeting - Foster City, CA \(swagit.com\)](#)
- February 5, 2024 (Item 7.1) – [Feb 05, 2024 City Council Regular Meeting \(trimmed\) - Foster City, CA \(swagit.com\)](#)