File No. 081449 Committee Item No. 6
Board Item No. ________

COMMITTEE/BOARD OF SUPERVISORS

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Completed by: Victor Young **Date** November 26, 2008
Completed by: ________ **Date** ________

An asterisked item represents the cover sheet to a document that exceeds 25 pages.
The complete document is in the file.

[Changes to the Payroll Expense Tax exclusion for clean energy technology businesses.]

Ordinance amending San Francisco Business and Tax Regulations Code by amending Section 906.2 to eliminate limits on company size and expand the definition of qualifying business activities.

Note: Additions are *single-underline italics Times New Roman*; deletions are ~~*strikethrough italics Times New Roman*~~. Board amendment additions are double underlined. Board amendment deletions are ~~strikethrough normal~~.

Be it ordained by the People of the City and County of San Francisco:

Section 1. The San Francisco Business and Tax Regulations Code is hereby amended by amending Section 906.2 of Article 12-A to read as follows:

SEC. 906.2. CLEAN ~~*ENERGY*~~ TECHNOLOGY BUSINESS EXCLUSION.

(a) Any person that employs a full-time staff of ~~*at least ten*~~ but not more than one hundred employees and is engaging in a clean ~~*energy*~~ technology business may exclude from the person's payroll expense all compensation paid to, on behalf of or for the benefit of the person's employees, and all distributions by an association by way of salary to those having an ownership interest in such association, who or that perform substantially all work or render substantially all services in direct support of such person's clean ~~*energy*~~ technology efforts, subject to the conditions and limitations set forth in this Section. For purposes of this Section, outside independent contractors shall not be considered employees of the clean ~~*energy*~~ technology business.

(b) For purposes of this section, the terms "person," "business," "association," clean ~~*energy*~~ technology" and "clean ~~*energy*~~ technology business" have the following meanings:

(1) The term "person" includes the combination of all subsidiaries, affiliates and other business entities related by ownership including but not limited to partnerships, joint ventures, limited liability companies, corporations and other business organizations of whatever form. Any beneficial ownership of the stock of publicly traded corporations shall not be considered for purposes of this definition.

(2) The term "business" is as defined in Section 6.2-5 of Article 6 of the San Francisco Business and Tax Regulations Code.

(3) The term "association" is as defined in Section 6.2-4 of Article 6 of the San Francisco Business and Tax Regulations Code.

(4) "Clean ~~*energy*~~ technology" means the development, manufacture or application of scientific advances that *a)* produce or contribute to the production of *or enable the use of* clean energy, *or b) result in quantifiable energy or water conservation, or c) result in greenhouse gas or toxics reductions, or d) make or enable carbon trading markets, including the verification of projects that produce carbon credits. Clean energy is defined as* ~~*utilizing energy produced by*~~ wind, solar energy, landfill gas, geothermal resources, ocean thermal energy conversion, ~~*quantifiable energy conservation measures,*~~ tidal energy, wave energy, biomass, biofuels, or hydrogen fuels derived from renewable sources. *Quantifiable energy or water conservation applications are defined as energy efficiency engineering and retrofit, energy storage devices for renewable energy, energy efficiency, electric vehicles and toxics reduction applications, "green" building materials as certified by LEED, technological developments for water conservation or purification, and enabling technology for the previously stated applications.* Clean ~~*energy*~~ technology does not include: (A) *general electrical contractors (B)* ~~*the installation of clean energy technologies,*~~ (B) any fossil fuel based energy production, including but not limited to, clean coal, clean diesel, natural gas and hydrogen from natural gas, (C) any nuclear based energy production, (D) waste to energy via combustion or incineration, or (E) other technologies that

are detrimental to human health. The Board of Supervisors may amend this legislation to include future technologies.

(5) "Clean ~~energy~~ technology business" means a business in which at least seventy-five percent of all business activities carried on during the tax year are directly related to clean ~~energy~~ technology.

(c) In order to be eligible for the payroll expense tax exclusion authorized under this Section, persons wishing to claim the exclusion must:

(1) Complete and submit an initial application to the Director of the Department of the Environment for review and evaluation.

(2) After approval, file an annual affidavit with the Department of the Environment affirming that they continue to meet the eligibility criteria set forth in regulations adopted by the Department of the Environment. The affidavit must be filed with the Department of the Environment on or before January 31 of every year after the year the application is first approved.

(3) Maintain a reasonable method of documentation that can be reviewed or verified objectively that tracks how employees whose compensation qualifies for the payroll expense tax exclusion spend their time at work, and provide such documentation to the Tax Collector upon request.

(4) File an annual Payroll Expense Tax Return with the Tax Collector regardless of the amount of tax liability shown on the return after claiming the exclusion provided for in this Section.

(5) Obtain or maintain a Green Business recognition, if available as to that business, from the City under Chapter 15 of the Environment Code during the tax year for which the payroll tax exemption is requested.

(d) The Director of the Department of the Environment shall:

(1) No later than the effective date of this ordinance, after a public hearing, adopt rules, regulations and forms regarding eligibility and the application process for the payroll tax expense exclusion. The Director of the Department of the Environment may amend such rules, regulations and forms from time to time as necessary.

(2) Review all applications for completeness and if an application is approved issue a certificate of eligibility to the applicant. The Director's decision on the application shall be final.

(3) Provide the Tax Collector with a list of persons eligible to claim the tax exclusion authorized under this Section for the preceding tax year by March 1 of each year. The Tax Collector shall grant or deny the tax exclusion on the basis of the Department of the Environment's determination along with the review, at the Tax Collector's option, of the documentation maintained by the employer under Subsection (c)(3) of this Section.

(e) The clean ~~*energy*~~ technology exclusion authorized under this Section shall be available to and may be taken by a person for each tax year that person holds a valid certificate of eligibility for a period of ten years from the effective date of this Section or the commencement of the person's clean ~~*energy*~~ technology business in the City, whichever is later. The date the Tax Collector first received the person's application for a business registration certificate for the person's clean ~~*energy*~~ technology business shall be presumed to be the date of commencement of such business unless the person establishes a different commencement date to the satisfaction of the Tax Collector.

(f) The clean ~~*energy*~~ technology exclusion authorized under this Section shall expire on the fifteenth anniversary date of the effective date of this Section. A person may not use or claim any unused portion of the ten year clean ~~*energy*~~ technology exclusion after the expiration date of this Section. Unless exempted under Sections 906 of this Article, every person engaging in a clean ~~*energy*~~ technology business in the City shall pay the tax imposed under this Article on the full amount of the person's payroll expense attributable to the City from and after the expiration of this Section.

(g) If a person's calculated liability for the Payroll Expense Tax does not exceed $2,500 for the tax year after applying the clean ~~energy~~ technology exclusion under this Section, the person shall be exempt from payment of the Payroll Expense Tax for that tax year as provided in Section 905-A.

(h) The effective date of this ordinance shall be January 1, 2006.

(i) The Tax Collector shall submit an annual report to the Board of Supervisors for each year for which the clean ~~energy~~ technology exclusion authorized under this Section is available that sets forth aggregate information on the dollar value of the clean ~~energy~~ technology exclusions taken each year, the number of businesses taking the exclusion, the change in the number of clean ~~energy~~ technology businesses engaging in business in the City, and any identifiable increase or decrease in the number of jobs in the clean ~~energy~~ technology business sector compared to the number of jobs in the clean ~~energy~~ technology business sector for the immediately preceding calendar year.

(j) The Assessor-Recorder shall submit an annual report to the Board of Supervisors for each year for which the clean ~~energy~~ technology exclusion authorized under this Section is available that sets forth any identifiable increases in property taxes resulting from clean ~~energy~~ technology businesses location, relocation or expansion to or within the City.

(k) The Controller, after three years from the enactment of this Ordinance, shall perform an assessment and review of the effect of the clean ~~energy~~ technology tax exclusion. Based on such assessment and review the Controller shall prepare and submit an analysis to the Board of Supervisors. The analysis shall be based on criteria deemed relevant by the Controller, and may include but is not limited to, data contained in the annual reports to the Board of Supervisors as required by subsections (i) and (j) of this Section.

(l) A misrepresentation or misstatement by any person regarding eligibility for the clean ~~energy~~ technology payroll expense tax exclusion authorized by this section that results in the underpayment or underreporting of the payroll expense tax shall be subject to penalties as provided in Section 6.17-2 of Article 6 of the San Francisco Business and Tax Administrative Code.

APPROVED AS TO FORM:
DENNIS J. HERRERA, City Attorney

By: ______________________
Catharine Barnes
Deputy City Attorney

FILE NO. 081449

LEGISLATIVE DIGEST

[Business and Tax Regulation Code – Cleantech Payroll Tax Exclusion.]

Ordinance amending San Francisco Business and Tax Regulations Code by amending Section 906.2 to eliminate limits on company size and expand the definition of qualifying business activities.

Existing Law

Business and Tax Regulations Code by amending Section 906.2 allows qualifying clean energy technology businesses a payroll tax exclusion for employees devoting 75% or more of their time to qualifying activities. The current exclusion applies only to companies that have between 10 and 100 employees.

Amendments to Current Law

This legislation would make two primary changes to the existing exclusion. The first change removes the minimum size requirement for eligible companies. The second change clarifies and expands the current definition of what qualifies as a cleantech company based on emerging technologies and trends within the sector, including: adding companies whose products or services enable the use of clean energy technology; adding water efficiency technologies; adding greenhouse and toxics reduction technologies; adding business that make or enable carbon trading markets; and adding businesses that install clean technologies.

Item 6 - File 08-1449

Department: Treasurer and Tax Collector

Item: Ordinance amending the Business and Tax Regulations Code by amending Section 906.2 pertaining to the City's Payroll Expense Tax exclusion for clean technology businesses (a) by removing the current minimum number of 10 employees employed by businesses and (b) by expanding the definition of qualifying business activities for clean energy technology businesses eligible for exclusion from the City's Payroll Expense Tax liability.

Description: Section 906.2 of Article 12-A of the Business and Tax Regulations Code provides for exclusions, to businesses engaged in clean energy technology, from the City's Payroll Expense Tax Liability. Presently, the Payroll Tax exclusion applies to any business that employs a full-time staff of at least 10 but not more than 100 employees engaged in clean energy technology.

Under the existing Payroll Tax exclusion, the business may exclude the amount the business would owe for the City's Payroll Taxes from (a) all compensation paid to, on behalf of or for the benefit of businesses which employ at least 10 but not more than 100 employees engaged in clean energy technology, and (b) from all distributions of salary to persons having an ownership interest in the business, who perform substantially all work or render all services substantially in direct support of the business' clean energy technology efforts, subject to the conditions and limitations set forth in Section 906.2.

The proposed ordinance would amend Section 906.2 of Article 12-A of the Business and Tax Regulations Code to remove the minimum number of at least 10 employees of businesses engaging in clean energy technology, such that any employer with between one (instead of at least 10) and 100 employees engaged in a "Clean Technology" business, as distinct from the presently defined "Clean Energy Technology" businesses would qualify for the City's Payroll Expense Tax exclusion. Therefore, the minimum number of employees to be eligible for the Payroll Tax exclusion would be reduced from 10 employees to one employee.

Further, the proposed ordinance would amend Section 906.2 of Article 12-A of the Business and Tax Regulations Code to change the term "clean energy technology" to "clean technology" and expand the definition of "clean technology" as shown in the following table.

Current Definition of clean energy technology:	Proposed Definition of clean technology:
"Clean energy technology" means the development, manufacture or application of scientific advances that produce or contribute to the production of wind, solar energy, landfill gas, geothermal resources, ocean thermal energy conversion, tidal energy, wave energy, biomass, biofuels, or hydrogen fuels derived from renewable sources. Clean energy technology does not include: (A) the installation of clean energy technologies, (B) any fossil fuel based energy production, including but not limited to, clean coal, clean diesel, natural gas and hydrogen from natural gas, (C) any nuclear based energy production, (D) waste to energy via combustion or incineration, or (E) other technologies that are detrimental to human health.	"Clean technology" means the development, manufacture or application of scientific advances that a) produce or contribute to the production of or enable the use of clean energy, or b) result in quantifiable energy or water conservation, or c) result in greenhouse gas or toxics reductions, or d) make or enable carbon trading markets, including the verification of projects that produce carbon credits. Clean energy is defined as wind, solar energy, landfill gas, geothermal resources, ocean thermal energy conversion, tidal energy, wave energy, biomass, biofuels, or hydrogen fuels derived from renewable sources. Quantifiable energy or water conservation applications are defined as energy efficiency engineering and retrofit, energy storage devices for renewable energy, energy efficiency, electric vehicles and toxics reduction applications, "green" building materials as certified by LEED [Leadership in Energy and Environmental Design], technological developments for water conservation or purification, and enabling technology for the previously stated applications. Clean technology does not include: (A) general electrical contractors (B) any fossil fuel based energy production, including but not limited to, clean coal, clean diesel, natural gas and hydrogen from natural gas, (C) any nuclear based energy production, (D) waste to energy via combustion or incineration, or (E) other technologies that are detrimental to human health.

According to Mr. David Augustine, Policy and Programs Manager of the Office of the Treasurer and Tax Collector, the proposed definition of clean technology business as distinct from the current definition of clean energy technology businesses described above would result in more businesses becoming eligible to receive the Clean Technology Payroll Expense Tax exclusion. In addition, according to Mr. Augustine, the reduction of the minimum number of employees, to qualify for the Payroll Tax exclusion for businesses engaged in clean technology, from 10 employees, to one employee would also increase the number of qualifying businesses eligible for the Payroll Expense Tax exclusion for those businesses engaged in Clean Technology.

The Treasurer and Tax Collector is required to report to the Board of Supervisors each calendar year the amount of the businesses' payroll excluded from the City's Payroll Expense Tax liability for businesses engaged in clean technology which receive a Payroll Expense Tax exclusion.

Mr. Augustine reports that, for calendar year 2007, two businesses, with 31 total eligible employees, had a total payroll of $2,386,129 which was excluded from the City's Payroll Expense Tax . Based on the existing Payroll Expense Tax rate of 1.5 percent, the total Payroll Expense Tax exclusion granted to such Clean Technology businesses in 2007, which would have otherwise been paid to the City, was $35,792.

Mr. Augustine reports that the amount of the increase in the Payroll Expense Tax exclusions, due to the proposed reduction of the minimum number of employees, employed by businesses engaged in clean technology, from 10 to one, and the expansion of the definition of clean technology, as described above, cannot be estimated at this time.

Comment:

Currently, businesses with a Payroll Expense Tax liability of $2,500 or less annually (i.e., total business payroll of $166,667 are excluded from paying the City's Payroll Expense Tax. Proposition Q, approved by the voters in the November 4, 2008 election, increased the total annual payroll eligible for exclusion from $166,667 to $250,000 effective January 1, 2009, with CPI increases to the payroll threshold amount eligible for exclusion every two years.

The Controller has estimated that the increase in the number of businesses excluded from paying the City's Payroll Tax will result in an estimated decrease in Payroll Expense Tax revenues being paid to the City of $6.5 million annually, offset by increased Payroll Expense Tax revenues paid to the City of $17 million annually due to Proposition Q. If additional businesses become eligible for the clean technology Payroll Expense Tax exclusion, as a result of the proposed ordinance, such businesses may already be eligible, irrespective of whether or not the business is engaged in Clean Technology, because the total payroll of the businesses $250,000 or below.

Recommendation:

Approval of the proposed ordinance is a policy matter for the Board of Supervisors.