

**REPORT OF THE
CHIEF LEGISLATIVE ANALYST**

DATE: June 27, 2016

TO: Honorable Members of the Ad Hoc on Comprehensive Job Creation Plan Committee

FROM: Sharon M. Tso *KEY for*
Chief Legislative Analyst

Council File No: 15-0842
Assignment No: 16-06-0560

Additional Information: Business Regulations by State, County, and City

SUMMARY

On April 19, 2016, the Ad Hoc on Comprehensive Job Creation Plan Committee (Committee) considered a report from the Chief Legislative Analyst (CLA) concerning the current climate of business regulation in the City of Los Angeles relative to other cities nationwide. At the meeting, the CLA presented information from the U.S. Chamber of Commerce Foundation's Regulatory Climate Index (Index), which characterized business regulation in several areas. (See Attachment)

During the meeting, members of the Committee inquired about the origin of the above regulations in terms of level of government responsibility (city, county, and state), in order to help inform the City on areas of business regulation that are within the City's jurisdiction to reform. In order to respond to this request, our Office conducted an analysis on the areas of business regulation presented in the Index and separated regulations into areas that were controlled by the state, county, or city.

RECOMMENDATIONS

Note and file. For informational purposes.

BACKGROUND

Business regulations and rules present significant implications for businesses as they could place a disproportionate burden on small businesses due to the margins of capital required to run a small firm. As stated by Motion (Wesson – Price) on July 2, 2015, regulations naturally accumulate and layer on top of existing rules, at times creating duplicative and outdated rules in which businesses must comply. As stated by the Motion, compliance with regulations over time may shift how a company prioritizes existing time and resources. Shifting resources towards compliance could prevent companies from focusing on innovation and growth and it may make the City less attractive to businesses and less competitive relative to other local jurisdictions nationwide. Business regulations are also often enacted by other levels of government. As a result, it is important for the City to gain an understanding of the regulations that are within the City's jurisdiction to reform, as well as efforts required to address regulations at other levels of government.

DISCUSSION/FINDINGS

In our initial report, our office presented information from the Index, which analyzed business regulations of cities nationwide, and characterized them into five key areas: Starting a Business, Dealing with Construction Permits, Registering Property, Paying Taxes, and Enforcing Contracts. Although the Index was able to provide a comprehensive analysis of business regulation, it did not delineate regulations coming from different levels of government (city, county, and state) even though some of the cities from the study resided within the same state (Los Angeles and San Francisco). Below is an analysis of key areas of business regulation evaluated in the Index, with an analysis of the level of government in California responsible for regulating those functions.

1. **Starting a Small Business:** Starting a small business is primarily a *state* function that is complemented by the need to apply for an employer identification number (EIN) at the *federal* level. According to the Index, creating a formal business entity to provide professional business services is relatively simple and inexpensive in the State of California with costs of about \$70 and a wait time of 5 business days. In order to start a business, a company needs to formally reserve their business name, file their articles of organizations, and adopt the company's operating agreement with the Secretary of State. Following this, a business must also apply for their EIN for tax and employer purposes at the state and federal level.
2. **Dealing with Construction Permits:** Construction permits are primarily a *city* function. Obtaining the proper construction permits varies across cities in terms of costs, time, and required procedures. Differences across cities for obtaining construction permits include the zoning approval process, environmental reviews, and building permit reviews for both the pre- and post-construction phases. Approval of the zoning process and the obtaining of planning permits is heavily influenced by environmental reviews arising from the California Environmental Quality Act (CEQA), and as a result, is a *state* function. Approval for work permits from the Department of Building and Safety, on the other hand, are *city* functions. Work permits for construction include building, electrical, plumbing, mechanical, and grading permits. During the post-construction phase, on-site inspections are conducted by the Department of Building and Safety and the Department of Planning, which are *city* functions, to ensure that buildings are compliant with current building and zoning codes.
3. **Registering Property:** The registration of property is a process that ensures administrative compliance for commercial building transactions between businesses. The registration of property includes obtaining a title report, title transferring, and title recording. Obtaining a title report in the State of California involves requesting and obtaining a title report from the property's residing county, as well as purchasing title insurance policies. As a result, obtaining a title report in California is both a *county* and *state* function, as the county issues a title report to the requesting party in order to implement a requirement by state law. Title transferring involves the payment of a real estate transfer tax. A real estate transfer

tax in the State of California, also known as a Documentary Transfer Tax, imposes a fee of \$1.10 per \$1,000 of value for a property. Additionally, some counties and cities within California require additional fees as well. For example, Los Angeles requires a city fee of \$4.50 per \$1,000 of value and a county fee of \$1.10 per \$1,000 of value, whereas the City and County of San Francisco requires a fee that is based on a percentage of assessed value of a property. For cities and counties that do not have additional fees, the amount of the fee required is the State Documentary Transfer Tax. As a result, title transferring and the collection of a real estate transfer tax are *city*, *county*, and *state* functions, with respect to the amount of the fee charged by each level of government. Lastly, title recording, which involves public recordation with the County Recorder, is primarily a *county* function.

4. **Paying Taxes:** The number of payments and amounts of taxes vary across cities, and are based on state and local tax rates. Taxes include a corporate income tax, employment tax, operating tax, business tax, disability insurance, and state franchise tax. The corporate income tax, employment taxes (hospital insurance contributions and unemployment tax), disability insurance, and state franchise tax are taxes imposed by the *state*. An operating tax, such as a sales tax, have rates that are determined at the *city*, *county*, and *state* level. Lastly, the business license tax on professional services is a tax required at the *city* level.
5. **Enforcing Contracts:** The enforcement of contracts involves ensuring that business-to-business agreements are protected under the law through the local court system. Regulations with regard to the litigation and enforcement of judgments are both *state* and *county* functions. Although the California Superior Courts in each county are bodies governed by the Judicial Council of California at the *state* level, individual county courts from the Superior Court system are able to create local rules and regulations for its own government at the *county* level.

As stated in the Motion, business regulations and rules often create a burdensome system that make the City of Los Angeles less attractive to businesses and less competitive relative to other local jurisdictions. However, most rules and regulations surrounding businesses are outside the jurisdictions for reform by the City. The City may choose to further study areas of business regulation for reforms in those areas under its authority (i.e. permitting costs and streamlining, business taxes, real estate transfer taxes, etc) in order to make the City more attractive to businesses. Additionally, the City may also choose to pursue changes in legislation and administrative action at both the County and State levels of government on those areas outside its regulatory authority.

Our Office will continue to monitor legislation in both the State and Federal level with regards to policies or administrative actions impacting business regulations.

FISCAL IMPACT: No Fiscal Impact.



Steve Luu
Legislative Analyst

Attachment: Tables – Business Regulation Rankings from Regulatory Climate Index

Business Regulation Rankings from Regulatory Climate Index

Starting a Business								
	Procedures		Time		Cost		Average Score	Rank in Larger Analysis
	Number of Procedures	Score	Number of Days	Score	Cost	Score		
Los Angeles	4	100	5	96	\$70	100	98.8	1
San Francisco	4	100	5	96	\$70	100	98.8	1
Raleigh	5	67	5	96	\$155	93	85.4	6
Dallas	5	67	6	93	\$300	81	80.3	7
New York City	7	0	8	86	\$1,306	0	28.6	9

Dealing with Construction Permits								
	Procedures		Time		Cost		Average Score	Rank in Larger Analysis
	Number of Procedures	Score	Number of Days	Score	Cost	Score		
Raleigh	13	100	39	100	\$12,927	97	99.0	1
Dallas	14	83	49	93	\$9,900	100	92.1	2
New York City	15	67	79	72	\$32,060	77	72.2	5
Los Angeles	14	83	105	54	\$85,841	23	53.5	7
San Francisco	19	0	184	0	\$108,063	0	0.0	9

Registering Property								
	Procedures		Time		Cost		Average Score	Rank in Larger Analysis
	Number of Procedures	Score	Number of Days	Score	Cost	Score		
Dallas	4	100	7	100	\$19,763	93	97.6	2
Raleigh	5	67	8	67	\$13,391	96	76.6	4
Los Angeles	5	67	10	0	\$28,318	90	53.5	7
San Francisco	5	67	10	0	\$35,888	87	51	8
New York City	7	0	10	0	\$249,383	0	0	10

Paying Taxes						
	Procedures		Time		Average Score	Rank in Larger Analysis
	Taxes Paid	Score	Number of Payments	Score		
Dallas	\$174,210	100	28	100	100	1
Raleigh	\$198,510	76	33	50	63	3
New York City	\$219,024	56	33	50	52.9	6
San Francisco	\$255,337	20	38	0	10.1	9
Los Angeles	\$275,766	0	38	0	0.0	10

Enforcing Contracts								
	Procedures		Time		Cost		Average Score	Rank in Larger Analysis
	Number of Procedures	Score	Number of Days	Score	Cost	Score		
Dallas	20	60	180	89	\$325	82.2	77.1	4
San Francisco	23	0	205	83	\$500	56.3	46.4	6
Raleigh	22	20	313	54	\$470	60.7	44.9	7
Los Angeles	23	0	305	56	\$545	49.6	35.2	8
New York City	20	60	511	0	\$880	0	20.0	9