

GREPORT OF THE CHIEF LEGISLATIVE ANALYST

DATE: April 24, 2020

TO: Honorable Members of the Los Angeles City Council

FROM: Sharon M. Tso 
Chief Legislative Analyst

Council File No.	20-0147-S48
Assignment No.	20-03-0339

SUBJECT: Economic Relief for the Restaurant Industry

SUMMARY

On March 17, 2020, the City Council adopted Motion (Rodriguez-Lee; C.F. 20-0147-S48) which instructs this Office to report, with the assistance of the City Administrative Officer (CAO), on all economic relief programs made available to the restaurant industry at the federal, State, and County levels; and provide recommendations to fund a City program that can complement those programs and fill any gaps identified. The Motion also instructs the Office of Finance, with the assistance of the CAO, to report on the budgetary impact of a one-year gross receipts tax holiday for the restaurant industry. In a report dated March 26, 2020 (C.F. 20-0417-S48), the Office of Finance addresses the latter request, as does a report from the Chief Legislative Analyst (C.F. 20-0147-S19).

This report provides: 1) a discussion relative to federal, state and local funding resources available to the restaurant industry; 2) an analysis of a potential gross receipts tax holiday; and, 3) recommendations to fund a City program that can complement existing technical assistance programs for small businesses and fill any funding gaps. Attachment 1 to this report describes in more detail the type and amount of economic assistance available through all levels of government.

The COVID-19 pandemic is having a devastating impact on the U.S. economy, in particular on the restaurant industry. Approximately 8,000 businesses in the restaurant industry were registered with the City and paid a gross receipts tax for the 2019 tax year. For that year, full service and limited service restaurants generated \$7.6 billion in gross receipts, and cumulatively paid \$10 million in gross receipts tax. Pursuant to “stay at home” orders issued by Governor Newsom and Mayor Garcetti, restaurants were required to limit business transactions to take-out and delivery, thereby incurring severe financial losses. In response, federal, state and local public officials are mobilizing to mitigate the economic impact on businesses and their employees.

Through legislation and administrative action, governments have established funding programs to assist small businesses, including the restaurant industry. While these federal, State, and local programs provide relief for businesses, some microbusinesses may be at a disadvantage in accessing funds due to the complex application process for funding opportunities. Microbusinesses, such as “mom and pop” restaurants may encounter language, infrastructure, and technical challenges that could obstruct access to compete for available funds. As a result, the

overwhelming demand for assistance is limiting access to all eligible businesses due to insufficient funds and limited staffing to process requests.

The Economic and Workforce Development Department (EWDD) BusinessSource Centers currently provide technical assistance, including loan financing and business development. However, due to the COVID-19 pandemic, demand for services has dramatically increased. EWDD indicates that to complement existing programs and fill in gaps in service, additional staff positions and funding are required within the BusinessSource Centers to better respond to the demand for loan servicing and technical assistance. Based on a preliminary review, EWDD proposes additional staff positions for each of the nine centers.

To complement existing technical assistance programs and fill in the gaps in service, it is recommended that the Council instruct the CAO and the CLA to identify funds (federal, State, and local resources) for additional staff positions at each of the nine centers. With increased staff, EWDD would be better positioned to provide technical assistance to help “mom and pop” restaurants and other small businesses with language, infrastructure, and technical challenges to apply for funds. It is further recommended that the City Council instruct the CLA, with the assistance of EWDD and the CAO, to report on the resources necessary to address any additional funding and staffing gaps in service and funding sources, to further complement existing programs to assist small businesses, including the restaurant industry. Lastly, it is recommended that EWDD develop and implement an outreach and education program, and create a one-stop shop for the loan and grant application process for all funding resources related to the COVID-19 pandemic, in a timely and efficient manner.

RECOMMENDATIONS

That the City Council:

- 1) Authorize the CAO and the CLA, with the assistance of EWDD, to identify funds (federal State, and local resources) to supplement current technical assistance services to respond to increased demand for loans and grants as a result of the COVID-19 pandemic, and once funds have been identified, authorize EWDD to amend existing BusinessSource Center contracts.
- 2) Instruct EWDD, with the assistance of the CLA and the CAO to:
 - A) Report on any additional gaps in service and funding sources to further complement existing programs, and any additional staffing and budgetary needs necessary to assist small businesses, including the restaurant industry.
 - B) Implement an outreach and education program to increase access to federal, state and local funding opportunities, streamline the loan and grant application process for federal, State and local funding assistance programs, and provide technical assistance to local restaurants impacted by the COVID-19 pandemic.

DISCUSSION

The COVID-19 pandemic is having a critical impact on the U.S. economy, in particular on the restaurant industry. In response, federal, State, and local public officials are mobilizing to mitigate the economic impact on businesses and their employees.

The CARES Act, recently enacted by Congress and signed by the President, provides funding in the form of grants and loans to assist small businesses, including the restaurant industry. The CARES Act initially provided \$377 billion in loans and grants available through the Small Business Administration. Business entities wishing to apply for a loan may also apply for an emergency grant of up to \$10 million to assist with operating costs including payroll, rent and mortgage payments, and other costs. Additionally, this legislation provides business tax breaks and deductions to assist small businesses. It is noted that the majority of these funds have been depleted. However, on April 23, 2020, Congress approved a \$484 billion measure that provides additional money for small businesses.

This new bill contains approximately \$320 billion for the Paycheck Protection Program, including \$60 billion for businesses that do not have established business relationships, such as rural and minority-owned companies. An additional \$60 billion was included for the Small Business Administration's Economic Injury Disaster Loan Program.

The State has enacted a number of measures to assist small businesses with accessing federal assistance as well as creating pathways for those businesses who may not qualify for federal assistance. For example, the State has allocated \$50 million to the Small Business Finance Center at California's IBank to mitigate barriers to capital for those small businesses (1-750 employees) that may not qualify for federal funds including businesses in low-wealth and immigrant communities. Loan proceeds can be used for rent, payroll, and other operating costs. Information regarding the lenders issuing these loans had not been released at the time this report was prepared. Also, effective April 2, 2020, small business taxpayers with less than \$5 million in taxable annual sales, can apply for a 12-month, interest-free payment plan for up to \$50,000 of sales and use tax liability. Lastly, the State has provided a 90-day extension on all businesses filing a return for less than \$1 million in taxes.

The County of Los Angeles has established the LA County Employer Assistance Grant Fund to provide a total of \$500,000 to local businesses. Individual businesses may be awarded up to \$10,000 based on demonstrated need. Approximately 25 percent of awards will be reserved for social enterprises that demonstrate a need and ability to serve vulnerable populations. Applications will be processed on a first-come first-served basis, and will be closed once 150 applications are received.

Additionally, the County has established a local Paycheck Protection Program (County PPP), in partnership with the Goldman Sachs 10,000 Small Businesses initiative and Community Reinvestment Fund (CRF). The program provides to \$15 million in additional private capital to assist small businesses and nonprofits, with 500 or less employees per location, in the Los Angeles County region. The application portal will provide an opportunity for small businesses and nonprofits to apply for County PPP loans if they have been unsuccessful through traditional banking institutions. This program provides urgent cash flow assistance to small businesses that

have been negatively impacted by the COVID-19 pandemic. Proceeds can be used for payroll, rent, and utilities and will be partially or wholly forgiven for businesses that maintain or rehire their workforce. Reports indicate that Congress is considering an additional allocation of funds to the PPP, which would allow more businesses to receive assistance.

The City addresses some of the funding gaps not covered by federal and state funding programs through existing programs. EWDD provides assistance to small businesses in the form of microloans to businesses with less than 100 employees. EWDD is currently accepting applications. The EWDD BusinessSource Centers provide technical assistance and loan financing for small businesses. The City also provides a business tax exemption to all businesses with gross receipts under \$100,000. According to the Office of Finance, approximately 2,500 restaurant establishments did not pay a gross receipts tax for the 2019 tax year.

Gross Receipts Tax Holiday – Restaurant Industry

Motion (Rodriguez- et al., C.F. 20-0417-S48, Attachment 2) requests a report on the budget impact of issuing a gross receipts tax holiday for the restaurant industry. According to the Office of Finance, there are over 8,000 locations in the City that are registered with the City as Full Service or Limited Service Restaurants. These businesses combined generate \$7.6 billion in gross receipts and paid nearly \$10 million in gross receipts tax for 2019 to the City. Approximately one-third of these businesses do not currently pay a business tax pursuant to the City’s Small Business Tax Exemption (less than \$100,000 in gross receipts).

Establishing a gross receipts tax holiday for the restaurant industry will impact the General Fund and simultaneously impact existing services that the City provides. Gross receipts tax data for 2020 will not be available until after taxes are filed in 2021. It is anticipated that more restaurants experiencing economic hardship during 2020 as a result of the COVID-19 pandemic will qualify for the Small Business Tax Exemption. If the Council wishes to proceed with a business tax holiday for the restaurant industry, the City Administrative Officer, with the assistance of the Office of Finance, should be instructed to report with the fiscal impact of a one-year gross receipts tax holiday, once tax data is available for the year 2020. We note that the business tax paid to the City is proportional to the amount of gross receipts generated by each business. Therefore, the financial impact incurred by a restaurant business affected by the COVID-19 pandemic that results in a reduction of revenue, will also lead to a reduction in the business tax owed to the City.

Lastly, a CLA report dated April 10, 2020 (C.F. 20-0147-S19), addresses the issue of reducing or waiving gross receipts tax liability for all non-cannabis related businesses. The CLA notes that taxes for year 2019 have already been paid for the most part. Businesses that have not paid their 2019 gross receipts are delinquent. However, if the Council wishes to suspend assessment penalties and interest for any tax liabilities that have not yet been paid and/or are due during the months of March, April, May or June, 2020, for businesses impacted by the COVID-19 pandemic, restaurant businesses that have not paid their 2019 gross receipts taxes would be assisted.

BusinessSource Center Staffing Challenges

EWDD reports that one of the greatest challenges with loan underwriting is that many “mom and pop” restaurant owners lack the knowledge to prepare documents and forms required for loan applications. For example, some clients do not understand what a “profit and loss statement” is

nor how to develop one. This is not just a question of language barriers but of technical capacity. EWDD BusinessSource Centers, whose mission and purpose is to provide such type of technical assistance, are understaffed and underfunded to serve the increased demand for loan and technical assistance services. EWDD indicates that to complement existing programs and fill gaps in service, additional staff and funding are required within the BusinessSource Centers to better respond to the demand for loan servicing and technical assistance. EWDD indicates that at least one additional staff position is needed at each of the nine BusinessSource Centers to appropriately respond to the demand with respect to federal, State and local government business assistance.

FISCAL IMPACT

Approval of the recommendations included in this report will not result in a fiscal impact.

Felipe V Chavez - rg
Felipe Valladolid Chavez
Legislative Analyst

- Attachments: 1) Federal, State, and Local Resources for the Restaurant Industry
2) Motion (Rodriguez-Lee)

Federal, State and Local Resources for the Restaurant Industry

Restaurant Industry in the City of Los Angeles

State and local emergency “stay-at-home” orders and restrictions that limit restaurant activity to take-out and delivery have significantly impacted the restaurant industry. Restaurants in Los Angeles vary in size with respect to number of employees, gross receipts, and/or seating capacity. For the most part, loans and grants available through the CARES Act are limited to businesses with less than 500 employees. For the restaurant industry, which falls under NAICS code Sector 72 “Accommodation and Food Service,¹” a full service restaurant with gross receipts less than \$7.5 million and a Limited-Service restaurant with gross receipts less than \$11 million would qualify as a small business.

The Office of Finance reports that there are over 8,000 restaurant establishments in the City of Los Angeles which generate approximately \$7.6 billion in gross receipts. These businesses pay approximately \$10 million in gross receipts tax to the City annually. This includes full service restaurants defined as establishments primarily engaged in providing food services to patrons who order and are served while seated and pay after eating, and limited service restaurants defined as establishments primarily engaged in providing food services (except snack and nonalcoholic beverage bars) where patrons generally order or select items and pay before eating.

The Los Angeles County Public Health Department reports that there are currently over 12,000 restaurants in the City with County permits. Neither the Office of Finance nor the County Public Health Department measure the size of a restaurant based on number of employees. However, because the CARES Act allows major corporations with over 500 employees worldwide to use the number of employees in a single location to meet the threshold, those corporations will be competing with microbusinesses in accessing CARES Act business loans and grants.

Below is a brief description of the various types of loans, grants, and other resources available for the restaurant industry. It is noted that additional funding programs for small businesses, including the restaurant industry, are in the process of being developed at the federal, State and local government levels.

¹ SBA – Size Standards NAICS Sector 721 – Accommodation; NAICS Sector 722 – Food Services and Drinking Places

CARES ACT of 2020

On March 27, 2020, Congress passed the Coronavirus Aid, Relief and Economic Security Act 2020 (CARES Act) which provides \$2.3 Trillion intended to provide economic relief to businesses and individuals. There are seven main groups that would see the widest-reaching impact²:

<u>CARES ACT BY MAJOR AREA</u>	<u>FUNDING ALLOCATION</u>
• Individuals	\$550 Billion
• Big Corporations	\$510 Billion
• Small Business Loans & Grants	\$377 Billion
• Business Tax Relief	\$280 Billion
• Hospitals and Public Health	\$180 Billion
• State & Local Governments	\$150 Billion
• Transportation Industries	\$ 72 Billion
• Disaster Assistance	\$ 45 Billion
• Federal Safety Net	\$ 42 Billion
• Education	\$ 32 Billion
• Individual Tax Reduction & Other	\$ 45 Billion
• <u>Reduce Individual Taxes</u>	<u>\$ 20 Billion</u>
TOTAL	\$2.3 Trillion

The main features of the CARES Act for small businesses are emergency grants and a forgivable loan program for companies with 500 or fewer employees, in addition to small business concerns³. Small business concerns refers to the Small Business Administration industry-based “size standard” requirement for the applicable North American Industry Classification System (NAICS) code, which are based either on number of employees or annual receipts, if larger than 500 employees.

Restaurants, foodservice, caterers, and other food service establishments that employ not more than 500 employees per physical location of the business are eligible to receive a single loan if they operate under the NAICS code beginning with 72 (Accommodation and Food Services – U.S. Census Bureau). There are also changes to rules for expenses and deductions intended to make it easier for companies to keep employees on the payroll and stay open in the near-term. Below is a brief description of the various types of grants, loans, and tax breaks available to small businesses, including the restaurant industry, through the CARES Act.

Emergency Grants - \$10 Billion

The bill provides \$10 billion for grants of up to \$10,000 to provide emergency funds for small businesses to cover immediate operating costs. These grants provide for immediate relief within three days of submitting the application of up to \$10,000 for eligible entities. Such entities include small businesses, sole proprietors, private non-profits, independent contractors, cooperatives, and tribal units, all with under 500 employees. The funds may be used for providing paid sick leave for employees unable to work due to the direct effect of COVID-19, maintaining payroll to retain employees during the disruption, increased materials costs, rent or mortgage payments, and repaying obligations that cannot be met due to revenue losses.⁴

² Source Committee for a Responsible Federal Budget – March 25, 2020

³ Small Business Concerns refers to how the Small Business Administration defines a small business.

⁴ Source: The National Law Review April 2, 2020.

Forgivable Loans - \$350 Billion

There is \$350 billion allocated for the Small Business Administration to provide loans of up to \$10 million per business. Any portion of that loan used to maintain payroll, keep workers on the books or pay for rent, mortgage and existing debt could be forgiven, provided workers stay employed through the end of June. The amount forgiven will be reduced proportionally by any reduction in employees retained compared to the prior year and reduced by the reduction in pay of any employee beyond 25 percent of their prior year compensation.

To encourage employers to rehire any employees who have already been laid off due to the COVID-19 crisis, borrowers that re-hire workers previously laid off will not be penalized for having a reduced payroll at the beginning of the period.

Paycheck Protection Program

The plan provides \$349 billion in cash flow assistance through 100 percent federally guaranteed loans to small businesses and 501(c)(3) nonprofit organizations during this emergency. This program can be retroactive to February 15, 2020, so employees can return onto payrolls. The loan's covered period is February 15 to June 30, 2020. The expected forgiveness amount can be expended on payroll costs, payments of interest on a mortgage obligation, rent obligations, and utility payments. Employers may apply for loans of up to \$10 million (formula tied to payroll costs) – and can cover employees earning up to \$100,000 or less per year. These loans may be forgiven if a firm uses the loan for payroll, interest payments on mortgages rent, and utilities, and would be reduced proportionally by any reduction in employees retained compared to the prior year.

Relief for Existing Loans

There is \$17 billion to cover six months of payments for small businesses already using SBA loans. The measure stipulates that small businesses would not have to make payment on those loans for up to six months.

Other Benefits

Qualified Improvement Property (QIP)

Businesses will be able to immediately write off costs associated with improving facilities instead of having to depreciate those improvements over the 39-year life of the building. This corrects the error in the Tax Cuts and Jobs Act and increases a business' access to cash flow by allowing them to amend a prior year's return, while incentivizing investment.

Employee Retention Tax Credit

The Employee Retention Tax Credit is a fully refundable tax credit for employers equal to 50 percent of qualified wages that eligible employers pay their employees. This tax credit applies to qualified wages paid after March 12, 2020, and before January 21, 2021. The maximum credit per employee is \$5,000.

The credit is available to employers whose operations were fully or partially suspended, due to a coronavirus-related shut-down order, or gross receipts declined by more than 50% when compared to the same quarter in the prior year.

Employer Social Security Payroll Tax Delay

Employers can defer payment of the employer share of the Social Security tax. The deferred employment tax can be paid over the following two years, with half of the amount required to be paid by December 31, 2021 and the other half by December 31, 2022.

Net Operating Losses (NOLs)

The provision relaxes limitations on a company's use of losses from prior years. NOLs are currently subject to a taxable income limitation, and they cannot be carried back to reduce income in a prior tax year. This provision provides that a loss from 2018, 2019, or 2020 can be carried back five years. This also temporarily removes the taxable income limitation to allow an NOL to fully offset income.

Resources for State and Local Governments

The legislation provides \$150 billion to state, tribal, and local governments. Funding to States will be available based on population. States like California and Texas will receive over \$10 billion each to meet costs related to COVID-19. According to the Center for Budget and Policy Priorities, it is anticipated that California will receive approximately \$15 billion.⁵ In most States, a portion of the funding will go to local governments serving populations over 500,000. Local governments are permitted to claim 45 percent of the amount allocated for their population, while the State retains the other 55 percent as it also serves that population. The State also retains 100 percent of the amount allocated to populations within a locality of 500,000 or more. The U.S. Treasury Department is charged with determining overlapping populations such as cities and counties. Of the anticipated \$15 billion for California, approximately \$1.8 billion would be the share for Los Angeles County.

⁵ Center on Budget and Policy Priorities – March 26, 2020

State of California Programs

The State of California also has several programs that restaurants will be able to access.

Capital and Technical Assistance Resources

California IBank has a Small Business Loan Guarantee Program for up to \$1 million and a micro lending program for loans up to \$10,000 with accommodations for disasters. The program is run through local mission-based lenders, the Financial Development Corporations: Small Business Finance Center.

California State Treasurer's Office

California Capital Access Program (CalCap)(1-500 employees) is a loan loss reserve program which may provide up to 100 percent coverage on losses as a result of certain loan defaults. Borrowers are limited to a maximum of \$2.5 million enrolled over a 3-year period. To qualify, the primary business and at least 51 percent of the employees or its income, sales, or payroll comes from business in California. Business activity resulting from the bank's loan must be created and retained in California. Eligible uses of this loan include land acquisition, construction or renovation, start-up costs, equipment or inventory purchases, capital projects, and working capital.

California Small Business Finance Center

The SBFC helps business create and retain jobs, and encourages investment in low- to moderate- income communities. The SBFC has the Jump Start Loan Program, a Small Business Loan Guarantee Program, and Farm Loan Program. Businesses and nonprofits located in California with 1-750 employees that have been negatively impacted or experienced disruption by COVID-19 may qualify. Loan proceeds may be used for rent, payroll, and other costs.

California Department of Tax and Fee Administration

A 90-day extension on all businesses filing a return for less than \$1 million in taxes has been issued. Interested businesses with qualifying sales and use taxpayers with deferred liabilities up to \$50,000 can pay their tax due in 12 equal monthly installments. No interest or penalties will be assessed against the liability.

Los Angeles County Employer Assistance Program

On April 7, 2020, the Los Angeles County opened its application process for the County's Employer Assistance Program which offers up to \$10,000 to small businesses facing economic hardship as a result of the COVID-19 pandemic.

City of Los Angeles Programs

The City of Los Angeles offers a number of programs to assist the restaurant industry.

BusinessSource Centers

The Economic and Workforce Development Department provide technical assistance, capacity building, financing and loan qualification, and other business resources to small and microbusinesses in the City through its nine locations.

Small Business Emergency Microloan Program

The City of Los Angeles has established the Small Business Emergency Microloan Program which provides financing needed to strengthen small business enterprises that have been impacted by the COVID-19 outbreak. The loan amounts range from \$5,000 to \$20,000 for up to a five year term. All fees associated with acquiring the loan have been waived and funds may only be used as working capital. Eligible borrowers include for-profit and tax-exempt businesses in the City with fewer than 100 employees that have been negatively impacted by COVID-19. Primary business operation must be in a commercial-use building within the City.

Small Business Tax Exemption

The City of Los Angeles currently offers a gross receipts tax exemption to businesses with less than \$100,000 in gross receipts. A March 26, 2020, Office of Finance report indicates that for calendar year 2019, 1,673 full service restaurants and 876 limited service restaurants reported gross receipts below \$100,000. The combined estimated business tax credit for this industry in 2019 is approximately \$53,000.

Restaurant and Hospitality Express Program

The Restaurant and Hospitality Express Program, offered by the Department of Building and Safety, facilitates the approval process for food service establishments, such as restaurants and bars. The program helps to streamline approvals, provide assistance, design and construction teams, and enhance coordination in permitting and regulations.

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MOTION

The novel coronavirus (COVID-19) is devastating the food services and drinking places industry. Governor Gavin Newsom and Mayor Eric Garcetti have ordered all bars and restaurants to close (with the exception of those who provide delivery and pick up services). Though these closures are critical in mitigating the spread of the coronavirus and ensuring the public health of Angelenos, many restaurants in the industry are small, family-owned enterprises that do not have the financial capacity to withstand long term closures. The impact of these closures will ripple through communities in Los Angeles as many working Angelenos rely on these jobs to support their families. As relief programs are considered at the Federal, State, and County levels, the restaurant industry should be prioritized in receiving economic support. Moreover, the City should explore opportunities to provide financial relief that complement any State and Federal programs that are made available.

I THEREFORE MOVE that the Chief Legislative Analyst, with the assistance of the City Administrative Officer, be directed to report on all economic relief programs made available to the restaurant industry at the Federal, State, and County levels, and to provide recommendations to fund a City program that can compliment those programs and fill any gaps identified.

I FURTHER MOVE that the Office of Finance, with the assistance of the City Administrative Officer, be directed to report on budgetary impacts of a one year gross receipts tax holiday for the restaurant industry.

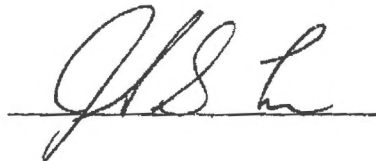
PRESENTED BY:



MONICA RODRIGUEZ
Councilwoman, 7th District

ORIGINAL

SECONDED BY:



MAR 17 2020



(SEE COUNCIL FILE NO. 20-0147-S48)