

**REPORT OF THE
CHIEF LEGISLATIVE ANALYST**

DATE: April 18, 2016

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

FROM: Sharon M. Tso 
Chief Legislative Analyst

Council File No: 15-0842
Assignment No: 16-04-0294

SUBJECT: Study on the Regulatory Climate of Various Cities

Summary:

On July 2, 2015, Motion (Wesson – Price) was introduced, which highlighted the unintended but significant costs of local regulations on business and economic growth (CF: 15-0842). The significant implications for businesses, in terms of regulations and rules, could place a disproportionate burden on small businesses due to the margins of capital to run a small firm, creating a “compliance burden.” As stated by the Motion, regulations naturally accumulate and layer on top of existing rules, at times resulting in duplicative and outdated rules with which the business community must comply. Although regulations are a necessity for facilitating economic activity and enabling a fair business environment, current regulatory environments are often cumbersome and confusing, creating a continual need for refined regulations that are simple and expedient for businesses.

As stated by the Motion, accumulation of regulations over time affects how a company allocates existing time and resources. At times, this results in the shifting of attention and priorities towards compliance, and could prevent companies from focusing on innovation and growth. In addition, an overabundance of compliance and regulations may make the City less competitive compared to other local jurisdictions nationwide. As a result, the Motion was introduced in order to allow for the City Council as policymakers to improve the current business climate by retrospectively reviewing current regulations, and cultivate a less cumbersome regulatory environment.

To begin evaluating the City’s current regulatory environment, we have reviewed information obtained from the U.S. Chamber of Commerce Foundation’s Regulatory Climate Index (2014) of local jurisdictions’ regulatory environments including the regulations of the City of Los Angeles. In analyzing the regulations of other cities, this information will serve as a platform to help initiate discussion on the review of current regulatory codes pertaining to the current climate surrounding business development, recruitment, and retention in the City of Los Angeles, and as requested by Motion (Wesson – Price), focus on:

1. Existing regulations using a formal process to analyze the current regulatory code and develop reform proposals
2. Search for regulations that create redundancy and/or contradict

3. Reducing compliance costs
4. Encouraging innovation
5. Fostering growth
6. Protecting public health and safety
7. Improving competitiveness

The final report will review this and other studies, as well as updates to information that may be available.

Summary of Results:

The following is an analysis of the Regulatory Climate Index (2014) by the U.S. Chamber of Commerce Foundation, which analyzes the regulatory climate of 10 cities nationwide and are as follows: Dallas, St. Louis, Raleigh, Boston, Atlanta, Detroit, Chicago, Los Angeles, San Francisco, and New York City. The 10 cities that were selected represent a wide range of economic and demographic backgrounds of small and large cities from across the region. For the purposes of this report, in order to make a comparison relative to the regulatory climate of Los Angeles, the four other cities that were selected represent the cities considered to be among the least burdensome to small businesses (Dallas, TX and Raleigh, NC) to the most burdensome (San Francisco, CA and New York City, NY). According to the Regulatory Climate Index, the City of Los Angeles is considered to have one of the most burdensome regulatory environments. However, the City in 2014, outperformed the other two large metropolitan cities in this report. To effectively improve the regulatory environment of Los Angeles, the City can learn from the best practices of other jurisdictions that are considered to be the most competitive and adapt to the lessons learned from business regulation.

Although there are sizable variations in the cities selected, it is important to keep in mind that this analysis evaluates the administrative procedures of several areas of business regulation, and that the business climate may have changed since the study was conducted. However, this study is useful for evaluating regulatory environments as it provides a snapshot of other cities. The scores that are given to each city are calculated through the simple average of scores from five areas of business regulation: starting a business, processing of construction permits, registration of property, payment of taxes, and enforcement of contracts. The average scores for the regulatory climate of a city is ranked relative to other cities represented within the study.

City	Average Score	Ranking
Dallas	89.5	1
Raleigh	73.7	3
Los Angeles	47.9	8
San Francisco	41.3	9
New York City	34.7	10

The scores for each area of business regulation are calculated by averaging the normalized values associated with the following three areas: the number of procedures, number of days, and the costs

associated with each regulation. The three areas associated with each business regulation, relative to each individual city, are normalized with respect to the maximum and minimum values of the 10 cities from the Regulatory Climate Index. The assumptions used for the evaluation of each area of business regulation are included within Attachment 1 (Assumptions) of this report.

Starting a Business:

Los Angeles and San Francisco are both tied for the top ranking position for starting a business. Starting a business in both cities is relatively easy compared to other cities in the analysis as it takes the lowest number of procedures, requires the lowest amount of time, and has the least amount of administrative costs of the 10 cities that were part of the study. Differences in the average scores associated with starting a business in Raleigh, Dallas, and New York City are a result of more procedures and higher costs associated with respect to each city. New York City has proven to be the most difficult environment to start a business as it requires businesses to post two advertisements for six consecutive weeks in local newspapers and \$1,306 in administrative costs to register and start a business, creating a burden for small businesses.

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

Processing Construction Permits:

The two cities that have demonstrated to be the most accessible and efficient with regard to processing construction permits (pre- and post-construction phases) are Raleigh and Dallas. Both achieve the best performance in terms of costs of permits, minimal procedures, and waiting times. Dallas has a streamlined permitting and licensing process that is expedited as businesses apply and attain construction permits. Raleigh, the top ranking performer in construction permits, also has an expedited process for applying and receiving construction permits, and outranks Dallas due to its lower procedures and processing times.

The cities of Los Angeles and San Francisco have demonstrated to be the most difficult for processing construction permits. Los Angeles and San Francisco’s lower ranking are a result of the unique regulatory environments of the State of California. Due to State law, both cities are subject to zoning and environmental reviews (i.e. CEQA), which contribute to the long processing times. In addition to this, Los Angeles and San Francisco have higher costs for permits, which

represent nearly 3 percent of total cost of construction. More specifically, Los Angeles has higher costs due to fees associated with building permit plan and approval fees as well as the arts development fees.

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:

Another area of business regulation that is integral for this analysis is the registration of property, which occurs during commercial building transactions between businesses. A distinct feature that makes Dallas the top performer in the category of registration of property is its absence of a real estate transfer tax both at the state and local levels. This significantly lowers transactional costs for small businesses. Raleigh also ranks higher amongst the other cities in terms of the registration of property. Similarly to Dallas, Raleigh has higher procedural efficiency and lower waiting times when transferring property in a commercial sale. A distinguishing factor of Raleigh is its lower administrative cost, which is the lowest amongst the 10 cities from the analysis.

In contrast, although Los Angeles is third amongst the cities sampled in the following table, in the larger analysis of the 10 cities from the study, Los Angeles ranks near the bottom. This is a result of the higher waiting times and administrative costs for transferring commercial real estate. In comparison to the higher ranked cities, Los Angeles has a higher real estate transfer tax that places an additional burden on small businesses and raises the transactional costs. In contrast, New York City, of the 10 cities that were part of the study, has the highest cost for the registration of property due to their real estate transfer and real property tax, as well as their mortgage recordation tax.

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:

Of the cities studied from the larger analysis, the city of Dallas is identified as the most business friendly due in significant part to its lower taxes. Dallas, and cities within the state of Texas in general, have a lower employment tax and no corporate income tax. The absence of some taxes and minimal charge for other taxes helps to significantly reduce the tax burden on entrepreneurs and small businesses, creating an attractive regulatory environment for investment. Similarly, Raleigh has a friendly tax code and a decreased tax burden, with a moderate corporate income tax of 6 percent and low employment and sales taxes.

In contrast, the City of Los Angeles has among the highest taxes for business owners of the 10 cities that were part of the study. Of the cities covered in this report, small businesses in the City of Los Angeles face the most burdensome tax system, as small companies face higher corporate tax rates, higher sales tax rates, and additional regulations. At the time of the U.S. Chamber of Commerce Foundation’s study (2014), Los Angeles required a business tax of 5.07 percent per \$1,000 on gross receipts greater than \$100,000 for professional services companies. As of 2016, the business tax on professional services companies is 4.75 percent per \$1,000 on gross receipts over \$100,000. Due to this decrease in the business tax, the City of Los Angeles may have an adjusted ranking within a future update of the Regulatory Climate Index in this area of business regulation. Businesses in Los Angeles, as well as San Francisco, are also required to pay 1 percent of state disability insurance per employee per year.

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:

The enforcement of contracts within a local jurisdiction’s court system is an important aspect of regulation for business owners as it ensures that business agreements are protected under the law. The most integral aspects in the enforcement of contracts are the time and costs required by courts, as they provide an indicator for the maintenance and protection of cities’ business environments. The wide variations in the enforcement of contracts throughout the analysis is a result of the total waiting times for steps in the administrative process. In the larger analysis, with regards to the 10

cities studied, Dallas is ranked 4th in the enforcement of contracts. Dallas falls short relative to the higher ranked cities due to the higher volume of procedures that are required to enforce a contractual agreement.

Of the 10 cities that were part of the study, the lowest ranked cities in the enforcement of contracts are Los Angeles and New York City. Both of these cities are subject to a higher number of procedures for enforcing contracts. The most significant factor that contributes to their low rankings are waiting times and administrative costs. For the enforcement of a contract in Los Angeles and New York City, businesses could expect to wait more than a year to settle a dispute through the litigation phase. In New York City, a business owner could wait over a year and a half to settle a contractual dispute.

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

CLA Recommendation: Note and file.

Fiscal Impact: None.



Steve Luu
Analyst

Attachment 1: Table – Assumptions to Construct the Regulatory Climate Index
Attachment 2: Motion (Wesson – Price)

Attachment:

Table 1.
Assumptions to Construct the Regulatory Climate Index

Areas of Regulation	Assumptions	Simple Average of the Component Scores
Starting a Business	The business entity is a limited liability company (LLC) with more than one owner that provides professional services; the LLC has \$4 million annual revenues and employs 20 workers; the LLC is not qualified for any special economic assistance.	33% procedures 33% time 33% required fees
Dealing with Construction Permits	A local construction company, with less than \$33.5 million annual revenues, builds a 3-story, 15,000-square-foot commercial office; the total construction costs are \$3,000,000; the new professional building is not located in a special economic zone and does not need additional special permits, such as historical zone and wetlands; the construction project is assumed to be free from environmental issues.	33% procedures 33% time 33% required fees
Registering Property	Buyers and sellers are local LLCs; the property is a new commercial building of 3 stories, 15,000 square feet; the property sells for \$4,000,000; the deed of the property is 15 pages long; the new professional building is not located in a special economic zone, and the professional building does not require any additional special permits or certifications.	33% procedures 33% time 33% required fees
Paying Taxes	The company provides professional services (e.g., accountant and IT services); the company has \$4 million annual revenues; profits are 15% of \$4 million revenue (\$600,000); the company employs 20 workers (half are singles and half are married); the labor share is 20% of revenues (\$800,000); the company is not qualified for any special economic assistance.	50% number of payments per year 50% the amount of tax paid
Enforcing Contracts	Plaintiffs and defendants are local LLCs doing business and based in the same city; plaintiffs request and obtain attachment of defendants' movable assets; the value of dispute is \$1 million; the lawsuit is brought in the lowest court in the state system with jurisdiction for the claim; professional fees for lawyers and expert witnesses are not included; only interactions mandated between the court, the plaintiff, and the defendant count as a procedure; communication from the court to parties counts as a procedure only if it requires parties to comply.	33% procedures 33% time 33% required fees

MOTION ECONOMIC DEVELOPMENT

The natural accumulation of local regulations over time imposes an unintended but significant cost to business and economic growth. Regulations naturally accumulate and layer on top of existing rules, sometimes resulting in a maze of duplicative and outdated rules the business community must comply with. However, no effective process currently exists for retrospectively improving or removing regulations. It is important for the City Council as policymakers, to carefully lower unforeseen obstacles to innovation and growth imposed by past regulatory measures.

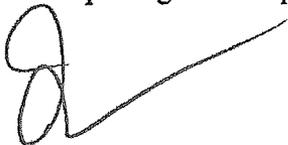
Our current regulatory approval process is focused on individual regulations. But regulations are hardly ever applied individually as a discrete entity – once approved, they are added to the list of regulations companies must already comply with. As the number of approved regulations grows, they inevitably interact in ways we may not expect. And when taken together, multiple regulations can overlap or conflict, and can interfere with a company's willingness and ability to innovate.

The accumulation of regulations over time affects how company management allocates their time and resources. After a certain point, a company will shift its attention and priority toward compliance with rules, and away from innovation or company growth. As the regulatory code grows, people are more likely to make mistakes and are often less motivated to comply. Too many regulations can actually have the opposite effect of what the regulation was intended to accomplish, because excessive regulations hamper a company's ability to operate effectively.

The City of Los Angeles needs to improve the current business climate in order to cultivate an environment that promotes job creation and innovation. The City can take steps to create a less cumbersome environment in which to operate a business if it were to retrospectively review current regulations in order to explore the possibility of crafting a regulatory policy that imposes as few burdens as possible, without compromising innovation, public safety and worker protections.

The City should be guided by a set of regulatory principles that serve as a basis for future actions:

1. Regulations should be used only as a tool to achieve a policy objective as a last resort; the use of regulations indicates the failure of other means to achieve the objective;
2. The cost of a regulation should be no greater than the value of the benefit created for the community;
3. Regulations must be written to ensure the imposition of the minimum possible constraints upon the community;
4. Regulations must be simple, fair and enforceable;
5. The regulation should clearly benefit the consumer or the public;
6. The regulation should complement other laws and rules; and,
7. Local regulations should not exceed federal and state standards unless there is a compelling and uniquely local reason.



WE THEREFORE MOVE, to instruct the Chief Legislative Analyst (CLA), the City Administrative Officer (CAO), in coordination with the City Attorney and other relevant city agencies, to be guided by the principles stated above and report back on the current regulatory code as it pertains to the current climate surrounding business development, recruitment and retention in the City of Los Angeles with a focus on:

1. Existing regulations using a formal process to analyze the current regulatory code and develop reform proposals
2. Search for regulations that create redundancy and/or contradict
3. Reducing compliance costs
4. Encouraging innovation
5. Fostering growth
6. Protecting public health and safety
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WE FURTHER MOVE, that the CLA and CAO, and other relevant city agencies, report back on the development of innovative and developing “shared economy” or “on-demand” business models, to ensure that the City’s current regulations keep pace with new ways of doing things, and to ensure that the City of Los Angeles is at the forefront of the development of new and innovative 21st century business models.

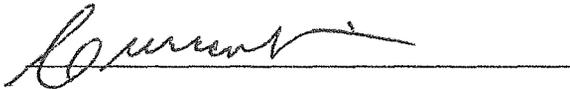
WE FURTHER MOVE, that the CLA and CAO, and other relevant city agencies, conduct a cost benefit analysis on current regulations that affect the areas listed above.

**PRESENTED
BY**



HERB J. WESSON, JR.
Councilmember, 10th District

**SECONDED
BY**



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JUL 1 2015