

The Time to Consider San Francisco Gross Receipts Tax Refund Claims is Now

By Michael J. Cataldo

The San Francisco Gross Receipts Tax (GRT) incorporates provisions of both the federal income tax and the California income and franchise tax. Taxpayers should review their federal and California tax reporting that may impact GRT liability, and consider filing GRT refund claims before the expiration of the one-year statute of limitations.

San Francisco (the City) GRT returns and full payment of tax are due by the last day of February of the following year—months before federal and California income tax returns are typically filed.¹ Since gross receipts subject to the GRT include “all amounts that constitute gross income for federal income tax purposes,”² many taxpayers may have estimated their federal gross income in order to timely file GRT returns. Some taxpayers may have overpaid the GRT if they overestimated federal gross income on their GRT returns, and should consider filing GRT refund claims before the one-year statute of limitations on such claims expires.³ For timely 2014 GRT payments, that date is **February 29, 2016**.⁴

During 2015, the City added section 6.15-1(g), which provides taxpayers an alternative to filing refund claims, instead allowing taxpayers to submit a request for refund within the same one-year period applicable to refund claims. While both refund claims and requests for refund must be submitted within this one-year period, any action on a refund claim must be made by the City Attorney who must secure Board of Supervisor approval for any claim over \$25,000.⁵ In contrast, a request for refund may be approved by

¹ Section 6.9-1(b); 6.9-2(a). Unless otherwise noted, all citations are to the San Francisco Business and Tax Regulations Code (“Code”). GRT returns are due annually on the last day of February of the following year, and there are no automatic extensions of time to file GRT returns. An extension is only permitted if good cause is shown, and even then, is limited to 60 days. (See Section 6.9-4(a).) Taxpayers may request a 60-day extension of time to file their 2015 GRT returns by submitting an extension request and remitting payment of at least 90 percent of their 2015 City business tax liability by February 29, 2016. Such extension requests may be submitted online at the following link: <http://sftreasurer.org/ExtensionRequest2015>

² Section 952.3(a).

³ Section 6.15-1(a) requires refund claims to be filed within the later of one year of: (1) the alleged overpayment; (2) the date the return accompanying such payment was due; or (3) the date on which such amount requested on an amended return or request for refund timely filed under section 6.15-1(g) was denied under that subsection (g).

⁴ Timely 2014 GRT returns and payments were due February 28, 2015. Since February 28, 2016 is a Sunday, refund claims for such payments may be filed by the following business day—February 29, 2016. See Section 6.2-8.

⁵ Section 6.15-1(e).

the City Tax Collector without the involvement of the City Attorney.⁶ If the City Tax Collector denies a taxpayer's request for refund, the taxpayer may timely file a claim for refund within one year of such denial.⁷

Securing refunds of overpaid GRT as a result of overestimating federal gross income may well be an ongoing issue for many GRT taxpayers. This is so not only because of the early due date of the GRT return, but also because of subsequent changes to the amount of federal gross income originally reported to the Internal Revenue Service (IRS)—whether those changes are initiated by the taxpayer via an amended federal income tax return, or by the IRS via audit adjustments.⁸ After the expiration of the one-year statute of limitations for GRT refunds, such taxpayers would be foreclosed from securing a refund of overpaid GRT resulting from over-reported federal gross income on GRT returns.

Unfortunately, this door does not swing both ways. In contrast to the one-year statute of limitations on refunds, the City has three years after the later of the date the GRT return was due or filed to assess additional GRT.⁹ Thus, if the amount of federal gross income originally reported to the IRS (and for GRT purposes) is subsequently increased, the City may assess additional GRT based on the increased federal gross income, so long as the assessment is made within the three-year statutory period applicable to assessments.

These uneven statutory periods for refunds and assessments can work great hardships on taxpayers. For example, if a certain item of federal gross income which was originally included for GRT and federal income tax purposes in Year 1 is subsequently moved to Year 2 as a result of a federal income tax adjustment initiated by either the taxpayer or the IRS, the impact may be minimal from a federal income tax perspective, however the results for GRT purposes could be significant. The City may assess additional GRT as a result of increased federal gross income in Year 2 if the assessment is made within the three-year statutory period for assessments, but the taxpayer may be foreclosed from securing a refund of overpaid GRT in Year 1. In this instance, the taxpayer could be subject to the GRT on the same item of federal gross income in both Year 1 and Year 2 simply as a result of an adjustment to federal gross income.

Similar GRT issues may arise due to reporting of California income and franchise tax. For example, GRT returns must be filed on a combined basis, with all related entities.¹⁰ Related entities for these purposes are defined to include those that are permitted or required by the Franchise Tax Board to have their income reflected on the same combined report for California income and franchise tax purposes.¹¹ Taxpayers that file GRT returns on a combined basis should review their California combined returns to compare the members included in the California combined group with those included in the GRT combined return.¹² Inconsistencies between the group composition of the California and GRT returns may result in

⁶ Section 6.15-1(g).

⁷ The City Tax Collector is deemed to have denied the request for refund if it has not acted on it within one year from the date it was filed. Note, however, that if the City Tax Collector denies a request for refund more than one year after it is filed, the one-year statute of limitations for filing a refund claim starts on the date the refund request is deemed denied, not the date the City Tax Collector actually denies the request for refund. See Section 6.15-1(g).

⁸ States generally extend the statute of limitations for refunds and assessments when there is a change to federal income tax that impacts the state tax. The GRT contains no similar provisions.

⁹ Section 6.11-2(a). Note that unlike most states, the City does not require taxpayers to report any changes to their federal income tax and extend the statute of limitations for assessments based on when those changes are reported.

¹⁰ Section 956.3.

¹¹ Section 952.5.

¹² Many taxpayers file their original California combined income/franchise tax returns conservatively by including or excluding certain members from the combined group for which there may be a basis to do otherwise, then file amended returns changing the group composition—all to avoid the possible imposition of California's large corporate understatement penalty

overpayment of the GRT for which refunds may only be granted before the expiration of the one-year statute of limitations.¹³

Additionally, some of the rules for sourcing gross receipts within and without the City are identical to the rules used to source receipts for California income and franchise tax sales factor purposes. For example, both the City and California source receipts from services to where the purchaser of the services received the benefit of the services,¹⁴ and receipts from intangible personal property to where the property is used.¹⁵ Adjustments to the sourcing of such receipts for California income and franchise tax sales factor purposes may result in overpaid GRT which may only be recovered by claiming a refund within the one-year statute of limitations.¹⁶

The magnitude of these issues will only increase as the GRT continues to be phased-in.¹⁷ Taxpayers should consider calendaring a review of their GRT filings at least annually before the expiration of the one-year statute of limitations. Since federal and California income tax adjustments that impact the GRT are often not made until well after the expiration of the one-year statute of limitations on GRT refunds, taxpayers should consider filing protective GRT refund claims when such adjustments are anticipated, even if they are not final.

The information presented is only of a general nature, intended simply as background material, is current only as of its indicated date, omits many details and special rules, and accordingly cannot be regarded as legal or tax advice.

■ (“LCUP”). Taxpayers doing so should consider the impact of such amendments to the California combined group on their combined GRT returns. See our Client Alerts dated [October 8, 2015](#), [May 4, 2009](#), [March 10, 2009](#), and [December 10, 2008](#), for a discussion of the LCUP.

¹³ A California combined reporting group will not necessarily be the same as a GRT combined group. For example, only corporations are permitted to be included in a California combined return, whereas partnerships, limited liability companies and other entities—as well as corporations may be included in a GRT combined group. See our Client Alerts dated [March 2, 2015](#), and [April 29, 2014](#), for a detailed discussion of the GRT, including combined GRT reporting issues.

¹⁴ Compare Section 956.1(e) to California Revenue and Taxation Code section 25136(a)(1).

¹⁵ Compare Section 956.1(f) to California Revenue and Taxation Code section 25136(a)(2).

¹⁶ Many taxpayers file their original California returns applying these sourcing rules conservatively, then reverse these conservative positions on amended returns to avoid the possible imposition of the LCUP. Taxpayers doing so should consider the impact of such amendments on their GRT returns.

¹⁷ The GRT is being phased-in over a 5-year period beginning in 2014. (See Section 959.) In 2014, only 10 percent of the maximum rates authorized by the GRT will apply, and the Payroll Expense Tax rate from the preceding year will be reduced by 10 percent. For 2015 -2017, roughly 25 percent, 50 percent, and 75 percent of the maximum GRT rates will apply, respectively, with corresponding reductions to the Payroll Expense Tax rates. By 2018, it is estimated that the GRT will completely replace the Payroll Expense Tax. The above phase-in percentages are targets subject to adjustment by the City Controller, depending on the amount of tax revenue generated by the GRT.

If you have any questions about the content of this alert, please contact one of the authors, the Pillsbury attorney with whom you regularly work, or one of the attorneys below.

Michael J. Cataldo [\(bio\)](#)
San Francisco
+1.415.983.1954
michael.cataldo@pillsburylaw.com

Jeffrey M. Vesely [\(bio\)](#)
San Francisco
+1.415.983.1075
jeffrey.vesely@pillsburylaw.com

Kerne H. O. Matsubara [\(bio\)](#)
San Francisco
+1.415.983.1233
kerne.matsubara@pillsburylaw.com

Annie H. Huang [\(bio\)](#)
San Francisco
+1.415.983.1979
annie.huang@pillsburylaw.com

Richard E. Nielsen [\(bio\)](#)
San Francisco
+1.415.983.1964
richard.nielsen@pillsburylaw.com

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