

City of Newport Beach

A Review of Business License Tax Requirements for Real Estate Agents



Overview

➤ Background

- City Code Requirements
- Business License Tax Rates and Revenue

➤ What factors do we consider to determine if Real Estate Agents are subject to Business License Taxation?

- Are we compliant with Federal and State legal standards?
- Is our treatment of the real estate industry consistent with the treatment of other industries that employ independent contractors?

Background

NBMC Code Requirements

- Any person who operates a business in the City must obtain a business license (NBMC §5.04.020).
- “Person” shall mean ... individuals transacting and carrying on any business in the city **other than as an employee** (NBMC §5.04.010).
- “Business” shall mean arts, professions, trades and occupations in all and every kind of calling, whether or not carried on for profit (NBMC §5.04.010).

Employees are not required to obtain business licenses.

Business License Tax Rates and Associated Revenue from Real Estate Agents and Brokers

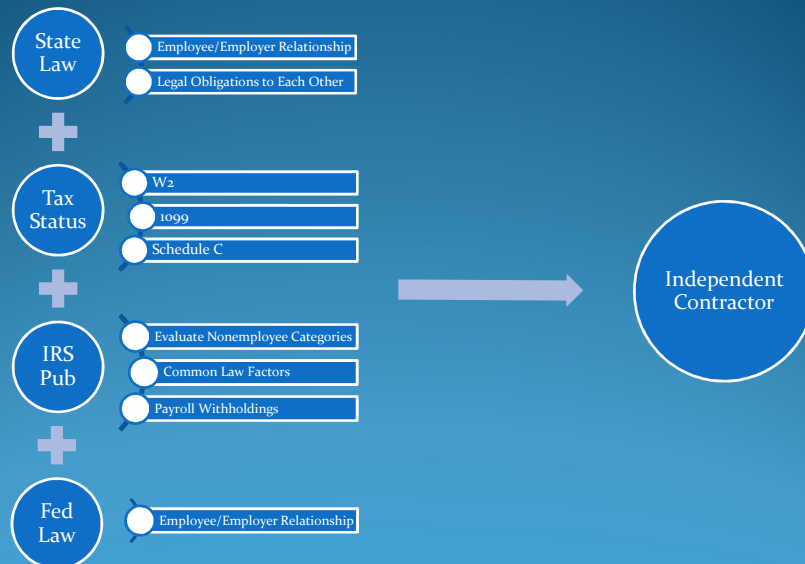
Annual Tax Rate

- Residential Location \$151
- Commercial Location \$159
- Out of Town \$239

Annual Revenue

- Currently, 1100 licensed agents and brokers
- 2012 \$234,557
- 2013 \$221,926

Evaluative Factors



California Law

Business & Professions Code § 16300:

When there is a dispute between a city... and a taxpayer, the manner in which a taxpayer reports or reported income to the Franchise Tax Board or the Internal Revenue Service shall create a presumption regarding whether the taxpayer performed services for an employer as an employee, or operated a business entity.

Most real estate agents, like most independent contractors, file a Schedule C to receive the benefit of federal and state deductions, creating the presumption of being a business entity.

Federal Standards

IRS Publication 15A states that a real estate agent is a statutory non employee if:

- 1) Substantially all payments for their services as direct sellers or real estate agents are directly related to sales or other output, rather than to the number of hours worked, and
- 2) Their services are performed under a written contract providing that they will not be treated as employees for federal tax purposes

Federal Law

U.S. Code Title 26, Chapter 25, § 3508, Treatment of Real Estate Agents and Direct Sellers, provides that

...in the case of services performed as a qualified real estate agent ...

- 1) the individual performing such services shall not be treated as an employee, and
- 2) the person for whom such services are performed shall not be treated as an employer.”

Legal Precedent

The application of the City’s business license requirements to real estate agents has previously been challenged and upheld in court:

- Cartelli vs. City of Newport Beach, Superior Court of California, County of Orange Case #30-2009-00235017
- Migliori vs. City of Newport Beach, Superior Court of California, County of Orange Case #30-2011-00508986

Independent Contractor Agreement

(Between Broker and Associate-Licensee)

(C.A.R. Form ICA, Revised 11/13)



CALIFORNIA
ASSOCIATION
OF REALTORS®

INDEPENDENT CONTRACTOR AGREEMENT
(Between Broker and Associate-Licensee)
(C.A.R. Form ICA, Revised 11/13)

3. INDEPENDENT CONTRACTOR RELATIONSHIP:

- A. Broker and Associate-Licensee intend that, to the maximum extent permissible by law: (i) This Agreement does not constitute an employment agreement by either party; (ii) Broker and Associate-Licensee are independent contracting parties with respect to all services rendered under this Agreement; and (iii) This Agreement shall not be construed as a partnership.
- B. Broker shall not: (i) restrict Associate-Licensee's activities to particular geographical areas, or (ii) dictate Associate-Licensee's activities with regard to hours, leads, open houses, opportunity or floor time, production, prospects, sales meetings, schedule, inventory, time off, vacation, or similar activities, except to the extent required by law.
- C. Associate-Licensee shall not be required to accept an assignment by Broker to service any particular current or prospective listing or parties.
- D. Except as required by law: (i) Associate-Licensee retains sole and absolute discretion and judgment in the methods, techniques, and procedures to be used in soliciting and obtaining listings, sales, exchanges, leases, rentals, or other transactions, and in carrying out Associate-Licensee's selling and soliciting activities; (ii) Associate-Licensee is under the control of Broker as to the results of Associate-Licensee's work only, and not as to the means by which those results are accomplished; (iii) Associate-Licensee has no authority to bind Broker by any promise or representation; and (iv) Broker shall not be liable for any obligation or liability incurred by Associate-Licensee.
- E. Associate-Licensee's only remuneration shall be the compensation specified in paragraph 8.
- F. Associate-Licensee shall not be considered an employee for state and federal purposes.
- G. The fact the Broker may carry workers' compensation insurance for Broker's own benefit and for the mutual benefit of Broker and Licensees associated with Broker, ... shall not create an inference of employment.
- H. Associate-Licensee shall not be considered an employee for state and federal purposes.
- I. Associate-Licensee shall not be considered an employee for state and federal purposes.
- J. Associate-Licensee shall not be considered an employee for state and federal purposes.
- K. Associate-Licensee shall not be considered an employee for state and federal purposes.
- L. Associate-Licensee shall not be considered an employee for state and federal purposes.
- M. Associate-Licensee shall not be considered an employee for state and federal purposes.
- N. Associate-Licensee shall not be considered an employee for state and federal purposes.
- O. Associate-Licensee shall not be considered an employee for state and federal purposes.
- P. Associate-Licensee shall not be considered an employee for state and federal purposes.
- Q. Associate-Licensee shall not be considered an employee for state and federal purposes.
- R. Associate-Licensee shall not be considered an employee for state and federal purposes.
- S. Associate-Licensee shall not be considered an employee for state and federal purposes.
- T. Associate-Licensee shall not be considered an employee for state and federal purposes.
- U. Associate-Licensee shall not be considered an employee for state and federal purposes.
- V. Associate-Licensee shall not be considered an employee for state and federal purposes.
- W. Associate-Licensee shall not be considered an employee for state and federal purposes.
- X. Associate-Licensee shall not be considered an employee for state and federal purposes.
- Y. Associate-Licensee shall not be considered an employee for state and federal purposes.
- Z. Associate-Licensee shall not be considered an employee for state and federal purposes.

Is our treatment of the real estate industry
consistent with the treatment of other
industries that employ independent
contractors?

Independent Contractors

- Independent contractors are required to obtain business licenses.
- A person is deemed an independent contractor (not a W2 employee) if that person:
 - 1) Is issued a 1099 return by its employer; and
 - 2) The employer does not remit federal and state tax on behalf of that person.

Industries with Independent Contractors in Newport Beach



How do other cities classify real estate agents for business license taxation purposes?

Independent Contractor

Buena Park
 Carlsbad
 Costa Mesa
 Cypress
 Fountain Valley
 Garden Grove
 La Habra
 La Palma
 Los Alamitos
 Laguna Beach
 Newport Beach
 Oxnard
 San Diego
 San Juan Capistrano
 San Marino
 Santa Monica
 Westminster

Employees of Broker

Brea
 Huntington Beach
 Long Beach
 Orange
 Tustin

Other

Beverly Hills
 Palm Springs
 Pasadena
 Santa Barbara
 Walnut Creek

Other Considerations

- If the tax becomes the responsibility of the broker to pay on behalf of their agents, there will be an increased likelihood that out of City brokers will have an unfair advantage over brokers and agents within the City if their tax is uncollectable.
- If real estate agents were to be exempted from the City's business license requirements, the initial legal concern is that we could face challenges from other types of independent contractors seeking exemption.

Summary – Frequently Asked Questions

- Real estate regulations require me to work for a broker. The broker is taxed, why should I also be taxed?
- Since my broker pays workers comp on my behalf, shouldn't I be classified as an employee of the broker for taxation purposes?
- Other cities exempt real estate agents from the business license tax, why doesn't Newport Beach?

City of Newport Beach

A Review of Business License Tax Requirements for Real Estate Agents

