

Attachment 2

APPEAL PETITIONS MUST BE FILED WITH THE CITY CLERK'S OFFICE WITHIN 14 CALENDAR DAYS AFTER THE DATE OF THE DECISION

APPEAL TO _____ COMMISSION OR CITY COUNCIL

PLEASE TYPE OR PRINT CLEARLY IN BLACK INK

June 20, 2012

Date

In accordance with the appeals procedure as authorized by the provisions of the Beverly Hills Municipal Code, the undersigned hereby appeals from the decision of Dept. of Administrative Services (Official, Board or Commission involved) rendered on June 7, 2012; which decision consisted of: The grounds submitted for this appeal are as follows: **(WARNING: State all grounds for appeal. Describe how decision is inconsistent with law. Use extra paper if necessary.)**

See attached letter appeal dated June 20, 2012; see also Exhibit A, letter brief dated April 12, 2012.

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The undersigned discussed the decision being appealed with:

Noel Marquis, Assistant Director, Administrative Services - Finance on April 11, 2012
(Department Head(s) Involved) Date

It is requested that written notice of the time and place for the hearing on this appeal before the City Council be sent to:

Allan Cooper, Esq., Ervin Cohen & Jessup LLP, 9401 Wilshire Blvd., 9th Floor, Beverly Hills Ca 90210
Name Address


Signature of appealing party
Ervin, Cohen & Jessup, LLP
9401 Wilshire Blvd., 9th Floor, Beverly Hills, CA 90210
Address
Tel: (310) 273-6333
Fax: (310) 859-2325
Telephone Number & Fax Number

Fee Paid \$3,714.20 (Ck. #51920) (For City Clerk's use) DATE RECEIVED

LOG NO. 28 X 12 Written Notice mailed to appellant:

Copies to: City Council, City Manager, City Attorney, Admin. Services
Involved Department

9401 Wilshire Blvd., 9th Floor
Beverly Hills, CA 90212-2974
acooper@ecjlaw.com
PH: 310.281.6396
FX: 310.859.2325
File 9325-4

June 20, 2012

VIA PERSONAL DELIVERY

City Clerk
City of Beverly Hills
455 North Rexford Drive, Room 290
Beverly Hills, CA 90210

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Re: Appeal to City Council of Beverly Hills Pursuant to Beverly Hills Municipal Code Section 3-1-213(L)

Dear Mayor Brien and Council Members:

Specialty Surgical Center, LLC and Specialty Surgical Center of Beverly Hills, L.P. (collectively "SSC") hereby appeal the June 7, 2012 Decision and Findings ("Decision") of the City of Beverly Hills Department of Administrative Services ("City"). The Decision finds that for purposes of the City's business tax ordinance, (a) SSC's surgery centers fall into Classification "F" as well as Classification "C", (b) 75% of SSC's gross receipts are attributable to its Classification "F" operations, and therefore (c) SSC owes the City \$5,536,365.48 in back taxes, interest, and penalties.

In short, the Decision holds that SSC's surgery centers are not really engaged in the professional business of having surgeries performed (Classification "C"—professions and semi-professions)—the classification under which SSC has consistently reported—but, rather, are predominantly engaged in the business of "renting or leasing...commercial property" (Classification "F") such that, the Decision finds 75% of SSC's revenues, each and every year since 2002, are attributable to its being a commercial landlord. The significant difference between the two is that Classification C taxpayers pay business taxes based on the number of professionals and semiprofessionals they employ, whereas Classification F taxpayers pay business taxes based on gross receipts, resulting in a much higher tax.

The notion that a surgery center's business is that of a commercial landlord is flawed not merely intuitively—ask SSC's patients if they think they are renting space and you will get a look that says "Huh?" and then an answer of "no"—but also constitutionally, legally, and factually. All these flaws were pointed out to City staff, in excruciating detail, in SSC's counsel's April 12, 2012 19-page letter ("Letter") to Scott G. Miller and Noel Marquis, the City's Director and

Assistant Director of Administrative Services. A copy of that letter is attached hereto as Exhibit A, and the Decision is attached hereto as Exhibit B for your convenience; we hope you will have and take the time to read them. The Decision, however, ignores or distorts the points made by SSC in the Letter, and makes assertions without basis; as a result, it comes to an unsupportable conclusion. The purpose of this letter is to explain how and why that is.

Before we begin our journey, it bears noting, although the Council is no doubt aware, that Beverly Hills Municipal Code (“Code”) Section 1-4-106 provides that your hearing of this matter is to be “de novo in that an independent re-examination of the matter shall be made.” When you do that, you will find that what has happened here is wrong, unfair, and punitive.¹

1. Facts On Which The Appeal Is Based

SSC’s business is as described in the Letter, at page 2. The Decision has no quarrel with that description, but it chooses to call SSC’s charges “facilities fees”. They are not. SSC’s charges are solely based on what medical procedures the physician recorded that he or she performed—not for time in the center, not for space, and not for supplies (except certain implants used in some procedures). Other than physicians, all of the professional and paraprofessional services are supplied by SSC. The City knows that SSC does not charge “facilities fees”, as SSC provided it with exemplars of its invoices; neither the term “facilities fees”, nor any other term consistent with the notion of “lease” or “rental” of “commercial real property” ever appears.

As the Council is well aware, the City’s business tax is a self-reported tax; that is, it places the burden on the taxpayer to classify its activities and report, and pay tax, accordingly. From a legal perspective, therefore, the tax law must be sufficiently clear that the reasonable taxpayer can do so. The Decision does not appear to question this proposition; instead, it says that SSC’s activities “clearly fall within any ordinary understanding of the word ‘renting’.” Decision at 7.

¹ The interest and penalties amount to roughly \$3.3 million—1.5 times the amount of the tax! This itself constitutes unconstitutional punitive damages, as (a) under any set of circumstances, this clearly is a novel issue about which, as a minimum, there is a good faith dispute; and (b) much of the time which has elapsed and for which interest and penalties are being assessed occurred so that the City could do its audit and the parties could attempt to reach a resolution, though ultimately the attempt was unsuccessful. Under these circumstances, the Code provisions cannot properly be construed to impose penalties or interest at any time before the assessment was made. To do so simply adds insult to injury.

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Putting aside the legal inadequacy of this statement, which will be addressed later herein, that statement by the City is demonstrably incorrect factually—**as the City has admitted**. First of all, one fact that is not, and cannot be, in dispute, is that although there have been surgery centers operating in the City since at least the 1990's, not a single surgery center in the City has ever reported its activities as falling within business tax Classification F—not one! SSC knows this because its counsel submitted a Freedom of Information Act (“FOIA”) request to the City, and that was the City’s response. *See* Ex. C hereto, a May 7, 2012 email from J. Zaragoza to M. Crowder in response to Ms. Crowder’s email specifically asking the number of surgery centers or suites in that classification from 1990 to the present. That FOIA request also revealed that as of January 2010, there were 28 ambulatory surgical centers in the City. *See* Ex. D hereto, a list of those centers provided by the City in response to SSC’s FOIA request. Admittedly, faced with the City’s threats of assessments similar to that involved, here, one or two centers have entered into settlement agreements which provide that they will report some of their revenues as Classification F activities; but prior to that, when left to their own devices, none of those entities had ever reported under Classification F.

What does this prove? One of three things, and three things only: (1) all surgery centers in Beverly Hills have conspired for more than 20 years to defraud the taxing authorities; (2) in fact, surgery centers do not consider themselves to be—and are not—engaged in the business of “leasing or renting” “commercial property”; or (3) that surgery centers’ activities do not “clearly fall within any ordinary understanding of the word ‘renting’”—that is, it is not clear at all. The first—a global conspiracy—is ridiculous on its face, and the City can offer no basis to support it. The second is what SSC believes to be true for the reasons set forth in the Letter (pages 13-18), and which will be referenced below—and which requires that this appeal be granted.

That leaves the third—that the Code is so unclear such that a surgery center such as SSC would not know that its activities to fall into Classification F. And it is here where the City admitted—long before there was a dispute between the City and SSC, or any other surgery center—that the City’s law is, in fact, **not clear**. Indeed, as far back as January 2005, the City knew that no surgery center was reporting under Classification F because such centers were “unaware” that their activities fell within multiple classifications such as Classification F. This comes straight out of the mouth of Noel Marquis himself; he also said that the Code does not allow for proper identification and classification of these businesses under Classification F. *See* Ex. A (Letter) at 5-7, Exs. 2 and 3. Given the City’s own words, then, as well as the conduct of the entire group of its taxpayers at issue here, the Decision is now saying that SSC’s activities clearly fall within any ordinary understanding of the word “renting” is not just wrong—it is disingenuous if not deliberately false.

But there are two more points—also undisputed—to consider. First, the City tried to get the result the Decision seeks herein—taxation of surgery centers (among other professionals) on a

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gross receipts basis—in the legally appropriate way when it put forth Proposition P in 2009, but that measure overwhelmingly lost. Now, it's trying to evade the 79%-21% defeat by attempting to re-classify SSC's business. Second, there is no Code section, regulation, or other means by which SSC could have ascertained what percentage of its revenues—revenues of a business that the City, on its best day, considers to fall into multiple classifications—is attributable to which classification. Thus, the City's position would impermissibly require surgery centers to play business tax "pin the tail on the donkey", at the peril of tax, interest, and penalties if it reports differently than the City would like.

2. Why the Decision Is Wrong

The Letter contained an exhaustive analysis of the facts and law applicable to the attempted imposition of Classification F on SSC's business. Most of its points went unaddressed in the decision. SSC does not wish to duplicate the Letter in this submission. Still, the inadequacies of the Decision must be pointed out, with appropriate citations to the Letter rather than repetition of it.

A. Constitutionality

The Letter provided two separate bases why the City's position is unconstitutional. The first was that the proposed assessment violates the California Constitution's prohibition (Article 13C, Sec. 2) on raising or imposing new taxes without voter approval. That prohibition is violated when, among other things, a government revises the methodology (mathematical equation) by which a tax is calculated, with the result of increasing it. (Gov't. Code §5370(h)(1)(B).) Here, the City is revising the methodology and increasing the taxation of SSC in two ways: First, by choosing to characterize SSC's business as leasing or renting commercial property, it is changing the basis of tax from "head count" to "gross receipts". Second, it is applying a 75% attribution of SSC's revenues to its alleged "leasing or renting" activities, when there is absolutely no methodology at all—not in the Code, not in any regulation or procedure, or otherwise—in short, without any legal basis at all that any taxpayer could find. Thus, it is enacting a new methodology, and one out of whole cloth, at that.

The Decision's response to the first is that it is not reclassifying SSC, but that SSC has been reporting under the wrong classification all along. But as shown above, SSC has been reporting under the same classification as every other surgical center in the City; the Code has no definition at all about what activities constitute "leasing" or "renting"; and the City has previously acknowledged that the Code does not adequately provide for the identification and classification of surgery centers as Classification F businesses.

Still, the Decision attempts to justify itself by referring to Code Section 3-1-212. Specifically, it relies on the language of the second paragraph of that section which states that the determination

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of the classification of business a registrant is engaged in, or is about to engage in, or the determination of the number of vehicles, machines, devices or articles of equipment used, or the number of persons employed or the gross receipts, gross operating expenses or gross payroll, for the computation of tax to be paid shall be an administrative function of the Director of Finance administration or his/her designated representative. But that reliance is misplaced. That entire section has to do with the director's duty to enforce the Code. Nothing in that section gives the director the authority to re-write, amend, or otherwise change the Code's definitions and classifications. For example, if the Code provided for taxation of horses, this section would not give the director the right to tax donkeys because they are similar to horses. As the Code states, the director's function is expressly **administrative**, not **legislative**. All the director has the power to do is to apply the Code's definitions—not enlarge or change them. What is being attempted here is a change/expansion of the Code definition of Classification F activities—a legislative action—by someone with no power to do so.

Interestingly in this regard, however, the first paragraph of that same section gives the Director of Finance Administration—the person charged with enforcement of the Code's tax provisions—the power to make rules and regulations “not inconsistent with the provisions of this article as may be necessary or desirable” to aid in the Code's enforcement (Section 3-1-212(a)). Yet having known since at least 2005—if not well before—the way surgery centers such as SSC were reporting, the Director never issued any such rules or regulations—another, albeit tacit, recognition that surgery centers' activities do not fall into Classification F. And if any further proof were ever needed, proof positive comes from the City's attempt to raise taxes the right way—Proposition P—but ultimately resorting to reclassification when the proposition was rejected by the voters. In any real sense, therefore, the Decision is indeed a reclassification.

The City has no real response to the second, as it unquestionably has made up the 75% out of nowhere. Look at the Letter—SSC has repeatedly demanded to know where this figure came from; now look at the Decision—no methodology at all, much less one a taxpayer could find in the Code. The only “responsive” comment made in the Decision is an assertion that SSC somehow “waived” its argument by failing to propose its own percentage. This assertion is wrong on multiple levels. SSC didn't fail to propose a percentage; while the Director doesn't like it, SSC's proposed percentage is “zero” because it does not believe its activities fall within Classification F. Moreover, to be valid, the methodology has to be in the tax law itself; the law cannot simply be an invitation to negotiate a methodology. And legally speaking, constitutional arguments are not waivable unless made expressly, knowingly and intelligently. Here, SSC has protested the lack of a methodology from which it could have derived the 75% figure from the get-go. Just look at the Letter.

The second reason the Code is unconstitutional as applied here is what's called the doctrine of “void for vagueness”. Simply put, it means that in order for a law to be valid, it must be clear

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enough so that ordinary people do not have to guess at its meaning and potentially come out differently as to its application. In the context of tax law, this means that the law has to provide a standard that is sufficiently definite to be understandable to the reasonable taxpayer who wants to comply with the law.

There is absolutely no question that the Code provisions in question here lack that definition—unless the definition is such which excludes surgery centers from Classification F. How could the Code possibly have been, or be, clear enough so that the ordinary taxpaying surgery center would have understood that it was in Classification F, if not a single surgery center ever filed under that classification on its own? How could the Code possibly have been, or be, sufficiently clear when the City's own Assistant Director of Finance Administration said that it was not? How could the Code possibly have been, or be, clear enough so that SSC would have known what percentage of its revenues the law considered to be attributable to Classification F activities, when there is no provision at all that would provide any guidance as to how to measure them? The answers to these questions are self-evident—and they are most certainly **not** that SSC's "activities clearly fall under any ordinary understanding of the term 'renting'."

There is no doubt the Decision is an unconstitutional attempt to force a round peg into a square hole.

B. SSC Is Not Engaged In The Business Of Leasing Or Renting Commercial Property

The Decision tacitly admits that SSC's activities do not constitute "leasing", and instead is based on the assertion that SSC "rents" commercial property. Ex. B (Decision) at 7. But again, the Decision is wrong.

The Decision says that the term "rent" "ordinarily is understood as compensation or a fee for use of property." Of course, that is not how the Code defines "rent"; the Code contains no definition at all. The Decision then goes on to quote Black's Law Dictionary as defining "rent" as "compensation paid; usu. periodically, for the use or occupancy of property (esp. real property)." Decision at 7. It then goes on to claim that because surgeries are performed in the surgery centers by non-employee surgeons, SSC is being paid for use or occupancy of property.

But the City ignores that fact that there is more to the definition of "rent" than any payment for any service that takes place in space. As pointed out in the Letter (Ex. A at 14-17), both leases and rentals are estates in land which have legally defined attributes that distinguish themselves from other arrangements, such as, most particularly, licenses to use space, which is discussed in more detail below. Such attributes generally include demised premises, exclusivity of possession as against all others (even the landlord), rental rates based on the characteristics of the space (size, location, etc.), periodic payments, and others (Ex. A (Letter) at 14-17). All of these are

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totally absent from SSC's operations. There are no demised premises (the patient doesn't know what room he or she will be in); the charges have nothing to do with size or location of the space at all, only with the procedure performed; payments are not periodic or based on length of time in the operating area; possession is not exclusive, etc. There isn't even a "renter".

Curiously—but revealingly—the position taken in the Decision's "analysis" on this issue is different than the analysis of the City's Planning Commission staff in 2010. SSC's FOIA request revealed a staff report for the Commission meeting of January 28 of that year relating to the ordinance changing medical land use policies in the City to limit or prohibit new or expanded medical uses in the City. In that report by Senior Planner Michele McGrath, she relates the views of the City's Business Tax specialists and states the following:

"Surgi-centers can be Class B ('Retail, Wholesale, Manufacturing and Contractors'), Class C [Professions and Semiprofessions], or Class F ('Commercial Property Renting or Leasing') depending on how the surgi-center bills activities. For example, if the surgi-center rents space by the hour to a doctor, such activity could fall under Class F."

(Emphasis added.) A copy of the report is attached hereto as Exhibit E.

As noted earlier in this letter, it is undisputed that SSC does **not** "rent space by the hour" to doctors. It does not bill for space at all, nor does it bill on any periodic basis, hourly or otherwise. It charges based on the procedure(s) performed. Based on this report then, presumably the City's Business Tax specialists would **not** consider SSC's activities to fall into Classification F. If nothing else, this difference between Ms. McGrath's/Business Tax specialists' view, on the one hand, and the Decision, on the other, is proof positive that the law is not clear; there are at least two, and per this staff report three, different classifications which could arguably be applicable; and what activity falls into which classification is not set forth with any clarity, or at all, in the Code. Thus, this not only demonstrates that under this view, SSC is not engaged in Classification F activities, but also underscores that the Code provision, as applied here, is void for vagueness, as there is no way a taxpayer like SSC could look at the Code and determine what classification(s) its business falls in and, if in more than one, how to allocate its activities and its revenues between or among them.

As the Letter demonstrated (Ex. A at 16-17)—and the Decision wholly ignores—at most for the City, SSC's operations have the attributes of a license, not a lease or rental. A license is a non-possessory, personal privilege to use the space of another, not an estate in real property like a lease or rental. How do we know this? First, the analysis of the law contained in the Letter shows this to be so. Second, a practical view of the issue leads to the same conclusion. For example, the Decision likens the surgery center to a hotel (which is not taxed under Classification F in any event, but under a different classification). But when you go to a hotel and the evening is over, what do you say? "I'm going to **my** room." And it is, for however long

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you stay, your room. You control who sleeps there; you can tell housekeeping not to come in; you control the room. Does an SSC patient say “I’m having surgery done in my operating room”? Does the patient control the procedure or the use of the operating area, or have the right to tell nurses not to be there? The answers are “no” and “no”. What goes on in a surgery center is that, at most, the center allows—licenses—the doctor to use the center for his surgeries, and the doctor utilizes all of what the center offers—not just space. At most, this is a licensing arrangement. And Classification F by its terms does not include “licensing” within its purview.

The Decision is also wrong when it says that SSC “has no role in the performance of professional surgical services.” Untrue. Not only are the nurses—who are licensed professionals—for the surgeries supplied by SSC, but SSC supplies the technicians, machinery, supplies, implements, etc. without which the surgeries cannot be conducted. And contrary to the Decision’s aspersions, these are not “incidental” items like housekeeping in a hotel. Indeed, surgery centers themselves are licensed by the State of California and must meet stringent requirements relating to public health and safety, as are nurses and others of its employees. The center is thus an indispensable part of the procedure, not just a warm host.

Finally, the Decision’s reasoning, if accepted, makes almost any activity “leasing or renting of commercial property.” By its logic, a movie theater’s business is “renting” the theater to the people who buy tickets. (Contrast that to where a film company rents out the theater for a premiere; that is “renting”, as the film company is in control of the theater for that night in terms of who gets in, what gets shown, and more). By its logic Neiman Marcus is “renting” to its shoppers (they have to stand somewhere in the store, don’t they?), dentists are “renting” space in their chairs to their patients, golf courses are “renting” the course to their golfers, etc., etc.—the list is endless. If that was the sense in which the Code was intended, it should have clearly said so—or Mr. Marquis should have issued a regulation that said so. Almost every activity is performed in some space or other, yet clearly not every such activity is “renting”. And neither is SSC’s business.

3. Conclusion

SSC and the City are living in very challenging times economically. SSC recognizes that cities and states are all trying to find ways to pay for the services their constituents want or demand, and are facing great difficulties—made even greater by taxpayers’ unwilling to vote, as the California Constitution requires, for higher or continued taxes.

Still, the challenge cannot fairly, appropriately, or legally be answered by torturing laws to say things they don’t, saying things are clear when they plainly are not, or saying businesses do X when they do Y. Yet that is what has happened here. Sometimes, doing the right thing means that you don’t get what you would like. It is incumbent on the City—on you, the Council—to do

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the right thing, even if that means the City won't get the revenue it would like. And based on the facts (including the City's own admissions) and the law, the "right thing" is to grant this Appeal and overturn the Decision.

Counsel for SSC will be out of State on business July 24-25, so SSC respectfully requests that the matter not be taken up by the Council on those dates. Counsel does look forward to discussing these issues at the hearing, to answering any questions the Council may have, and to getting the answers to the questions it has asked but which have not been forthcoming.

Very truly yours,



Allan Cooper

cc: Phil Starr, Ervin Cohen & Jessup LLP
Laurence S. Wiener, City Attorney
Kayser Sume, City Attorney's Office
Mitchell E. Abbott, Esq.

EXHIBIT A

April 12, 2012

VIA FEDERAL EXPRESS AND PERSONAL DELIVERY

Noel Marquis
Assistant Director of Administrative Services
City of Beverly Hills
455 N. Rexford Drive
Beverly Hills, California 90210

Scott G. Miller
Director of Administrative Services
City of Beverly Hills
455 N. Rexford Drive
Beverly Hills, California 90210

Re: **April 12, 2012 Administrative Hearing on Assessment of Business Tax Liability for Specialty Surgical Center, LLC and Specialty Surgical Center of Beverly Hills, L.P.**

Gentlemen:

This firm represents Specialty Surgical Center, LLC (located at 9675 Brighton Way, Suite 100, Beverly Hills 90210) and Specialty Surgical Center of Beverly Hills, L.P. (located at 8670 Wilshire Boulevard, Suite 310, Beverly Hills 90211) (collectively "SSC"). We received Noel Marquis's March 26, 2012 correspondence scheduling SSC's hearing in connection with its appeal from the City of Beverly Hills' ("City") January 9, 2012 Assessment of Business Tax Liability ("Assessment"). We will be attending that April 12, 2012 hearing at 2:00 p.m. on behalf of SSC.

The Assessment is based entirely upon the City's purported re-classification of SSC from a Class "C" business (professions and semiprofessions)—the classification under which it clearly falls and under which it has consistently reported since its inception—to a business falling into both that classification and into a Class "F" business (renting and leasing commercial property) for city business taxation purposes. From that flawed premise, the City then arbitrarily allocates 75% of SSC's business to the asserted Class F activities and from there assesses \$12,173,010.70 in alleged liability for "unpaid business taxes, penalties and interest through January 31, 2012."

As will be shown below, this purported re-classification is fatally flawed for numerous reasons. This letter sets forth just some of them; it is neither intended to be exhaustive nor to be interpreted as any kind of admission, and SSC reserves its right to assert other reasons or arguments in the future.

I. BACKGROUND

A. SSC

SSC operates two stand-alone outpatient ambulatory surgical centers in Beverly Hills, one located at 9675 Brighton Way, Suite 100, Beverly Hills, 90210 (the "Brighton Way Facility") and one located at 8670 Wilshire Boulevard, Suite 301, Beverly Hills, 90211 (the "Wilshire Facility"). The Brighton Way Facility opened its doors in October 1998, and the Wilshire Facility opened in November 2003; both are encompassed within the term "SSC" as used herein. Physicians perform various medical procedures in the surgery suites. SSC provides registered nurses, medical equipment, anesthesia, medications, and related supplies and ancillary products for use by the physicians. SSC does not separately charge for use of any of its supplies except for implants that are part and parcel of certain medical procedures (such as neural and shoulder implants).

Physicians block out dates/times to schedule surgeries in the center hand-in-hand with their use of SSC's staff and supplies. When physicians contact SSC to reserve a date/time for a procedure, they provide SSC staff with the patient's name and medical-related information. SSC then uses this information to verify that the patient has insurance and that SSC has a contract for reimbursement for the given procedure with that patient's insurance company, Medicare, etc.

After the procedure, the physician dictates into a recording device exactly what medical procedures he/she performed. The dictation is sent to a coding company that translates the specific medical procedures the physician performed into pre-determined fees to bill the patient based on that patient's medical insurance and a CPT-based fee schedule¹. SSC then directly bills the patient/insurance company for those procedures. Ultimately, the patient/insurer receives a bill from the physician for performing the medical procedure and a separate bill from SSC. SSC does not bill or charge the physicians for using its suites. Moreover, SSC's bills to its patients do not charge for supplies, time in the suites, or use of the suites. No patients stay at SSC overnight.

B. The City Of Beverly Hills Municipal Code

Within limits, the City is permitted to tax entities, such as SSC, that engage in business within its city limits. The type and amount of taxation is dependent on which classification(s) an entity falls into. Specifically, the City of Beverly Hills' Municipal Code ("Code"), Section 3-1-201(C) provides:

¹ CPT stands for Common Procedural Terminology.

A business tax is hereby imposed in the amount prescribed in the applicable section. The required business tax is imposed pursuant to the taxing power of the city of Beverly Hills solely for the purpose of obtaining revenue. A business tax must be paid by every person engaged in any business or occupation conducted within the city of Beverly Hills.

(See also Code §3-1-205 (Business Tax defined as: "The tax imposed upon a person engaged in business within the city of Beverly Hills and is calculated by multiplying the measurement focus of the businesses classifications by the tax rate for the businesses classification.").)

Since SSC opened its Brighton Way Facility in October 1998, SSC has reported and paid tax solely based on Classification C of the Code. Classification C applies to "Professional and Semi-professionals" and provides that:

All registrants engaged in businesses classified by finance administration as classification C, professions and semiprofessions, shall pay an annual tax for each professional and semiprofessional employee, based on the annualized average number of professional and semiprofessional persons employed in the prior calendar year or in the case of a new business an estimate by the registrant of the average number of professional and semiprofessional persons to be employed during the current calendar year, plus a per employee tax for each nonprofessional employee, based on the annualized average number of nonprofessional persons employed in the prior calendar year or in the case of a new business an estimate by the registrant of the average number of nonprofessional persons to be employed during the current calendar year, as established in the city of Beverly Hills "schedule of taxes, fees and charges" for classification C.

On January 9, 2012, the City issued a Notice of Assessment ("Assessment") on the asserted basis that a portion of SSC's business activities should have been classified as "Commercial Property Renting and Leasing," and thus SSC should have reported and paid tax on that portion under Classification F of the Code, in addition to the tax imposed under Classification C. Classification F of the Code provides as follows:

All registrants engaged in the business of leasing or renting any commercial property, and which are not subject to the provisions of subsection E of this section, and classified by finance

administration as classification F, commercial property renting and leasing, shall pay an annual gross receipts tax for each one thousand dollars (\$1,000.00) of gross receipts, provided, based on the annualized actual gross receipts of the prior calendar year or in the case of a new business an estimate by the registrant of the gross receipts during the current calendar year, as established in the city of Beverly Hills "schedule of taxes, fees and charges" for classification F.

The City's application of the gross receipts tax of Class F to SSC's activities serves to substantially increase SSC's taxes over the "head count" tax of Class C: the Assessment is for \$12,173,010.70 in "unpaid business taxes, penalties and interest [from 2002] through January 31, 2012."

The City's position appears to be—although it is yet to be stated with any clarity—that SSC's allowing physicians to perform outpatient medical procedures in the center constitutes SSC's being "engaged in the business" of "leasing" or "renting" the surgical suites and may be taxed accordingly under Section 3-1-219(F), in addition to being taxed as a Class C provider of professional or semi-professional services. The City's position also appears to be—this time, not just with lack of clarity, but with lack of any articulated methodology at all—that of the monies received by SSC, 75% relate to the Class F activities, and only 25% to the Class C activities. The Assessment does not claim that SSC's activities fall into any other classification.

C. Procedural History

The City's antipathy toward the medical profession is by now not only well known, but well documented, and the largest reason for it is, of course, money; the City's view is that the medical profession does not provide the City with the amount of revenue the City would like. So prevalent is this view that in 2011, the City passed Ordinance No. 11-O-2602, the purpose and effect of which is to severely limit, if not eliminate, medical office use in the City.

As opposed to that ordinance, however—which at least claimed to articulate some non-financial reasons—the Assessment in this case is purely an attempt to raise revenue by taxation through the expedient of re-classification of SSC's business into a different category than that under which it has reported since inception. And the origins of this attempt—and the reasons the attempt is improper—are nothing if not crystal clear. The City wanted the medical profession, among others, to pay more taxes. It commissioned an outside consultant, MBIA MuniServices Company ("MBIA") to find ways to raise revenue either under the existing Code or by amending the Code. After an initial review, MBIA recognized that under the existing Code, it could not determine which activities engaged in by surgery centers could or would fall under which tax classification, and, thus, it suggested that the best course of action would be to

conduct a review of a randomly selected test case to better understand how surgical centers operate and what the main taxable activities are:

I have reviewed the ordinance and done some minimal research on the inter-net [*sic*] of some surgery centers in Beverly Hills. Obviously, the doctor and/or surgery center must be registered with the City and pay the tax.

While there are many instances where a business *may* be subject to multiple taxation classifications, the nature of the doctors fixed fee classification could cause some issues. If all of the taxable activity were to be taxed on gross receipts, it would be easy to allocate a portion of the gross between multiple classifications. However, since the "C" class is not based on gross receipts, a doctor may argue that the activities he is conducting are part of his professional business activity and, while they may be subject to taxation, are covered under the "C" class registration.

I believe that the best course of action is to conduct a review of a randomly selected entity. As has been the case in our previous audit endeavors, starting with a test case helps MMC and the City better understand how the industry is operating and what the main taxable activities are. Once completed, MMC can submit to the City a review of the taxation issues discovered and the legal or political impact that may arise.

(Ex. 1 (10/1/04 Memorandum from Joshua Davis of MBIA to Noel Marquis City of Beverly Hills Deputy Director, Administrative Services ("Marquis" or "Deputy Director"), emphasis added.)

Less than two weeks later, the Deputy Director wrote an interoffice communication to the Mayor and City Council members addressing the issue of "whether surgical centers or clinics pay an appropriate amount under the existing Municipal Code or even if the existing Code allows for proper identification and taxation of these businesses." (Ex. 2 at 1, emphasis added.) The Deputy Director recommended that although the issue could be addressed through a change to the Municipal Code sections related to business tax, there might be "other more effective alternatives." (*Id.* at 1, 4 ("While this issue could be addressed through a change to the Municipal Code sections related to business tax[,] staff believes there may be other more effective alternatives.") Specifically, the Deputy Director discussed classifying businesses such as surgical centers in multiple categories to raise City revenue, but admitted that it was not currently taking place because those businesses were "unaware that they are involved in multiple activities." (*Id.* at 3.) Nevertheless, the Deputy Director expressed that, based on the

assumption that patients would receive bills itemizing each type of service provided, the City could classify the so-called "rental of the surgical suite[s]" by doctors under Class F which would subject surgical centers to a gross receipts tax, as opposed to just the flat rate tax that the surgical centers were paying (and are still paying) under only Class C. (*Id.* at 3-4.)

Specifically, staff believes that surgical centers, like many businesses reviewed, should be classified in multiple categories. Often, businesses involved in multiple categories of business activity fail to properly register and pay their business tax. **This is often because the business is unaware that they are involved in multiple activities.**

(*Id.* at 3, emphasis added) The October 11, 2004 interoffice communication from the Deputy Director to the Mayor and City Councilmembers ended with the Deputy Director's stating that he was not opposed to placing a measure on the ballot but recommended first auditing several surgical centers to determine whether such action would be financially worthwhile.

RECOMMENDATION

Staff is not opposed to placing a measure on the ballot to create a new category, change the measurement focus of the existing category (i.e. to gross receipts) or change the tax requirements. However, it appears a quicker and easier option may exist. At present, and based on the information at hand, staff recommends that audits of several surgical centers and similar types of businesses be conducted to determine the potential level of tax liability this approach would produce.

(*Id.* at 4.)

Though not stated in the memo, the Deputy Director's "quicker and easier option" obviously was to do what the City has done here: claim that a surgery center's activities fall, in whole or in part, into Class F—the class that results in taxation based on gross receipts. The City subsequently used SSC as its "test case," auditing SSC in or around late 2005/early 2006. And after concluding its audit, the City apparently made the economic determination that there was enough at stake to make it financially worthwhile to try to subject surgery centers like SSC to a gross receipts tax.

But the City obviously recognized that as the Deputy Director himself had pointed out, the existing Code does **not** allow for proper identification of these businesses—which is why the business would be unaware that it was involved in multiple activities. Indeed, in a memo to

the Deputy Director from Joshua Davis of MBIA dated January 21, 2005, Mr. Davis talked about tax liability for F-Class registration for “doctors who are renting the surgery centers to other doctors,” and also asserted that the doctors were “renting staff” as part of the transaction, which he claimed constituted “leasing employees” taxable on gross receipts under a “G-Class” registration. (Ex. 3.) Significantly, however, Mr. Davis stated that “At this time, we have not encountered an entity that is properly reporting this income”—not surprising, since it would never occur to surgery centers that they were involved in “renting or leasing commercial property” or “leasing employees.”

The City therefore determined that it was necessary to amend the Code itself and seek the requisite voter approval required by Proposition 218 (no new taxes without voter approval). Accordingly, the City placed a business license tax (“Measure P”) on the ballot on March 3, 2009. If enacted, Measure P would have increased business taxes paid by surgical centers by modifying the method for calculating business taxes from one which is currently based on the number of people a given business employs (which is how SSC is taxed under Classification C) to one that is based on gross receipts (which is what the City is attempting to do now by classifying SSC as Classification F). Measure P was confronted with vehement opposition and was defeated by 79% of voters.

Unwilling to accept the defeat it suffered trying to do things the right way, the City has reverted back to the “quicker and easier option”—trying to extract more revenue from surgical centers like SSC by purporting to reclassify their activities under the existing Code, notwithstanding that the City had already acknowledged that the Code needed to be amended because it lacked clarity and that the taxpayers would and did not know that their activities fell into this classification. The Assessment is based on just such a reported reclassification. In short, the voters having denied the City entrance through the front door, the City is trying to go through the back door—and to make an end-run around the constitutional requirement of voter approval for new taxes.

II. ARGUMENT

The Assessment is invalid for numerous reasons. In general, however, they fall into one or more of three categories: (1) the Assessment is an attempt to raise or impose new taxes without voter approval in violation of Proposition 218 and the California constitutional amendment enacted thereby, and, in fact, is an attempt to raise or impose new taxes where the voters have already spoken and rejected such a result; (2) the existing Code is impermissibly and unconstitutionally vague because a taxpayer such as SSC is not able to ascertain that its activities fall into Class F in whole or in part, much less what part of its activities falls into each tax classification; and (3) even assuming *arguendo* that the Code passed constitutional muster and was not void for vagueness, SSC in fact is not “engaged in the business of leasing or renting any commercial property.” Each will be discussed in turn.

A. The City's actions are unconstitutional because they raise or impose new taxes without the requisite voter approval

The City's attempt to effectively enact new law without voter approval is unconstitutional. The California Constitution provides that no local government may impose or increase a tax unless and until that tax is submitted to the electorate and approved by majority vote. Cal. Const. Art. 13C, §2. The City is and was aware of this because, *inter alia*, it attempted to obtain voter approval in 2009 but was unsuccessful. It cannot now circumvent its constitutional obligations under the pretext of a "reclassification" of businesses like SSC under the current Beverly Hills Municipal Code.

Specifically, the California Constitution Article 13C, Sec. 2, entitled Voter Approval for Local Tax Levies, Local Government Tax Limitation, provides:

Notwithstanding any other provision of this Constitution:

(a) All taxes imposed by any local government shall be deemed to be either general taxes or special taxes. Special purpose districts or agencies, including school districts, shall have no power to levy general taxes.

(b) **No local government may impose, extend, or increase any general tax unless and until that tax is submitted to the electorate and approved by a majority vote.** A general tax shall not be deemed to have been increased if it is imposed at a rate not higher than the maximum rate so approved. The election required by this subdivision shall be consolidated with a regularly scheduled general election for members of the governing body of the local government, except in cases of emergency declared by a unanimous vote of the governing body.

(c) **Any general tax imposed, extended, or increased, without voter approval, by any local government on or after January 1, 1995, and prior to the effective date of this article, shall continue to be imposed only if approved by a majority vote** of the voters voting in an election on the issue of the imposition, which election shall be held within two years of the effective date of this article and in compliance with subdivision (b).

(d) **No local government may impose, extend, or increase any special tax unless and until that tax is submitted to the electorate and approved by a two-thirds vote.** A special tax shall not be deemed to have been increased if it is imposed at a rate not higher than the maximum rate so approved.

Cal. Constit. Art. 13C, §2 (Voter Approval For Local Tax Levies) (Ex. 4).

The City obviously was and is—and even if it weren't, would be deemed to be—aware of this constitutional mandate. That is why the City placed a business license tax (“Measure P”) on the ballot on March 3, 2009 which would, if passed, have hiked business taxes paid by doctors (and other professionals like lawyers and accountants) by modifying the method for calculating business taxes from the “head count” tax currently applicable to businesses in the C classification to the “gross receipts” tax currently applicable to classification F businesses. Measure P, however, was soundly defeated by 79% of the voters. Such a defeat makes the Assessment—which seeks to accomplish the very thing that the voters rejected, and then impose penalties and interest on top of it—all the more pernicious.

The fact that the City is acting in violation of Proposition 218 and the California Constitution is clear. In *AB Cellular LA, LLC v. City of Los Angeles* (2007) 150 Cal. App. 4th 747, 753, the City of Los Angeles tried to expand cell phone taxes to cover all air time where the owner or lessee of the cell phone had a billing address in the city. The city had adopted in 1993 an ordinance that would have allowed it to do so but the city council, at the time of adopting the ordinance, had also adopted instructions limiting the cell tax to calls originating or terminating in the city. The ordinance also contained a provision that it could not be construed as imposing a tax in violation of the United States Constitution. Proposition 218 passed in 1996. In 2000, Congress passed the Mobile Communications Sourcing Act, authorizing local governments to impose cell taxes based on the customer's place of primary use. The city then issued new instructions authorizing taxation based on the ordinance, unlimited by the 1993 instructions.

The trial court granted the cell carriers' petition for writ of mandate to overturn the new instructions, and the City appealed. The Court of Appeal affirmed the granting of the petition, and, on the carriers' cross-appeal, modified the judgment to include a declaration that the tax increase, as reflected in the final instructions, violated Proposition 218. In so holding, the Court also interpreted Government Code Section 53750 (h)(1)(B), which provides that a tax is increased if a decision by an agency revises the methodology by which a tax is calculated if that revision results in an increased amount of tax on any person or parcel. The Court interpreted “methodology” to mean the mathematical equation for calculating taxes that is officially sanctioned by the local taxing entity. The Court also thought that the city's historical interpretation—the 1993 instructions—was controlling.

The case at hand is even more compelling. The Assessment clearly changes the methodology by which the tax on SSC is calculated and results in an increased amount of tax on SSC. The Assessment has done so in two ways: it has reclassified SSC's business such that the

methodology is based on gross receipts instead of head count, and it has arbitrarily selected a percentage basis of gross receipts finding no authority, or any methodology at all, in the Code.

Proposition 218 required voter approval; the City sought but did not receive it. Now the City is attempting to circumvent this defeat and its constitutional obligations by a "re-classification" of SSC's business. Such a "reclassification" changes the methodology by which SSC has paid taxes since 1998, and by which other surgery centers have paid taxes since long before that. It was not until around 2004-05, at the earliest, that the City changed its view, all the while recognizing that a Code amendment was the appropriate way to proceed. The back-door approach adopted by the City in the wake of its defeat at the polls is unconstitutional.

B. The City's actions are unconstitutional because the Code is impermissibly vague

The Code places the burden on the taxpayer to determine what classifications its business falls under and to pay taxes based on the methodology specified in the Code for that classification. It places the taxpayer at its peril—with interest and penalties—if the taxpayer reports under the wrong classification, or in not all classifications to which its activities applies. Thus, as a matter of due process, the Code must be sufficiently clear that an ordinary taxpayer is able to know (1) what classification(s) his/its business activities fall under and (2) if those activities fall under multiple classifications, how to determine what portion of those activities falls into which classification. If the Code (including any regulations or other guidelines adopted thereunder) does not enable the ordinary taxpayer to make these determinations, it is impermissibly and unconstitutionally vague. And that is exactly the case here.

The vagueness doctrine bars enforcement of a statute which either forbids or requires the doing of an act in terms so vague that men of common intelligence must necessarily guess at its meaning and differ as to its application. U.S. Const. Amend. 14; Cal. Const. Art. 1, §7; *Gatto v. County of Sonoma*, 98 Cal. App. 4th 744, 773-74 (2002) ("A regulation is constitutionally void on its face when, as matter of due process, it is so vague that persons 'of common intelligence must necessarily guess at its meaning and differ as to its application.'"); *Connally v. General Construction Co.*, 269 U.S. 385, 391 (1926); *Ketchens v. Reiner*, 194 Cal. App. 3d 470, 477 (1987) (holding that statutes making it a misdemeanor to insult a teacher in the presence of a pupil or abuse a teacher in the presence of other school personnel or pupils is unconstitutionally vague, and thus parent and taxpayers were entitled to preliminary injunction barring enforcement of statutes); *Duffy v. State Bd. of Equalization*, 152 Cal.App.3d 1156, 1173 (1984) ("To be valid, a tax statute must prescribe a standard sufficiently definite to be understandable to the average person who desires to comply with it."). The void for vagueness doctrine is designed to prevent arbitrary and discriminatory enforcement. *Gatto*, 98 Cal. App. 4th at 774; *Smith v. Goguen*, 415 U.S. 566, 573 (1974) (holding that provision of the

Massachusetts flag misuse statute that subjects to criminal liability anyone who publicly treats contemptuously the U.S. flag was void for vagueness under the due process clause where 'contemptuous treatment' was not defined); *Ketchens*, 194 Cal. App. 3d at 477; *Kolender v. Lawson*, 461 U.S. 352, 357 (1983) (doctrine seeks to avoid "arbitrary and discriminatory enforcement") (holding that the statute was unconstitutionally vague by failing to clarify what was contemplated by the requirement that a suspect provide a "credible and reliable" identification). The problem with a vague regulation is that it "impermissibly delegates basic policy matters to policemen, judges, and juries for resolution on an ad hoc and subjective basis . . ." *Gatto*, 98 Cal. App. 4th at 774; *Grayned v. City of Rockford*, 408 U.S. 104, 108–109 (1972); *Ketchens*, 194 Cal. App. 3d at 477.

The principles behind and standard for evaluating vagueness were enunciated in *Grayned v. City of Rockford*, 408 U.S. 104, 108-109 (1972):

Vague laws offend several important values. First, because we assume that man is free to steer between lawful and unlawful conduct, we insist that laws give the person of ordinary intelligence a reasonable opportunity to know what is prohibited, so that he may act accordingly. Vague laws may trap the innocent by not providing fair warning. Second, if arbitrary and discriminatory enforcement is to be prevented, laws must provide explicit standards for those who apply them. A vague law impermissibly delegates basic policy matters to policemen, judges, and juries for resolution on an *ad hoc* and subjective basis, with the attendant dangers of arbitrary and discriminatory applications.

(Internal citations omitted.)

As applied here, what that means is that the Code must supply explicit standards which the taxpayer can read and apply. But the Code does no such thing. In fact, it supplies no standards at all. It does not contain any definition of, or any other way of ascertaining, what it means when it says "engaged in the business of leasing or renting commercial real property." That language might be sufficient as applied to the owner of a commercial office building who enters into leases, or month-to-month rental agreements with tenants, just as there would be no doubt that hitting a teacher with a baseball bat would be "abusing" the teacher. But as applied to SSC, the lack of a definition or other means by which SSC—which does not enter into leases or rental agreements, has no tenants, charges based on procedure performed and not on time or square footage, etc.—could determine that it was "engaged in the business of leasing or renting any commercial property" and thus in Class F, is fatal. No better examples of this can be found than in the documents of the City and its consultant: (1) Businesses fail to "properly"

register “often because the business is unaware that they are engaged in multiple activities” (Ex. 2 at 3); (2) “[W]e have not encountered an entity that is properly reporting this income” (Ex.3 at 2); and (3) the physician is renting staff, which constitutes “leasing employees” requiring Class G registration—a classification not even mentioned in the Assessment.

Similarly, the Code is impermissibly and unconstitutionally vague based on its failure to provide any means for a taxpayer whose business falls into multiple classifications to determine which portion of its business falls into which classification so that it can determine which tax methodology applies to which portion of its business. In other words, even if SSC could have made the determination that it was somehow considered to be in the business of leasing or renting commercial property—which it couldn’t—it still could not have determined that 75%, or any other particular percentage, of its business fell into that classification; nothing in the Code, or anywhere else, provides the means for doing so. And that the percentage chosen by the City is arbitrary is clear from two undisputed facts. First, the percentage of SSC’s business that the City has mentioned as potentially falling within Class F has been a moving target; originally, the City communicated to SSC that it felt that 50% of SSC’s business fell into Class F, but then the Assessment asserted it at 75%. This is not surprising, since the Code itself is completely silent on how to calculate any such allocation.² Moreover, the City’s position is that every single year, the percentage has been the same. Really? Not possible, and certainly not determinable. The truth is that the percentages are totally arbitrary, finding no source or definition in the Code or elsewhere, so that SSC had and has no way to determine what portion of its gross receipts should be attributable to which class of business activities, even if there were more than one. And as if more facts were needed, Mr. Davis’s statement that surgery centers are “leasing employees,” requiring Class G registration as well, would require even further apportionment.

So going back to due process, here, an individual of common intelligence would never be able to make the determination that a surgical center such as SSC is in the “business of leasing or renting [] commercial property,” as there is nothing in the Code that explicitly or implicitly includes SSC as part of Classification F. And because SSC charges based on medical procedures performed—and not time in a suite or other designated space in its facilities—there is no indication that its work could even arguably be categorized under Classification F. Indeed, the City has admitted this, given that it hired MBIA to review the Code and the classifications therein as it applied to surgical centers, and exchanged memoranda discussing the ambiguity thereof. (See, e.g., Ex. 2 (memo from the City’s Deputy Director to the Mayor and City

² Relatedly, the City has cherry-picked certain surgical centers to be subject to its reclassification. The arbitrary process in identifying which surgical centers are subject to further taxation and penalties is a violation of SSC’s due process rights as well.

Councilmembers on October 11, 2004 stating: “[T]here is a question as to whether the nature of surgical centers is sufficiently different from ‘normal’ medical practices to warrant their own business tax classification. The more immediate concern is whether surgery centers or clinics pay an appropriate amount under the existing Municipal Code or even if the existing Code allows for proper identification and taxation of these businesses.”.)

SSC’s position that the Beverly Hills Code violates its due process rights because it is unconstitutionally vague is further evidenced by the facts that, *inter alia*, a doctor and surgical center would have no idea that they are engaged in the business of “leasing” or “renting” commercial property, the terms are not defined in the Code, and what SSC does is not “leasing” or “renting” in the common meaning of those terms. And even if SSC could make the determination that it were conducting some business activities that fit into Classification F, it still would have had no means of determining from the Code how much of its activities related to which classification and thus how much it should pay in taxes in order to comply with the Code. Although it would be relatively clear for a landlord to be able to determine how much is owed based on the rent he is receiving (and because it is clear that there is no other business which the landlord is conducting), there is no such clarity with surgical centers that neither charge nor collect rent, but, rather, bill based on medical procedures performed. The City’s memoranda discussing how to tax surgical centers bolsters SSC’s position because there would have been no need for MBIA, or for any discussion back and forth between MBIA and the City, if the Code were clear on how to assess taxes for surgical centers like SSC.

C. SSC is not engaged in the business of leasing or renting commercial property and thus is not subject to Classification F taxation

Assuming the City were somehow able to get over the constitutional hurdles, the Assessment would still be required to be struck down because the City cannot meet its burden to show that SSC is somehow (1) engaged in the business of (2) leasing or renting, (3) commercial property, all within the meaning of the Business Tax Ordinance.

I. SSC is not “leasing or renting” commercial property

As noted at the outset, SSC provides personnel, equipment, medication, supplies, and other products required for physicians to be able to perform medical procedures at the centers, and it charges based on the procedure performed, not on the basis of time, space, or other measure. Such activities do not constitute “leasing” or “renting” “commercial property.”

It should be pointed out that neither Classification F, nor any other provision of the Code, defines “leasing” or “renting” for taxation, or, indeed, for any other purposes. This is a further indictment of the Code’s unconstitutional vagueness of its tax classification as applied to SSC. But the point of this section is different: In the absence of definitions in the Code,

whether SSC is “engaged in the business” of “leasing” or “renting” commercial real property must be judged under both well-established legal standards and the common-sense meaning of the terms.

“Rental” implies, at a minimum, the right to exclusive control of the premises against all the world, including the owner. *See, e.g., Qualls v. Lake Berryessa Enterprises, Inc.*, 76 Cal. App. 4th 1277, 1283 (1999). Similarly, a lease gives the lessee the right to exclusive possession of the property for a definite period of time. *Beckett v. City of Paris Dry Goods Co.*, 14 Cal. 2d 633, 636 (1939); California Real Estate Property Management, Fred Crane, Sept. 2006, Ch. 2 (hereafter “Cal. Real Estate”) at 10 (lease conveys a possessory interest in real estate which allows the tenant to exclusively occupy the leased premises in exchange for rent, called a *leasehold estate* or a *lease*); *Qualls*, 76 Cal. App. 4th at 1283; Cal. Civil Code §761; 7 Cal. Real Est. §19:1 (3d ed.) (lease as personal property or real property). These concepts do not apply to SSC’s activities because, among other things, (a) there is no “tenant” who is paying “rent,” (b) there is no right to exclusive occupancy as against the world or the owner, (c) there are no demised premises, (d) there is no definite period of time; and (e) charges are not based on space, time, or anything other than on what procedure is being performed.

Turning from the legal to the non-legal, in construing a statute, courts “first consult the words themselves, giving them their usual and ordinary meaning.” *DaFonte v. Up-Right, Inc.*, 2 Cal. 4th 593, 601 (1992). The words of a statute must be considered within the context of the statutory scheme of which they are a part, and the various parts of the statute must be harmonized by considering the particular words, clause or section in the context of the statute as a whole. *DuBois v. Workers’ Comp. Appeals Bd.*, 5 Cal. 4th 382, 388 (1993). When attempting to ascertain the usual and ordinary meaning of a word, courts appropriately refer to the dictionary definition of the word. *Wasatch Property Management v. Degrate*, 35 Cal. 4th 1111, 1121-22 (2005). The Beverly Hills Business Tax Ordinance does not define the terms “leasing” or “renting.” *Cf.* Code §3-1-205. Thus, it is appropriate to refer to the dictionary to ascertain the meaning of such words.

“Renting” is defined as “grant[ing] the possession and enjoyment of (property, machinery, etc.) in return for the payment of rent from the tenant or lessee.” (*See* dictionary.com at <http://dictionary.reference.com/browse/renting>; *see also* 7 Cal. Real Est. §19:77 (3d ed.) (defining rent in the real estate context as “consideration paid by the tenant for the use, possession, and enjoyment of the demised premises.”); Black’s Law Dictionary, 7th Ed. (defines “rent” as “consideration paid, usually periodically, for the use or occupancy of property (esp. real property)).) “Leasing” is defined as “grant[ing] the temporary possession or use of (lands, tenements, etc.) to another, usually for compensation at a fixed rate.” (*See* dictionary.com at <http://dictionary.reference.com/browse/leasing>; 7 Cal. Real Est. §19:1 (3d ed.) (defining lease in the real estate context as a grant of “exclusive possession and use of property to the tenant against the world, including the owner, for a consideration, for a term

that endures for a definite and ascertained period, however long or short the period may be, with a reversion to the owner at the end of the term, but it does not transfer any title interest in the leased premises to the tenant.”); Black’s Law Dictionary, 7th Ed. (defines “lease” (noun) as “a contract by which a rightful possessor of real property conveys the right to use and occupy that property in exchange for consideration, usu. rent” and (verb) “to grant the possession and use of (land, buildings, rooms, movable property, etc.) to another in return for rent or other consideration.”).)

Under these ordinary and usual meanings of the words “renting” and “leasing,” neither the physicians nor the patients “rent” or “lease” the surgical suites. Neither the physicians with nor without an ownership interest in SSC have the right to “exclusive possession or use” of any particular part of SSC’s facilities, nor do the patients; the patients pay SSC for medical procedures performed based on a CPT-based fee schedule (not use of any particular room or other specified space within SSC), and the temporary possession or use of a particular room in SSC’s facilities is incidental to SSC’s primary business of providing medical services. Moreover, the definitions for “renting” and “leasing” are measured by time, whereas SSC bills based on procedure; *i.e.*, SSC does not bill for time spent in its facilities or number of Band-Aids used, but rather bills the patient/insurance company (not the physicians) for procedures the physicians perform.

Take a typical case. A patient shows up for his/her procedure. He/she checks in in the waiting room with other patients, where he/she stays until brought in to the interior space; he/she then spends time being prepped in space used for that purpose; he/she is then wheeled into a room where the procedure is performed; and he/she is then taken to a recovery room, again where other patients are recovering from their procedures, until he/she is released.

So let’s do the analysis: (1) Who is the “renter” or “lessee”? It can’t be the physician; the physician does not pay anything to the surgery center, does not have the center or any particular portion of the center to himself/herself, and can’t exclude SSC personnel. It can’t be the patient, either, as the patient didn’t book the procedure, did not negotiate the charges, did not ask for or receive a particular space, or anything else that renters commonly do. (2) What are the demised premises being “leased” or “rented”? The waiting room? The pre-op room? The surgery space? The recovery room? There is no exclusive possession; there are no designated premises that were agreed upon. In short, again, there is a total absence of what would be expected in a rental or lease agreement. (3) What is the term of the “lease” or “rental”? There is none; the procedure and recovery take as long as they take, and the charge is the same for that procedure without regard to the time taken. (4) What is the “rent”? A single fee is charged. No amount is paid for the use of the space itself.

The truth is that as the City recognized as far back as 2004, the Code does not properly identify what a surgery center does as falling into Classification F. Instead, the City is trying to

“shoehorn” SSC’s business into a category which clearly does not fit. SSC is not “leasing” or “renting” commercial property under any definition, whether Code, legal, or common sense.

What is the nature of the arrangement, then? *At most* (for the City), it is a *license*.³ A license is a non-possessory, revocable right to use another person’s real estate, called a *servient tenement*; it is a personal privilege held by an individual. Cal. Real Estate at 10; *Beckett v. City of Paris Dry Goods Co.*, 14 Cal. 2d 633, 637 (1939) (license is a personal, revocable, and non-assignable permission to do one or more acts on the land of another without possessing any interest therein); *Spinks v. Equity Residential Briarwood Apartments*, 171 Cal. App. 4th 1004, 1040 (2009) (“A ‘license’ is a personal, revocable and generally non-assignable privilege conferred (either orally or in writing) to do a particular act (or acts) upon the land of another. It is a non-possessory right to use the property as specified between the parties.”) (internal citations omitted, emphasis added); *Qualls*, 76 Cal. App. 4th at 1283 (whether an agreement for the use of property constitutes a license or a lease generally is determined by the nature of the possession granted; if the contract gives exclusive possession of the premises against all the world, including the owner, it is a lease, but if it merely confers a privilege to occupy the premises under the owner, it is a license); *Jensen v. Hunter*, 5 Cal. Unrep. 83, 90 (1895) (license is an authority to do a particular act, or a series of acts, upon another’s land, without possessing an estate therein).

Here, when a doctor uses the center’s facilities, suite, he/she is, at most, granted the privilege to use a suite, recovery room, etc. (but not exclusive possession of the center or suite against all the world), thereby creating, at most, a license, not a lease. Cal. Real Estate at 10 (a license is the nonexclusive right given to an individual to use a space or area within a parcel of real estate, or its improvements, that belong to another person); *Covina Manor, Inc. v. Hatch*, 133 Cal. App. 2d Supp. 790, 793 (1955) (license is an authority to do a particular act or series of acts upon the land of another, and conveys no estate in the land). In other words, the physicians and patients are merely granted the privilege to occupy the premises for a specific act (the medical procedure), and neither the physician nor the patient has the right of exclusive possession against the owners of the surgery center.

Indeed, unlike in a lease arrangement, the doctors here do not have anything formalizing an agreement between them and the surgical center (let alone anything that would convey an intent to have a landlord/tenant relationship), the doctors do not pay rent to the surgical center, the doctors do not have exclusive use of any part of the surgical center, the doctors have no right to exclude others from the surgical center, and the doctors have no termination date for use of the surgical center. *Cf.* Cal. Real Estate at 10-11 (characteristics which distinguish a license from a lease include (1) no writing to formalize the agreement; (2) no rental payment; (3) no specific location on or within the property where the use will occur;

³ SSC contends that not even a “license” arrangement exists.

(4) no intent to convey a leasehold estate; (5) no right to exclude others; (6) no termination date; (7) termination at the owner's will, unless the license is irrevocable.). Consequently, there is, at most, a licensing of the premises, not a leasing or renting of the premises (7 Cal. Real Est. §19:1 (3d ed.) (Lease as personal property or real property); *Qualls*, 76 Cal. App. 4th at 1283; *Spinks*, 171 Cal. App. 4th at 1040-41 (2009)).

Moreover, a license is neither personal property nor real property, and it is neither owned by a person nor appurtenant to adjoining real estate. Cal. Real Estate at 10. Thus, a license—not being property or capable of ownership—cannot be transferred to the licensee's successors or assignors. *Id.*; see *Beckett*, 14 Cal. 2d at 639. The right to use is held by an individual under an agreement, without the rights to assign or to privacy. Cal. Real Estate at 10. Therefore, SSC could not possibly be engaged in the "business of renting or leasing commercial property" because it has no personal or real property to rent or lease; *i.e.*, the doctors only have a "personal privilege" to perform medical procedures at the surgical center by use of their license.

By its very terms, Classification F only applies to taxpayers "engaged in the business of leasing or renting commercial property." It does **not** apply to taxpayers who **license** others to use commercial property. Thus, to subject such taxpayers to a gross receipts tax, the Code would need to be amended—and approved by the voters.

If the City's position were correct, movie theaters would be "renting" or "leasing" commercial space to viewers by letting them sit in the theater to watch the movie. Gyms would be "renting" or "leasing" space to their members. Lawyers would be "renting" or "leasing" space to their clients who sit in their conference rooms. Indeed, taken to the extreme, a department store would be "renting" or "leasing" its space to its customers, as no doubt a part of the purchase price of the goods sold defrays the store's real estate expense. The Code does not, and cannot be stood on its head to so provide. Clearly this was not the intent of the City in enacting the Code, or else the Code would have explicitly said so. And it is well-recognized that in considering a classification for taxation purposes, courts look to the "burden placed upon the community in relation to the particular classifications." *Clark v. City of San Pablo*, 270 Cal. App. 2d 121, 133 (1969).

If MBIA had not been commissioned to come up with new ways to raise revenue, this issue would not exist. Why? Because as the Deputy Director recognized, no one—including the City—read, or would have read, the Code to provide that a surgery center is a commercial landlord. To say that it is, and that the Code says that it is, is disingenuous.

II. SSC is not in the business of leasing or renting of surgical suites

Next, even if there were a lease or rental (there is neither), SSC cannot be found to be “engaged in the business of leasing or renting any commercial property.” The surgical centers are owned by either doctors or medical corporations engaged in the business of rendering medical services, which is distinguishable from a landlord/tenant relationship. Any “renting or leasing” is incidental to the core business of providing medical service such that SSC is not “engaged in the business” of leasing. In other contexts, to be engaged “in the business of” an activity, such activity must be a regular part of the primary business. *See, e.g., Travelers Indemnity Co. v. Maryland Casualty Co.*, 41 Cal. App. 4th 1538, 1546-47 (1996) (in determining whether an insured is “engaged in the business of renting or leasing” motor vehicles without operators, the court considers the plain language of the statute, and considers whether the renting or leasing activities is “a regular part of the insured’s business”) (overruled on other grounds in *Sentry Select Ins. Co. v. Fidelity & Guaranty Ins. Co.*, 46 Cal. 4th 204 (2009)). Here, the “renting or leasing” is not a regular part of SSC’s (or the physicians’) business; rather they are regularly engaged in providing medical services. This is supported by the fact that SSC bills for only medical procedures and not time or space, and the fact that the bills go directly to the patients.

II. Great weight should be given to the consistent construction of the ordinance not to include Classification F

As the present dispute demonstrates, the explicit language in Classification F is, *at best* for the City, ambiguous. It is well settled that when the meaning of an ordinance is ambiguous and cannot be determined from its plain meaning, great weight should be given to long standing and uniform construction of that ordinance.

Here, SSC has been in Beverly Hills since 1998. And until when notice was given in December 2005, the City of Beverly Hills had never attempted to tax SSC (or other surgical centers in Beverly Hills) in the manner that the City is currently attempting to extend its Code. Indeed, it has consistently interpreted the surgical centers to fit only in Classification C (not F). Therefore, the City’s consistent interpretation of the Code for the last decade or so should be given deference and accepted as the interpretation of the Code. Indeed, as Mr. Davis’s January 21, 2005 memo (Ex. 3) acknowledged, not a single surgery center had ever reported itself as a Classification F business, and the City had never taxed one as such.

In *Mason v. Retirement Bd. of City & Cty. of San Francisco*, 111 Cal. App. 4th 1221, 1228 (2003), city and county employees filed petitions for writ of mandate and complaints for declaratory relief against the city and county retirement board, challenging the legality of the board’s exclusion of postretirement cash payments for unused vacation and sick leave from computation of retirement benefits. In affirming the lower court’s granting of summary

judgment to the board, the Court of Appeals for the First District of California stated the following:

Our conclusion is supported by several rules of statutory construction. Foremost among them is the rule that courts must give great weight and respect to an administrative agency's interpretation of a statute governing its powers and responsibilities. Consistent administrative construction of a statute, especially when it originates with an agency that is charged with putting the statutory machinery into effect is accorded great weight. Such deference is particularly warranted when an agency's interpretation is of long standing. This rule is supported by practical considerations. When an administrative interpretation is of long standing and has remained uniform, it is likely that numerous transactions have been entered into in reliance thereon, and it could be invalidated only at the cost of major readjustments and extensive litigation.

Id. (internal citations and quotations omitted) (concluding that "the Board's decades-long, consistent interpretation of the charter provisions is entitled to substantial deference"); *Gerard Ste. Marie v. Riverside Cty. Regional Park & Open-Space District*, 46 Cal. 4th 282, 292 (2009) (where court held that consistent administrative construction of a statute, especially when it originates with an agency that is charged with putting the statutory machinery into effect, is accorded great weight in a court's statutory interpretation); *Whitcomb Hotel, Inc. v. Cal. Emp. Com.*, 24 Cal. 2d 753, 757 (1944) ("When an administrative interpretation is of long standing and has remained uniform, it is likely that numerous transactions have been entered into in reliance thereon, and it could be invalidated only at the cost of major readjustments and extensive litigation."). This is particularly true when, as here, the ordinance was not amended to give it the meaning the City is now contending. See *Horn v. Swoap*, 41 Cal. App. 3d 375, 382 (1974) ("If the Legislature . . . makes no substantial modifications to the act, there is a strong indication that the administrative practice was consistent with the legislative intent."); *DeYoung v. City of San Diego*, 147 Cal. App. 3d 11, 18-19 (1998) (*overruled on other grounds*).

But even if the City argues that its administrative interpretation of the Code was not of long standing, or that it had never interpreted the Code on this issue at all, that would not help the City here. For a City certainly may not interpret and apply an ordinance differently from the way it had previously done in the past in such a way as to increase taxes; as noted previously, that would violate Proposition 218. A first-time interpretation of a statute in a way that raises taxes is unconstitutional, particularly where the interpretation is, as here, inconsistent with the plain language of the statute as an ordinary taxpayer would understand it.

III. CONCLUSION AND REQUEST FOR RECUSAL

For the reasons set forth above, SSC believes that the Assessment is entirely improper. On every level—constitutional, statutory and case law, factual, and just plain common sense—the City’s attempt to call a camel a horse so it can obtain increased taxes is inappropriate and wrong. SSC does nothing more than provide the means by which doctors can perform medical procedures and provide the professional and semi-professional services, equipment, and supplies to enable them to do so. The Code does not classify licensing as Class F. The Assessment should be rescinded so that litigation—which the City has already commenced—can be avoided. As this letter demonstrates, such litigation is baseless and lacks probable cause. The issue should end now.

On a procedural note, SSC notes that the March 26, 2012 letter informing SSC of the April 12, 2012 hearing date in this matter was sent by Noel Marquis—the Deputy Director whose memorandum acknowledges the deficiencies in and vagueness of the Code but who nonetheless advocated the “quicker and easier” alternative to the appropriate means of dealing with the problem (a Code amendment). Mr. Marquis’s writing, and his conduct, are thus front and center in this dispute. Under these circumstances, it is inappropriate that he be participating in, much less the hearing officer for, the determination of this appeal, as SSC is not likely to get a fair hearing under such circumstances. SSC therefore respectfully requests that the hearing on this appeal be presided over and determined by someone with no vested interest in the outcome beyond, of course, the obvious interest that a City employee has in upholding an action by the City.

Very truly yours,



Allan Cooper

cc: Phil Starr, Ervin Cohen & Jessup LLP
Laurence S. Wiener, City Attorney
Kayser Sume, City Attorney’s Office
Mitchell E. Abbott, Esq.

EXHIBIT "1"



MuniServices Company

FRESNO ♦ SACRAMENTO ♦ WESTLAKE VILLAGE ♦ WASHINGTON DC ♦ DETROIT ♦ PHILADELPHIA

LOCAL TAX COMPLIANCE DIVISION

EXTERNAL MEMORANDUM

TO: NOEL MARQUIS
FROM: JOSHUA DAVIS
SUBJECT: SURGERY CENTER/DOCTOR TAXATION
DATE: 10/01/2004
CC:

I have reviewed the ordinance and done some minimal research on the inter-net of some surgery centers in Beverly Hills. Obviously, the doctor and/or surgery center must be registered with the City and pay the tax. However, as you suspected, there is a probability that these entities are conducting multiple taxable activities from their office.

We would utilize the same logic used during the course of the beauty salon review conducted. Beauticians were paying a flat per-employee fee and conducting activities that were taxable as gross receipts under your tax code. Sec 3-1-208 of the BHMC requires an entity to register for each taxable activity that they conduct. So in the nature of the salons, a barber needs to have "A" class registration for cutting hair, a "B" class registration for selling shampoo, and an "F" class registration for subletting space to independent contractors.

This same logic can be applied to doctors and surgery centers throughout Beverly Hills. For example; A doctor who performs a breast augmentation procedure would charge a fee for the procedure, a separate fee for the use of the facilities, and in most cases would charge a separate fee for the implant itself. The procedure fee would obviously be covered under the doctors "C" class registration, however, the practice of itemizing and selling the implant could subject the doctor to a "B" class registration.

There are a number of other taxable activities and entities that may be associated with that location. There may be a cooperative of doctors that manages the facility, and if a separate entity, then they would also be required to have a separate registration. Also, there are a lot of independent and transients that work from surgery centers. Anesthesiologists, are usually independent contractors that only work from the location when there are procedures, and usually charge a separate fee to the patients.

While there are many instances where a business may be subject to multiple taxation classifications, the nature of the doctors fixed fee classification could cause some issues. If all of the taxable activity were to be taxed on gross receipts, it would be easy to

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allocate a portion of the gross between multiple classifications. However, since the "C" class is not based on gross receipts, a doctor may argue that the activities he is conducting are part of his professional business activity and, while they may be subject to taxation, are covered under the "C" class registration

I believe that the best course of action is to conduct a review of a randomly selected entity. As has been the case in our previous audit endeavors, starting with a test case helps MMC and the City better understand how the industry is operating and what the main taxable activities are. Once completed, MMC can submit to the City a review of the taxation issues discovered and the legal or political impact that may arise.

EXHIBIT “2”



CITY OF BEVERLY HILLS
ADMINISTRATIVE SERVICES
INTEROFFICE COMMUNICATION

October 11, 2004

TO: Honorable Mayor and City Councilmembers
FROM: Noel Marquis, Deputy Director Administrative Services
SUBJECT: Surgical Center Business Tax Issues

BACKGROUND

Recently, questions were raised by Councilmember Webb as to the application of business taxes on surgical clinics in the City of Beverly Hills. For the purpose of this report there are several issues staff will attempt to address:

- First, there exists a question as to the equity of the contribution from flat rate per employee tax categories when compared to gross receipts tax categories.
- Secondly, there is a question as to whether the nature of surgical centers is sufficiently different from "normal" medical practices to warrant their own business tax classification. The more immediate concern is whether surgery centers or clinics pay an appropriate amount under the existing Municipal Code or even if the existing Code allows for proper identification and taxation of these businesses. Specifically, such operations may be more akin to hospitals, with multiple revenue streams that differ substantially from a typical medical or other professional practice. While this issue could be addressed through a change to the Municipal Code sections related to business tax staff believes there may be other more effective alternatives.

Within this report staff will attempt to address each of the above issues and present sufficient information such that a decision can be reached. Staff's analysis will include opportunities for additional revenues within the existing Code and opportunities for Code amendment.

Honorable Mayor and City Councilmembers
Surgical Center Business Tax Issues
October 11, 2004

On the issue of Flat Rate Tax:

In prior analysis of the flat rate tax categories, staff determined that this tax basis (flat rate per employee) has an inherent inequity. As example, a professional who bills clients \$100 an hour pays a much higher tax rate, as a percentage of gross receipts, than a professional who bills clients \$500 an hour. In this example each professional would pay \$1,095.41 for the current calendar year. Let's assume just the professional who works and bills 2,080 hours a year. The professional who bills \$100 an hour would pay 0.0053 cents per dollar of gross receipts as compared to the \$500 per hour professional who would pay 0.0011 cents per dollar of gross receipts. The lower billing professional pays nearly 5 times the tax rate as the higher billing professional.

For comparison, retail businesses pay 0.00125 cents per dollar of gross receipts, residential landlords pay 0.012 cents per dollar of gross receipts and commercial landlords pay 0.0235 cents per dollar of gross receipts. Further, this inequity has a tendency to increase over time. Gross receipt tax revenues generally tend to grow by the overall business growth of an area and category while flat rate taxes, at least under the Beverly Hills Municipal Code, increase annually by the CPI. An example of how the difference in the revenue derived from gross receipt and flat rate taxes will illustrate the change over a 5 year period. For our example we will assume that business activity grows by 5% a year over the CPI. The retail business that pays \$1,095 today will pay \$1,435.32 in 5 years while the professional who pays the same amount today will pay \$1,185.26 or \$250.06 less.

As we saw the last time this issue was raised, there would likely be vehement opposition. At that time, a good part of the expressed concern was the inappropriateness of providing gross receipts information. That appeared to be a "red hearing" insofar as the information, such as that currently provided by retailers and landlords, is confidential. A secondary concern was the potential unintended consequence of taxing "pass through" revenues such as client monies received into trust funds. Staff does not feel either issue would create an administrative problem. Taxes on professionals are based upon gross receipts in many jurisdictions, including Los Angeles and Santa Monica.

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October 11, 2004

The real issue is that many professionals would pay much more than they do under the existing code. This seems all the more obvious given the rapid increase in professional service fees in the intervening 15 years.

On the issue of the nature of surgical centers:

After a preliminary review of the facts by staff of Administrative Services, some initial conclusions have been reached. Specifically, staff believes that surgical centers, like many businesses reviewed, should be classified in multiple categories. Often, businesses involved in multiple categories of business activity fail to properly register and pay their business tax. This is often because the business is unaware that they are involved in multiple activities.

Beverly Hills Municipal Code Section 3-1.208 requires businesses to register and pay tax in each category in which they conduct business. For example, beauty salons are required to register in category A, services under which they pay a flat rate per employee. However, many beauty salons also sell retail hair care products requiring registration in category B. Further, salon owners often rent salon space to independent contractor beauticians requiring registration in category F. Similarly, most of our major hotels are registered in and pay taxes for multiple categories (commercial leasing, residential leasing, retail sales, restaurants, spa services, etc.). Other professional businesses have been found, during audits, to require registration in multiple categories. Many Pharmacists and Optometrists/Ophthalmologists have been found to engage in retail activity and therefore require registration in both category C and category B (retail sales). (Generally speaking prescription sales of drugs and corrective lenses are not separately taxable. However, sales such as over the counter medicines, sunglasses and frames and other goods are subject to separate business tax categories and taxation.)

The fact that doctors, like most professionals, tend to bill their clients for each type of service provided should make determination of the business activities and appropriate registration fairly straightforward. For example, a patient who has heart surgery would most likely receive a bill for the surgeons services, the hospital or surgical suite, service of an anesthesiologists, supplies used, x-rays and so on. From this

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bill staff could determine that the following separate and taxable business activities had taken place:

- The service of the surgeon - class C - professional services.
- The rental of the surgical suite - class F - commercial rental.
- Supplies used - class B - retail sales.
- X-rays - class C - professional services.
- Services of the anesthesiologists - class C - professional services.

Continuing with this analysis, a surgical center that provided a billing service for a participating group of surgeons and charges a percentage of the amount billed for the services provided would be conducting business in class G (as an agent). Further, these various levels of taxation can be applied under the existing Municipal Code regardless of whether the revenue in question is derived from an insurance company, Medicare/Medical or directly from the patient.

RECOMMENDATION

Staff is not opposed to placing a measure on the ballot to create a new category, change the measurement focus of the existing category (i.e. to gross receipts) or change the tax requirements. However, it appears a quicker and easier option may exist. At present, and based on the information at hand, staff recommends that audits of several surgical centers and similar types of businesses be conducted to determine the potential level of tax liability this approach would produce.

Please note that if a measure is to be placed on the March ballot the City Council must act by December 10, 2004.

Staff will be happy to provide additional research or information as needed.

Noel Marquis

EXHIBIT "3"



MuniServices Company

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LOCAL TAX COMPLIANCE DIVISION

EXTERNAL MEMORANDUM

TO: NOEL MARQUIS
FROM: JOSHUA DAVIS
SUBJECT: SURGERY CENTER/DOCTOR TAXATION
DATE: 01/21/2005
CC:

In the initial review of the surgery centers in Beverly Hills, MMC found the following example to be a common practice among the Surgery Centers in Beverly Hills:

Background

Activities

The Doctor's perform plastic surgery for the face; breast, thighs, legs, buttocks and reconstructive surgery. A fee is charged for the Doctor's services and then a separate fee is charged to the patient for the surgical room. The charge for the room includes all of the items used during the surgery. A lump sum is charged for the room, nothing is itemized. The doctor will also in certain situations sell products to the patient for skin care or other post-op needs.

Employees

The employees of the doctors are several nurses and a few clerical employees. All procedures are only day procedures. If a patient needs to stay overnight then they are sent to a local hotel.

The anesthesiologist used for the procedure is independent of the doctor. The anesthesiologist gets paid either by the patient or by the insurance. On occasion the Doctor will rent out his surgery center to another doctor. The rental of the surgery center includes the nurses and staff that the Doctor (Owner) has working there.

Ownership Structure

The owner of the surgery center is not the doctor personally. Typically each doctor has two corporations at each location. One corporation is for his medical practice, and the other for the Surgery center itself.

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Taxation

Based on the common practice among the surgery centers it appears that there is potential liability to the City of Beverly Hills and that the industry as a whole is under-reporting their tax liability as well as not registering for all required taxes. Each entity has separate issues ranging from under-reporting the "C Class" number of professionals & semi-professionals, to conducting multiple taxable activities.

Commercial Rental

The first issue that stands out is the potential liability for an "F Class" registration for the doctors who are renting the surgery centers to other doctors. Since the surgery center is being rented, the doctor must pay on the gross receipts received for the rental.

Additionally, the doctor is renting staff as a part of the transaction. This is also leasing employees which gross receipts are taxable under a "G class" registration.

At this time, we have not encountered an entity that is properly reporting this income.

Retail Transactions

Another Potential liability identified is a "B class" Registration for the doctors who are selling tangible goods from their office. The gross receipts from the sale of skin care products, crutches, wheel chairs, etc., and potentially implants, must be reported separately on a "B class" registration.

While MMC has not identified surgery centers at this time that are itemizing charges to their patients, we believe that there may be some entities that are receiving income from itemized charges to their patients. Additionally, MMC is researching the possibility of taxing an estimated amount of the lump-sum charge that relates to the goods sold.

At this time, we have not encountered an entity that is properly reporting this income.

Non-Related Business Entities

The "Out of City" doctors who are renting the surgery centers from the local doctor are also liable for their own "C Class" registration if they aren't registered in the City. Additional obligations for the "B Class" are also applicable as indicated for the primary operator of the center. These accounts will be researched for appropriate registrations once they have been identified during the course of the review of the primary entity.

EXHIBIT "4"

CALIFORNIA CONSTITUTION
ARTICLE 13C [VOTER APPROVAL FOR LOCAL TAX LEVIES]

SEC. 2. Local Government Tax Limitation. Notwithstanding any other provision of this Constitution:

(a) All taxes imposed by any local government shall be deemed to be either general taxes or special taxes. Special purpose districts or agencies, including school districts, shall have no power to levy general taxes.

(b) No local government may impose, extend, or increase any general tax unless and until that tax is submitted to the electorate and approved by a majority vote. A general tax shall not be deemed to have been increased if it is imposed at a rate not higher than the maximum rate so approved. The election required by this subdivision shall be consolidated with a regularly scheduled general election for members of the governing body of the local government, except in cases of emergency declared by a unanimous vote of the governing body.

(c) Any general tax imposed, extended, or increased, without voter approval, by any local government on or after January 1, 1995, and prior to the effective date of this article, shall continue to be imposed only if approved by a majority vote of the voters voting in an election on the issue of the imposition, which election shall be held within two years of the effective date of this article and in compliance with subdivision (b).

(d) No local government may impose, extend, or increase any special tax unless and until that tax is submitted to the electorate and approved by a two-thirds vote. A special tax shall not be deemed to have been increased if it is imposed at a rate not higher than the maximum rate so approved.

EXHIBIT B



Noel Marquis, Assistant Director,
Administrative Services – Finance

Decision and Findings in re:
Business Tax Assessment Hearing

Specialty Surgical Center, LLC and
Specialty Surgical Center of Beverly Hills, L.P.

Hearing Date: April 11, 2012 (continued through May 15, 2012 for
submission of supplemental material)

Taxpayers: Specialty Surgical Center, LLC (not in attendance) and
Specialty Surgical Center of Beverly Hills, L.P. (not in
attendance)

Hearing before: Noel Marquis, Assistant Director
Department of Administrative Services

Also in Attendance: Patrick K. Bobko, Esq., City Attorney's Office
Allan Cooper, Esq., Ervin, Cohen & Jessup
Phil Starr, Esq., Ervin, Cohen & Jessup
Pantea Yashar, Esq., Ervin, Cohen & Jessup

I. Summary of Assessment History

Taxpayers Specialty Surgical Center, LLC and Specialty Surgical Center of Beverly Hills, L.P. (hereafter collectively "Specialty") operate outpatient surgery centers in the City of Beverly Hills ("City"). The City began investigating Specialty's operations a number of years ago and has conducted numerous discussions with its counsel and employees. As recently as August of 2011, City representatives met with

representatives of Specialty's management and ownership to exchange information regarding Specialty's operations.

There is little dispute regarding the specific facts of Specialty's operations. Instead, Specialty disputes the City's analysis and administrative treatment of those facts under controlling provisions of the Beverly Hills Municipal Code ("BHMC" or "Municipal Code").

Based on information Specialty provided to the City, the City informed Specialty that it determined Specialty was required to register and pay business taxes in the City's Classification "F" ("Class F") for registrants "engaged in the business of leasing or renting any commercial property." (BHMC Section 3-1-219). Specialty has objected to this determination and refused to register in Class F.

On January 9, 2012, the City issued an assessment for business taxes due in and for calendar years 2003 through 2011. On January 18, 2012, Specialty, through its counsel Ervin, Cohen & Jessup, requested a hearing on the assessment pursuant to BHMC Section 3-1-213.

The City scheduled and conducted a hearing on the assessment on April 12, 2012, before Noel Marquis, Assistant Director of Administrative Services. No representatives of Specialty appeared at the hearing. Instead, Specialty was represented by its counsel, Allan Cooper, Phil Starr and Pantea Yashar of Ervin, Cohen & Jessup. Specialty presented argument at the hearing as to why it believes it was not required to register and pay taxes in the City's Class F.

During the hearing, Mr. Marquis offered to maintain the hearing open until April 20, 2012, for the purpose of allowing Specialty to submit any additional documentation that it would like considered. At Specialty's request that deadline twice was extended to maintain the hearing open for supplemental document submission: first to April 27, 2012 and subsequently to May 15, 2012. Specialty submitted a letter brief ("Hearing Brief") dated April 12, 2012, which was received by the City on April 13, 2012. Further, Specialty submitted a letter dated May 8, 2012, which was received by the City on May 9, 2012, and which contained information on Specialty's gross receipts. Specialty made no further supplemental submissions, and the hearing closed on May 15, 2012.

II. Documents Considered in Regard to Assessment and Hearing

The City has considered all correspondence and documents exchanged by Specialty or its counsel and the City, including, without limitation, the following:

Letter brief dated April 12, 2012, from Ervin, Cohen & Jessup

Letter dated May 8, 2012, from Ervin, Cohen & Jessup

III. Summary of Taxpayer Operations and Arguments

The salient facts of Specialty's operation are not materially in dispute. Specialty operates two outpatient surgery centers. The centers provide fee-based surgical facility space for independent doctors to perform certain types of surgeries on their patients. These procedures do not require overnight recovery stays.

The doctors that perform the surgical procedures are not employed by Specialty. They maintain their own separate practices. When the doctor determines in his or her professional judgment that a surgical procedure is warranted, the doctor arranges with their patient to perform that procedure at Specialty's facilities. The doctor's office schedules the procedure at Specialty's facilities and provides Specialty the patient's name and medical information. (Hearing Brief, at p. 2.) Specialty, in turn, confirms that the patient has insurance, or other medical care coverage such as Medicare, that will pay Specialty's fee.

On the day of the surgery, the patient arrives at Specialty's facility and completes an admission process. Prior to the surgery, the patient may be attended to by a nurse. These nurses may be employed by Specialty or they may be independent contractors. The doctor separately arrives at Specialty's facility and performs the scheduled surgery in one of Specialty's surgical facilities. After the surgery is completed, the patient is taken to a recovery room, where he or she typically is attended to by a nurse who may be employed by Specialty. Upon appropriate recovery, the patient is discharged.

The patient is billed separately for both components of the procedure. The doctor charges a professional fee for his surgery (as do other physicians necessary to the procedure, such as an anesthesiologist). Independently, Specialty charges a facility fee for the procedure. These charges typically are paid directly by the patient's insurance at rates contracted with the charging party. Thus, Specialty has contracts with insurers that set a schedule of fees for different surgical uses of its facilities.

Specialty provided City staff the foregoing description of its operations, which description is consistent with the facts as described in Specialty's Hearing Brief. Based on these facts, the City determined that Specialty's business function is to provide surgical facility space for a fee. In this space doctors, who are not employed by Specialty, will perform surgical procedures upon patients that have no relationship to Specialty other than having been instructed by their doctors to appear at Specialty's facilities at a certain time.

To date, Specialty has registered its business and paid taxes in the City's Classification "C" ("Class C") for "professions and semiprofessions" as provided in BHMC Section 3-1-219. Such registration is proper because Specialty employs a number of nurses to provide care in aspects of the patient stay at Specialty's facility. Such services, however, are not the dominant, or even a substantial, component of the

facility product Specialty provides. Instead, they are supplemental services that support Specialty's core function of providing the surgical facility space in which doctors and patients can complete a surgical procedure.

BHMC Section 3-1-208(a) requires every business to register in, and pay a tax for, each type of business it performs. That section provides, in relevant part, as follows:

"Unless otherwise provided in this article, every person who engages in any business within the city must register with the department of finance administration and pay a separate business tax for:

* * *

2. Each type of business as set forth in section 3-1-219 of this article which a registrant conducts at every primary and branch establishment within the city."

In short, the registration and payment of business tax in multiple classes is required where a taxpayer engages in different types of business defined by the City's business classifications.

The City's Municipal Code places the "administrative function" of determining a business' classification upon city staff. (BHMC Section 3-1-212). Exercising that function, the City has determined that Specialty's dominant business activity – provision of surgical facility space for a fee – falls within Class F for "leasing or renting any commercial property."

During both the City's investigation and the assessment hearing, Specialty has denied that it is required to register in business tax Class F. Although cast in various forms, Specialty asserts two basic arguments in support of its position. First, it asserts (incorrectly) that the City has changed its administrative policy for the improper purpose of raising Specialty's taxes in violation of the California Constitution as reflected in the amendment passed by the voters as Proposition 218. Second, it asserts that as a definitional matter its operations do not fall within the terms of business tax Class F. Specialty's arguments are set forth in its Hearing Brief and are not repeated herein.

IV. Analysis of Specialty's Arguments Against Assessment

A. Administrative Investigation and Tax Classification Determination.

Specialty devotes a significant portion of its Hearing Brief attempting to mischaracterize the City's investigation and tax classification determination as a purposeful decision to change the tax treatment of surgery centers. In so doing,

Specialty relies heavily upon the fact that it always has registered only in Class C, but does not critically evaluate whether such a single class registration was appropriate. Specialty's argument essentially reduces to the assertion that the City should have discovered its incomplete registration earlier.

Specialty's argument fundamentally ignores the fact that the City's business tax is a self-reported tax. Under the Municipal Code, Specialty has the obligation to register in each defined classification in which it transacts business and to voluntarily report the appropriate measurement focus for such classification, *i.e.*, payroll hours for Class C and gross receipts for Class F. As with most taxes, the City has the right to investigate and audit taxpayers and, if necessary, assess additional taxes where registration and reporting have not been completed properly. There is no process, nor is there any requirement, for the City to analyze each taxpayer and its registration form for accuracy when filed each year.

Surgery centers are relatively new businesses. The nature of their operations is not generally known by the public and business models differ even among surgery centers. Until the City investigated Specialty, the City did not know the role Specialty played in the outpatient surgical process and that such role consisted of providing surgical facility space for a fee so that independent parties could perform surgical procedures. Once these operations were investigated the City determined that Specialty was required also to register in business Class F.

Specialty produced no evidence at the hearing (because none exists) that the City previously investigated Specialty, or similarly operated businesses, and determined that a single Class C registration for business tax was appropriate. Specialty's argument that the City changed its position to require multiple business class registration lacks the necessary predicate: evidence that the City ever took or endorsed the position that a single Class C registration was appropriate. The City took no position on Specialty's operations or its self-reported tax until the City investigated.

BHMC Section 3-1-208(a) plainly requires multiple tax classification registration where a taxpayer performs multiple defined business activities. The City's determination that registration in multiple tax classifications was appropriate simply applies pre-existing requirements of the City's Municipal Code. Specialty's repeated references to its filing of a single Class C registration for many years reflects nothing more than a pattern of non-compliance. The City's discovery of this non-compliance and subsequent assessment constitutes routine enforcement of the Municipal Code that rationally cannot be construed as a "change" of position.

Absent a change in position, Specialty's claim that the assessment violates the California Constitution as reflected in Proposition 218 carries no weight. Specialty cites as support the opinion in *AB Cellular LA, LLC v. City of Los Angeles*, 150 Cal.App.4th 747 (2007) involving utility taxation of cellular service. In that case, the City of Los

Angeles initially prepared and circulated to taxpayers a formal written position excluding certain transactions from taxation. That policy was submitted to the Los Angeles City Council for review in connection with other City decisions. The City of Los Angeles subsequently sought to reverse its position and tax the previously excluded transactions in response to federal legislation that it believed sanctioned broader taxation of cellular service. The Court of Appeal ruled that such a change in officially sanctioned methodology constituted an increase in taxation and required a vote for approval.

The facts of *AB Cellular* are critically different from the issues herein and undercut Specialty's arguments. The City has never issued any policy or instruction to Specialty sanctioning single Class C registration for Specialty; this observation absolutely precludes any possibility for a "change in methodology." Unlike *AB Cellular*, where the City of Los Angeles changed exclusions affecting the computation of taxable transactions within a utility tax framework, the City's methodology here is and has always been consistent: Taxpayers that transact businesses in two classes must register and pay taxes in each. Here, Specialty must (i) register and pay a per employee tax for Class C professionals and (ii) register and pay a gross receipts tax for Class F leasing or renting of commercial space. Contrary to Specialty's assertion, what has changed is not the City's treatment or the methodology of tax computation in the respective classifications, but rather, the fact that the City discovered Specialty's failure to properly register.

Specialty's numerous references to extraneous facts, and its accusations of improper motives, do not alter the analysis above. For example, Specialty accuses the City of investigating it and assessing additional taxes in order to increase revenue. That observation is irrelevant because BHMC Section 3-1-201(c) states in relevant part, "The required business tax is imposed pursuant to the taxing power of the city of Beverly Hills solely for the purpose of obtaining revenue." One of the main purposes of the City's power to investigate and assess is precisely to recover revenue due to the City but unpaid because taxpayers (such as Specialty) have failed to properly register and have underpaid their taxes.

Specialty's references to the fact the City staff considered an option of creating a new surgical center classification is similarly irrelevant because the City had no obligation to do so. City staff's consideration of alternatives is a prudent analytical step and the creation of a new tax classification could have addressed many concerns not at issue here, such as utilizing an alternate tax measurement focus for such a hypothetical class. Ultimately, staff concluded that multiple class registration within the existing classifications was appropriate. Whether Specialty would prefer a separate surgical center class is irrelevant.

In sum, Specialty has introduced no evidence that the City ever disseminated any official position that single Class C registration was appropriate for operations such

as those Specialty conducts. Hence, there has been no improper “change” of position. Specialty’s attempt to buttress its incomplete argument with extraneous observations does not alter this analysis.

B. Specialty’s Operations Fall Within the Terms of Class F for Leasing or Renting of Commercial Property.

Specialty argues alternatively that even if the City has not engaged in an improper change of policy, Specialty nonetheless is not obligated to register in Class F because its operations do not constitute “leasing or renting” of commercial property. To this end, it makes a number of strained definitional arguments. More importantly, it wholly ignores the fact that its sole reason for its existence is to provide surgical facility space in exchange for a fee.

The analysis of Class F begins with its own language, which applies to taxpayers in the business of “leasing or renting” commercial property. Specialty spends considerable effort in its Hearing Brief attempting to conflate the two terms with the intent of limiting the classification with concepts that apply predominantly to leasing. This approach, however, ignores the plain language that sets forth these two terms in the disjunctive. Use of the term “or” indicates the definition is intended to apply beyond whatever Specialty may consider to be formal leasing to the more general concept of “renting.” Assuming for the sake of this analysis only that Specialty’s activities do not fall within the concept of “leasing,” such activities clearly fall within any ordinary understanding of the term “renting.”

In common usage, the term “rent” ordinarily is understood as compensation or a fee for the use of property. The transaction or arrangement whereby people exchange this consideration is known as “renting.” Consistent with this observation, Black’s Law Dictionary (cited by Specialty) defines rent as: “Consideration paid, usu. periodically, for the use or occupancy of property (esp. real property).”

The two critical components of rent and renting are (i) “consideration” that is exchanged for (ii) “use” of property. Specialty’s operations satisfy both requirements.

There is no reasonable dispute that Specialty receives consideration in its transactions. The “Facility Fee” it charges for the use of its facilities forms the gross receipts that are the subject of the City’s assessment. Specialty even concedes on the second page of its Hearing Brief that at the time a procedure is scheduled, its staff confirms that Specialty has a contract for payment with the patient’s insurance or other medical coverage provider, such as Medicare.

Specialty points to the fact that it does not charge a fee to the doctors performing the surgeries as rebutting the conclusion that it is “renting.” Initially, such a fact is

irrelevant as neither the common understanding of “renting” nor the Class F definition are dependent on who pays the rent. It is enough that “rent” (*i.e.*, compensation for use of property) is paid to Specialty to establish it is in the business of renting.

More importantly, Specialty's argument ignores the practical reality of compensation for medical care. A specific patient's entire medical treatment, from diagnosis and consultation through treatment and follow-up typically is paid by third-party insurance or governmental medical coverage. Billing for all aspects of the care tends to be submitted separately by providers to these third-parties who, in turn, directly remit payment back to the providers. This payment arrangement does not alter the fundamental fact that Specialty is compensated a facility fee for use of its surgical space.

A simple review of Specialty's role in the transaction confirms that its facility fee is compensation for “use” of its surgical facility space. At the point Specialty is contacted to schedule a procedure, the doctor-patient relationship is already established: the patient has consulted the doctor who, in turn, has determined that a surgical procedure is necessary. What both doctor and patient need at that time is a space to perform the procedure and it is for this reason alone that they contact Specialty.

Specialty has no role in the performance of professional surgical services. Patients cannot go to the surgery center independently for treatment because Specialty does not employ any doctors to perform such surgeries. Instead, the patient's surgery will be performed by an independent doctor. The only reason a patient enters Specialty's facilities is because the patient's doctor has instructed him or her to meet there for the surgery.

Based on these facts, it is clear that the provision of surgical facility space is Specialty's overwhelmingly dominant business activity. Seeking to deflect attention on this point, Specialty observes that it provides a number of support functions, such as waiting room facilities, provision of medical supplies, *etc.* This observation does not alter the analysis. Specialty's reason for existence is the provision of the surgical facility space. Patients do not go to its office solely for the hospitality of the waiting room or to obtain a roll of medical tape. Patients go for surgery performed in surgical space. Other services are wholly dependent upon and support the surgical facility function, much like housekeeping services and cosmetic consumables are part of the rental fee charged for a hotel room.

Finally, Specialty seeks to distract attention from the fact that it is renting commercial space by focusing on its contention that neither the doctor nor the patient has an exclusive right to occupy the surgical facility and that they utilize certain common facilities. Assuming for the sake of argument only that exclusive possession was a requirement for a “lease” there is no such requirement for the broader term “renting” as

it is commonly understood. Many common rental arrangements, such as hotels, include within the rent the right to use common areas with others.

Further, Specialty's argument that neither the doctor nor the patient is entitled to exclusive possession likely overstates the practical reality. Surgical environments are highly controlled settings and it is unlikely that non-essential personnel are entitled to just walk-into the middle of a surgical procedure. Even Specialty's personnel likely are not allowed to enter the surgical environment unless they have the doctor's consent and are necessary to the surgical procedure. In this regard, the transaction is similar to a number of common rental transactions - such as office, residence and hotel renting - whereby the owner has the right to enter the rented space for certain functions (such as maintenance, security and inspection) but the parties have an agreement regarding non-disturbance during its use.

A plain analysis of Specialty's operations demonstrates that its provision of surgical facility space for a fee conforms at a minimum to the ordinary and common meaning of the broad term "renting."

C. Registration and Allocation of Gross Receipts to Class F

The City's assessment of business taxes for Specialty allocated seventy-five percent (75%) of Specialty's gross receipts to Class F. Specialty introduced no evidence during the assessment hearing supporting an alternate percentage allocation to Class F. Accordingly, Specialty has waived any claim to have the Hearing Officer consider an alternate allocation.

Rather than provide evidence of an alternate allocation of gross receipts, Specialty argues that the requirement to register in Class C somehow subsumes all "renting" activity and, therefore, no allocation to Class F should be required. In this regard, Specialty misconstrues both the requirements of the City's Municipal Code and the effect of Specialty's multiple operations.

The Municipal Code plainly requires registration and payment of taxes in multiple classifications for each type of business operation described in the classifications of BHMC Section 3-1-219. As set forth above, Specialty's activity consists predominantly of making surgical facility space available for a fee – conduct which, at a minimum, falls within the Class F definition of "renting." The existence of a professional component merely adds an additional classification in which Specialty must register and pay taxes. The registration and tax obligations are additive and the observation that professional services are provided through employee nurses only operates to increase those obligations.

Based on the City's dialogue with Specialty and all information submitted in connection therewith, the City has determined that Specialty's renting of surgical facility space is its overwhelmingly dominant operation. Such professional services as are provided by Specialty's nurses are performed in support of that dominant operation. The City finds that Specialty's operations are consistent with an allocation to Class F of not less than seventy-five percent (75%) of its gross receipts, and that the corresponding reduction of gross receipts by twenty-five percent (25%) on account of its professional activities is fair and reasonable.

D. Submission of Gross Receipts Data

The City held the assessment hearing open until May 15, 2012, pursuant to multiple requests by Specialty to allow for the submission of supplemental data for the Hearing Officer's consideration. By letter dated May 8, 2012, Specialty's attorneys submitted additional information regarding the calculation of Specialty's gross receipts for the years under assessment.

The May 8, 2012, letter was signed by Specialty's counsel who certified that it contained "true and correct" information regarding gross receipts. The Hearing Officer has reviewed the May 8, 2012, letter and accepts the accuracy of the data therein based on the representations of Specialty's counsel. Accordingly, the assessment amount set forth in the Hearing Officer's findings herein has been revised to reflect this supplemental information.

E. Objection to Hearing Officer

Specialty objects in its Hearing Brief to the undersigned acting as Hearing Officer due to participation in the City's investigation of surgery centers and the resulting assessment of business taxes against Specialty. This objection is not well-founded. The Municipal Code specifically contemplates that this hearing be conducted before a final assessment is rendered by staff who have been investigating this matter. BHM Section 3-1-213(h) indicates that a purpose of the hearing is for the registrant to "submit evidence why the assessed tax interest and penalties should not be fixed." The hearing is an opportunity for the Hearing Officer to receive input from a taxpayer and is not adversarial. No person played any prosecutorial role in the hearing. The Hearing Officer has received all submitted evidence and is in the best position to consider such evidence pursuant to City administrative policy. As set forth below, if Specialty disagrees with the findings herein, it may appeal the final assessment to the City Council.

V. Findings

By this letter Specialty Surgical Center, LLC and Specialty Surgical Center of Beverly Hills, L.P. are hereby informed that the City of Beverly Hills makes a finding of assessment as follows:

1. Specialty Surgical Center, LLC is conducting business in the City of Beverly Hills at 9675 Brighton Way, Suite 100, Beverly Hills, CA 90210.
2. Specialty Surgical Center of Beverly Hills, L.P. is conducting business in the City of Beverly Hills at 8670 Wilshire Blvd., Suite 301, Beverly Hills, CA 90211.
3. Surgical Centers such as Specialty Surgical Center, LLC and Specialty Surgical Center of Beverly Hills, L.P. conduct business operations in "Classification F: Commercial Property Renting And Leasing" and "Classification C: Professions And Semiprofessions" under the City's Municipal Code. (Municipal Code Section 3-1-219).
4. Businesses in Classification F must pay an annual gross receipts tax for each one thousand dollars (\$1,000) of gross receipts, based on the annualized actual gross receipts of the prior calendar year. (Municipal Code Section 3-1-219).
5. The tax rate in Classification F is \$23.50 per one thousand dollars (\$1,000) of gross receipts.
6. Businesses in Classification C must pay an "annual tax for each professional and semiprofessional employee, based on the annualized average number of professional and semiprofessional persons employed in the prior calendar year . . . plus a per employee tax for each nonprofessional employee, based on the annualized average number of nonprofessional persons employed in the prior calendar year. . . ." (Municipal Code Section 3-1-219).
7. The current tax rate for Classification C is \$1,322.90 for the first 2,080 hours of professional and semiprofessional payroll and 0.63606 per each additional hour of professional and semiprofessional hours plus 0.12778 for each hour of nonprofessional employee payroll.

8. Gross receipts is defined, in relevant part, as the "total amount of the sales price of all sales, the total amount charged or received for the performance of any act, service or employment of whatever nature it may be" and "without any deductions therefrom on account of the cost of the property sold, the cost of materials used, labor or service costs, interest paid or payable, losses or any other expense whatsoever." (Municipal Code Section 3-1-205).
9. The City's Municipal Code Section 3-1-205 provides the following relevant definitions:

"NUMBER OF PROFESSIONAL AND SEMIPROFESSIONAL PAYROLL HOURS; PROFESSIONAL BUSINESS CLASSIFICATIONS: One of the following:

- a. Where the professional business being registered bills its clientele based on total professional and/or semiprofessional hours of service provided, the total number of professional and semiprofessional hours charged to client accounts, whether compensation of any form whatsoever has been received, in the previous calendar year.
- b. Where the professional business being registered does not bill its clientele based on total professional and/or semiprofessional hours of service provided, the total number of professional and semiprofessional payroll hours recorded, including, but not limited to, regular, overtime, part time, vacation, compensated absences, and all other hours for which compensation of any form is provided, of professional and semiprofessional persons employed in the registrant's business within the city of Beverly Hills, in the previous calendar year."

"NUMBER OF PAYROLL HOURS; NONPROFESSIONAL BUSINESS CLASSIFICATIONS: The total number of payroll hours recorded, including, but not limited to, regular, overtime, part time, vacation, compensated absences, and all other hours for which compensation of any form is provided, of persons employed in the registrant's business within the city of Beverly Hills in the previous calendar year."

10. Based on the information available to the City of Beverly Hills, Specialty Surgical Center, LLC and Specialty Surgical Center of Beverly Hills, L.P. are providers of space for the performance of outpatient surgical procedures and providers of professional services related to the care of patients during such procedures.

11. Based on the information available to the City of Beverly Hills, Specialty Surgical Center, LLC and Specialty Surgical Center of Beverly Hills, L.P. were required to register in both Classification C and Classification F and pay business taxes required by each classification, but failed to do so.
12. The City of Beverly Hills finds that not less than seventy-five percent (75%) of the gross receipts of Specialty Surgical Center, LLC and Specialty Surgical Center of Beverly Hills, L.P. are attributable to Classification F operations.
13. Based on the best information available to the City of Beverly Hills, Specialty Surgical Center, LLC and Specialty Surgical Center of Beverly Hills, L.P. have tax liability to the City of Beverly Hills for business taxes due in and for calendar years 2003 through 2011 in the amount of \$5,536,365.48 as follows:

Classification F Tax											
Tax Basis Year	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	Total
For Calendar Year	2003	2004	2005	2006	2007	2008	2009	2010	2011		
Specialty Surgical Center LLC											
Gross Receipts	11,208,125.00	12,484,318.00	8,403,947.00	5,301,167.00	5,020,620.00	5,434,673.00	6,767,949.00	7,137,213.00	7,089,476.00		68,847,488.00
Allocation to F Class	75%	75%	75%	75%	75%	75%	75%	75%	75%		
Tax Bases	8,406,093.75	9,363,238.50	6,302,960.25	3,875,875.25	3,765,465.00	4,076,004.75	5,075,961.75	5,352,909.75	5,317,107.00		51,635,618.00
Tax	197,543.20	220,036.10	148,119.57	93,433.07	88,468.43	95,786.11	119,285.10	125,793.38	124,952.01		1,213,438.98
Payments	-	-	-	-	-	-	-	-	-		-
Tax Due:	197,543.20	220,036.10	148,119.57	93,433.07	88,468.43	95,786.11	119,285.10	125,793.38	124,952.01		1,213,438.98
Penalty Rate	50%	50%	50%	50%	50%	50%	50%	50%	50%		
Penalty	98,771.60	110,018.05	74,059.78	46,718.53	44,244.21	47,893.06	59,642.55	62,896.69	62,478.01		608,718.49
Interest Rate	1.50%	1.50%	1.50%	1.50%	1.50%	1.50%	1.50%	1.50%	1.50%		
Tax due date	1/31/2003	1/31/2004	1/31/2005	1/31/2006	1/31/2007	1/31/2008	1/31/2009	1/31/2010	1/31/2011		
Months of Interest	113	101	89	77	65	53	41	29	17		
Interest Charge	334,835.73	333,354.70	197,738.62	107,915.18	85,276.22	76,149.96	73,360.34	54,720.12	31,862.76		1,296,214.64
Total Due:	631,150.53	663,408.66	419,918.97	248,064.80	219,008.86	219,829.13	252,287.99	243,410.19	219,290.79		3,116,370.10
Specialty Surgical Center of Beverly Hills, L.P.											
Gross Receipts	-	24,895.00	5,513,682.00	11,392,599.00	10,208,073.00	7,334,861.00	9,131,254.00	8,417,143.00	7,870,143.00		59,832,630.00
Allocation to F Class	75%	75%	75%	75%	75%	75%	75%	75%	75%		
Tax Bases	-	18,671.25	4,135,246.50	8,499,449.25	7,656,054.75	5,501,145.75	6,848,440.50	6,312,857.25	5,902,607.25		44,874,472.50
Tax	-	438.77	97,178.29	199,737.06	179,917.29	129,276.93	160,938.35	148,352.15	138,711.27		1,054,550.10
Payments	-	-	-	-	-	-	-	-	-		-
Tax Due:	-	438.77	97,178.29	199,737.06	179,917.29	129,276.93	160,938.35	148,352.15	138,711.27		1,054,550.10
Penalty Rate	50%	50%	50%	50%	50%	50%	50%	50%	50%		
Penalty	-	219.39	48,589.15	99,868.53	89,958.64	64,638.46	80,469.18	74,176.07	69,355.64		527,275.05
Interest Rate	1.50%	1.50%	1.50%	1.50%	1.50%	1.50%	1.50%	1.50%	1.50%		
Tax due date	1/31/2003	1/31/2004	1/31/2005	1/31/2006	1/31/2007	1/31/2008	1/31/2009	1/31/2010	1/31/2011		
Months of Penalty	113	101	89	77	65	53	41	29	17		
Interest Charge	-	664.74	129,733.02	230,696.30	175,419.35	102,775.15	98,077.09	64,533.18	35,371.37		838,170.22
Total Due:	-	1,322.90	275,500.46	530,301.89	445,295.28	296,690.54	340,384.61	287,061.40	243,438.28		2,419,995.37
Classification C Tax											
Tax Basis Year	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	Total
For Calendar Year	2003	2004	2005	2006	2007	2008	2009	2010	2011		
Specialty Surgical Center LLC											
Tax	21,846.60	14,966.13	8,866.96	8,866.96	6,570.08	12,131.47	13,684.46	13,725.53	15,050.15		117,708.34
Payments	(21,846.60)	(14,966.13)	(8,866.96)	(8,866.96)	(6,570.08)	(12,131.47)	(13,684.46)	(13,725.53)	(15,050.15)		(117,708.34)
Tax Due	-	-	-	-	-	-	-	-	-		-
Specialty Surgical Center of Beverly Hills, L.P.											
Tax	2,402.02	19,416.62	26,676.01	26,676.01	25,324.32	34,092.04	31,751.61	29,996.85	28,348.41		224,683.89
Payments	(2,402.02)	(19,416.62)	(26,676.01)	(26,676.01)	(25,324.32)	(34,092.04)	(31,751.61)	(29,996.85)	(28,348.41)		(224,683.89)
Tax Due	-	-	-	-	-	-	-	-	-		-
For Calendar Year	2003	2004	2005	2006	2007	2008	2009	2010	2011	Total	
Total due											
Specialty Surgical Center LLC											
and											
Specialty Surgical Center of Beverly Hills L.P.	631,150.53	664,731.76	695,419.43	778,366.68	654,304.14	516,518.67	592,672.60	530,471.59	462,729.06		5,536,365.48

These findings have determined that Specialty Surgical Center, LLC and Specialty Surgical Center of Beverly Hills, L.P.'s liabilities for unpaid business taxes due in and for calendar years 2003 through 2011, including penalties and interest thereon through June 30, 2012, as set forth above, is \$5,536,365.48. Thereafter, a monthly interest charge of \$34,019.81 (at a rate of 18% per annum) will be added to this balance until this obligation has been fully satisfied. A copy of the chart set forth above is attached hereto.

The City's Municipal Code Section 3-1-213 (L) "Appeal From The Decisions of the Director of Finance" provides you the following appeal rights to this decision:

L. "Appeal From The Decisions Of The Director Of Finance Administration: Any registrant or person assessed not in agreement with the decision of the director of finance administration with respect to the amount of such tax, interest and penalties, if any, may appeal to the city council as provided in title 1, chapter 4, article 1 of this code. (Ord. 96-O-2255, eff. 3-22-1996)"

Title 1, Chapter 4, Article 1 provides the following:

1-4-101: RIGHT TO APPEAL:

A. Where a right of appeal to council exists under this code, and a procedure is not otherwise specifically set forth in this code, an appeal may be taken to the council, in accordance with the procedures set forth in this article, from any act, ruling, or determination of any commission, board, or official or from the denial, suspension, or revocation of any permit or license.

B. No right of appeal to the council from any administrative decision made by an official of the city pursuant to any of the provisions of this code shall exist when such decision is ministerial and thus does not involve the exercise of administrative discretion or personal judgment exercised pursuant to any of the provisions of this code.

C. No appeal pursuant to the provisions of this article may be taken from any administrative decision made by an official of the city, unless the decision to appeal has been first taken up with the official rendering the decision. (1962 Code § 1-6.101)

**1-4-102: TIME WITHIN WHICH APPEAL PETITIONS MUST BE FILED;
WITHDRAWAL OF APPEAL PETITIONS:**

A. Any appeal petition shall be filed with the city clerk within fourteen (14) calendar days after the date of the decision. In the event the last day of the filing period falls on a nonbusiness day, the appeal period shall be extended to include the next business day. The timely filing of the appeal petition is jurisdictional. The fee schedule for appeal petitions shall be approved by the council and maintained on file by the director of finance administration.

B. If an appeal petition, filed pursuant to subsection A of this section, is withdrawn at any time prior to the council decision on the appeal petition, then subsequent to such withdrawal, the council may review the decision which was the subject of the withdrawn petition. Such review may be ordered by motion of the council duly adopted within fifteen (15) calendar days after the appeal petition is withdrawn. If the council orders a review of such a decision, the effectiveness of such decision shall be stayed until council review is final. (1962 Code § 1-6.102; amd. Ord. 94-O-2211, eff. 9-2-1994)

1-4-103: CONTENTS OF APPEAL PETITIONS:

Every appeal petition shall contain a statement of the facts upon which the appeal is based in sufficient detail to enable the council to understand the nature of the controversy, the basis of the appeal, and the relief requested. (1962 Code § 1-6.103)

1-4-104: STAYS PENDING APPEALS:

Upon the filing of an appeal petition, the effectiveness of any permit, entitlement to use, or other right granted by the decision appealed from shall be stayed pending a final decision by the council. (1962 Code § 1-6.104)

1-4-105: CONSIDERATION OF APPEAL PETITIONS:

After an appeal petition is filed in accordance with this article, the city clerk shall place the matter on the council agenda for council action. Based on the appeal petition and the written material presented, the council shall determine whether to refer the matter back to the commission, board, or official rendering the decision pursuant to subsection A of this section or whether to grant a hearing on the appeal pursuant to subsection B of this section. The council shall not permit oral testimony in its determination under this section.

A. If the council finds the facts in the appeal petition contain new and material evidence not previously presented to the board, commission, or official, the council may order that the board, commission, or official rehear the matter. Written notice of the rehearing shall be mailed to the appellant and to such other persons who have appeared and addressed the board, commission, or official at the prior hearing in connection with such matter, and mailing shall be at least ten (10) days before such rehearing, and such other notice as required by law for the previous hearing shall also be given.

B. Except as provided for in subsection A of this section, the council shall set the matter for a hearing. At least ten (10) days prior to the hearing, written notice shall be mailed to the appellant and to other persons who appeared and addressed the board, commission, or official at the prior hearing on the matter, and such other notice as required by law for the previous hearing shall also be given. (1962 Code § 1-6.105)

1-4-106: HEARINGS BY THE COUNCIL:

Unless otherwise ordered and noticed, hearings shall be held as a part of the regular meetings of the council. The hearing shall be de novo in that an independent reexamination of the matter shall be made. The appellant shall have the burden of proof in all cases, and where it appears that an appellant was served with a notice of hearing but fails to appear either in person or by counsel, or fails to present or offer evidence, the council may adopt the determination or approve the act of the board, commission, or official, or it may itself decide the matter upon the record with or without taking any additional evidence. Any oral or documentary evidence may be received, but the mayor shall exclude irrelevant, immaterial, or unduly repetitious evidence. Unless a demand is made, witnesses will not be sworn. It shall not be a ground for objection that the evidence is hearsay or secondary, however, the council's decision shall be made upon substantial evidence. (1962 Code § 1-6.106)

1-4-107: DECISIONS BY THE COUNCIL FINAL:

Upon the hearing of the appeal, the council may refer the matter back to the board, commission, or official, with directions for further consideration, or the council may reverse, affirm, or modify the decision or may make such decision or determination as may appear just and reasonable in the light of the evidence presented. The decision of the council shall be final and conclusive at one minute after twelve o'clock (12:01) midnight on the first day after issuance. (1962 Code § 1-6.107)

1-4-108: FINDINGS BY THE COUNCIL:

The council shall prepare written findings if, prior to closing the public hearing, the appellant, the applicant, or an aggrieved party requests the council to make written findings. In such event, the council shall direct the city attorney to draft a resolution containing the facts found to be true, which findings shall be considered and adopted by resolution at a subsequent regular meeting of the council. The findings shall include the reasons for the council's ruling, including, but not limited to, findings of facts, if any, required by the code sections or ordinance upon which the appeal is based. (1962 Code § 1-6.108)

ISSUED THIS 7th DAY OF JUNE, 2012

NOEL MARQUIS
Hearing Officer

A handwritten signature in black ink, appearing to read "Noel Marquis", is written over a horizontal line.

Enclosure

Classification F Tax

Tax Basis Year	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	Total
For Calendar Year	2003	2004	2005	2006	2007	2008	2009	2010	2011		
Speciality Surgical Center LLC											
Gross Receipts	11,208,125.00	12,484,318.00	8,403,947.00	5,301,167.00	5,020,620.00	5,434,673.00	6,767,949.00	7,137,213.00	7,089,476.00		68,847,488.00
Allocation to F Class	75%	75%	75%	75%	75%	75%	75%	75%	75%		
Tax Bases	8,406,093.75	9,363,238.50	6,302,960.25	3,975,875.25	3,765,465.00	4,076,004.75	5,075,961.75	5,352,909.75	5,317,107.00		51,635,616.00
Tax	197,543.20	220,036.10	148,119.57	93,433.07	88,488.43	95,786.11	119,285.10	125,793.38	124,952.01		1,213,436.98
Payments	-	-	-	-	-	-	-	-	-		-
Tax Due:	197,543.20	220,036.10	148,119.57	93,433.07	88,488.43	95,786.11	119,285.10	125,793.38	124,952.01		1,213,436.98
Penalty Rate	50%	50%	50%	50%	50%	50%	50%	50%	50%		
Penalty	98,771.60	110,018.05	74,059.78	46,716.53	44,244.21	47,893.06	59,642.55	62,896.69	62,476.01		606,718.49
Interest Rate	1.50%	1.50%	1.50%	1.50%	1.50%	1.50%	1.50%	1.50%	1.50%		
Tax due date	1/31/2003	1/31/2004	1/31/2005	1/31/2006	1/31/2007	1/31/2008	1/31/2009	1/31/2010	1/31/2011		
Months of Interest	113	101	89	77	65	53	41	29	17		
Interest Charge	334,835.73	333,354.70	197,739.62	107,915.19	86,276.22	76,149.96	73,360.34	54,720.12	31,862.76		1,296,214.64
Total Due:	631,150.53	663,408.86	419,918.97	248,064.80	219,008.86	219,829.13	252,287.99	243,410.19	219,290.79		3,116,370.10

Specialty Surgical Center of Beverly Hills, L.P.											
Gross Receipts	-	24,895.00	5,513,662.00	11,332,599.00	10,208,073.00	7,334,861.00	9,131,254.00	8,417,143.00	7,870,143.00		59,832,630.00
Allocation to F Class	75%	75%	75%	75%	75%	75%	75%	75%	75%		
Tax Bases	-	18,671.25	4,135,246.50	8,499,449.25	7,656,054.75	5,501,145.75	6,848,440.50	6,312,857.25	5,902,607.25		44,874,472.50
Tax	-	438.77	97,178.29	199,737.06	179,917.29	129,276.93	160,938.35	148,352.15	138,711.27		1,054,550.10
Payments	-	-	-	-	-	-	-	-	-		-
Tax Due:	-	438.77	97,178.29	199,737.06	179,917.29	129,276.93	160,938.35	148,352.15	138,711.27		1,054,550.10
Penalty Rate	50%	50%	50%	50%	50%	50%	50%	50%	50%		
Penalty	-	219.39	48,589.15	99,868.53	89,958.64	64,638.46	80,469.18	74,176.07	69,355.64		527,275.05
Interest Rate	1.50%	1.50%	1.50%	1.50%	1.50%	1.50%	1.50%	1.50%	1.50%		
Tax due date	1/31/2003	1/31/2004	1/31/2005	1/31/2006	1/31/2007	1/31/2008	1/31/2009	1/31/2010	1/31/2011		
Months of Penalty	113	101	89	77	65	53	41	29	17		
Interest Charge	-	664.74	129,733.02	230,696.30	175,419.35	102,775.16	98,977.09	64,533.18	35,371.37		838,170.22
Total Due:	-	1,322.90	275,500.46	530,301.89	445,295.28	296,690.54	340,384.61	287,061.40	243,438.28		2,419,995.37

Classification C Tax

Tax Basis Year	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	Total
For Calendar Year	2003	2004	2005	2006	2007	2008	2009	2010	2011		
Speciality Surgical Center LLC											
Tax	21,846.60	14,966.13	8,866.96	8,866.96	8,570.08	12,131.47	13,684.46	13,725.53	15,050.15		117,708.34
Payments	(21,846.60)	(14,966.13)	(8,866.96)	(8,866.96)	(8,570.08)	(12,131.47)	(13,684.46)	(13,725.53)	(15,050.15)		(117,708.34)
Tax Due:	-	-	-	-	-	-	-	-	-		-
Specialty Surgical Center of Beverly Hills, L.P.											
Tax	2,402.02	19,416.62	26,676.01	26,676.01	25,324.32	34,092.04	31,751.61	29,996.85	28,348.41		224,683.89
Payments	(2,402.02)	(19,416.62)	(26,676.01)	(26,676.01)	(25,324.32)	(34,092.04)	(31,751.61)	(29,996.85)	(28,348.41)		(224,683.89)
Tax Due:	-	-	-	-	-	-	-	-	-		-
For Calendar Year	2003	2004	2005	2006	2007	2008	2009	2010	2011		Total
Speciality Surgical Center LLC and Specialty Surgical Center of Beverly Hills L.P.	631,150.53	664,731.76	695,419.43	778,366.68	664,304.14	516,519.67	592,672.60	530,471.59	462,729.06		5,536,365.48

EXHIBIT C

Melissa Crowder

From: Jose Zaragoza
Sent: Monday, May 07, 2012 8:01 AM
To: Melissa Crowder
Subject: RE: New notes have been added to case #27323

I looked up the sic code for surgery center and came up with 8093. I entered that sic code to generate the list you are asking for. There were zero returns using that sic code.

-----Original Message-----

From: mcrowder@beverlyhills.org [mailto:mcrowder@beverlyhills.org]
Sent: Friday, May 04, 2012 2:18 PM
To: Jose Zaragoza
Subject: New notes have been added to case #27323

Hi Jose,

Can you please provide the information on the business tax returns and provide the number of surgery centers or suite under business category F from 1990-present? I've been provided all the information from Community Development so I'm just waiting on your info.

Thanks,
Melissa

For more information, click <https://clients.comcate.com/rebs/caseDetail.php?ag=31&id=461312>

EXHIBIT D

Beverly Hills Ambulatory Surgical Centers January 2010

From ASC Website

436 N. BEDFORD

✓ BEDFORD AMBULATORY SURGERY CENTER	BeverlyHills	CA
✓ BEDFORD OUTPATIENT SURGERY CENTER	BeverlyHills	CA
✓ BEDFORD PLASTIC SURGERY CENTER	BeverlyHills	CA
✓ BEDFORD SURGICAL CENTER	BeverlyHills	CA
✓ BEVERLY HILLS ADVANCED SURGERY CENTER 120 SPALDING	BeverlyHills	CA
✓ BEVERLY HILLS AMBULATORY SURGERY CTR 435 N. ROXBURY	BeverlyHills	CA
✓ BEVERLY HILLS DOCTORS SURGERY CENTER 120 SPALDING	BeverlyHills	CA
✓ BEVERLY HILLS ENDOSCOPY, LLC 465 ROXBURY	BeverlyHills	CA
BEVERLY HILLS MEDICAL, INC	BeverlyHills	CA
✓ BEVERLY HILLS ROBERTSON SURGERY CENTER 150 N. ROBERTSON	BeverlyHills	CA
✓ BEVERLY HILLS SURGICAL INSTITUTE 9025 WILSHIRE	BeverlyHills	CA
BEVERLY HILLS WILSHIRE SURG-CTR MED GP	BeverlyHills	CA
✓ BRIGHTON SURGICAL CENTER, INC 9675 BRIGHTON	BeverlyHills	CA
✓ CAMDEN SURGERY CENTER OF BEVERLY HILLS 414 N. CAMDEN	BeverlyHills	CA
✓ COMPREHENSIVE OUTPATIENT SURGE 250 N. ROBERTSON	BeverlyHills	CA
✓ DOHENY ENDOSURGICAL CENTER 9090 WILSHIRE	BeverlyHills	CA
✓ LINDEN CREST SURGERY CENTER 9735 WILSHIRE	BeverlyHills	CA
ORCHID OUTPATIENT MEDICAL AND	BeverlyHills	CA
✓ REXFORD OPERATING ROOMS, INC 9301 WILSHIRE	BeverlyHills	CA
✓ ROXBURY SURGERY CENTER 450 N. ROXBURY / 465 N. ROXBURY	BeverlyHills	CA
✓ S & B SURGERY CENTER 120 S. SPALDING	BeverlyHills	CA
✓ SPALDING OUTPATIENT SURGERY CENTER 120 S. SPALDING	BeverlyHills	CA
SPECIALISTS AMBULATORY SURGERY	BeverlyHills	CA
✓ SPECIALITY SURGICAL CENTER ⁸⁶⁷⁰ 8670 WILSHIRE & 9675 BRIGHTON	BeverlyHills	CA
✓ SPECIALTY SURGICAL CENTER OF BEVERLY HILLS	BeverlyHills	CA
✓ SURGIWORLD 465 N. ROXBURY	BeverlyHills	CA
✓ TRIANGLE SURGERY CENTER 450 N. ROXBURY	BeverlyHills	CA
WILSHIRE SURGICAL MEDICAL CENTER	BeverlyHills	CA
✓ WILSHIRE SURGICENTER 8641 WILSHIRE	BeverlyHills	CA

ME
MESS, 2
ATTORNS

150 N. Robertson
SH? ✓

EXHIBIT E



STAFF REPORT
CITY OF BEVERLY HILLS

For the Planning Commission
Meeting of January 28, 2010

TO: The Planning Commission
FROM: Michele McGrath, Senior Planner
SUBJECT: Consideration of Changes to Medical Land Use Policy that Limit or Prohibit New or Expanded Medical Uses in the City.

EXECUTIVE SUMMARY

After City Council meetings in July, 2009, the Planning Commission was directed to develop an ordinance further regulating medical uses in the City. On November 19, 2009, the Planning Commission conducted a study session to review additional regulation of medical uses (staff report attached) and requested that staff return with the following information provided in this report: identification of categories of medical uses and corresponding traffic/parking and tax information for each category as is available; number of medical offices/doctors in the City and map showing locations; amount of new medical land use approved in the City in recent years; existing commercial buildings with enough parking to convert or add medical use; adequacy of the City's current parking requirements for medical offices/buildings; and, information about instituting a transportation impact fee. In addition, the Commission requested draft CUP findings for medical uses including consideration as to how flexibility can be incorporated in the process, e.g. allowing small conversions or small amounts of additional medical floor area in existing buildings. Finally, the Commission requested additional information on instituting an annual or overall cap on medical uses.

Categories of Medical Uses

Medical uses can be defined in different ways by zoning codes, building codes and tax and licensing codes. The City of Beverly Hills defines "medical office" as follows:

"MEDICAL OFFICE: Any facility providing health service and/or medical, surgical, or dental care. 'Medical office' shall include, but not be limited to, a health center, health clinic, doctor's office, chiropractor's office, dentist's office, or any office offering therapeutic service or care. 'Medical office' shall not include a 'medical laboratory' as defined in this section."

A medical laboratory is separately defined as follows:

"MEDICAL LABORATORY: Any facility providing medical or dental services for the purpose of diagnosing or treating medical or dental conditions that does not receive patrons on site."

Some specific types of medical offices are defined in other Code sections such as in the Overnight Stay Ordinance which includes definitions of "specialty clinic" (surgi-center) and "sleep disorder center." The definition of medical offices includes all of the support functions for medical offices such as waiting rooms, conference rooms and administrative offices just as all of these functions are included as part of general offices. Because medical office uses require more parking spaces, applicants often try to separate out portions of the medical office use for parking purposes which is not consistent with staff's interpretation of Code.

The categories of medical uses generally identified in municipal zoning codes include:

- medical offices/outpatient clinics;
- laboratories;
- hospitals/inpatient care; and, in some cases,
- long-term in-patient care (nursing homes).

Staff has found no further delineation of medical uses in any other municipal zoning codes surveyed. The main criterion for classification appears to be whether the medical use operates on an outpatient (medical office/clinic), inpatient (hospital, nursing home), or no patient (medical lab) basis. One of the relatively recent developments in medical uses is the increase in ambulatory surgery centers ("surgi-centers"). Surgi-centers are not generally defined separately in zoning codes and are regulated in the same category as medical offices/clinics because they operate on an outpatient basis.

The outpatient/inpatient distinction may stem from Building Code classifications. The 2007 California Building Code classifies all buildings and structures as to use and occupancy according to fire safety and relative hazard involved. The "Business Group B" occupancy includes the majority of commercial businesses such as banks, salons, outpatient clinics, laboratories, and professional services such as architects, attorneys, dentists, physicians, engineers, etc. Surgi-centers are included in this classification unless accommodating more than five patients receiving outpatient medical care that may render the patient incapable of unassisted self-preservation. In this case the surgi-center occupancy would be classified as "Institutional Group I" along with hospitals, nursing homes, detoxification facilities, residential care facilities, congregate living facilities, and other facilities offering inpatient services.

To consider further distinctions in categories of medical uses, it is helpful to have an understanding of the characteristics of a "typical" medical office use. Medical offices and clinics traditionally schedule a full day of appointments with patients in quick succession and have a large number of employees providing services. According to a number of medical

websites, the average patient time with a primary care physician in the United States is less than 20 minutes and the average patient wait-time for that appointment is a little over 20 minutes, resulting in a constant stream of patients, many who stack up in waiting rooms. For these reasons, the ITE* traffic and parking numbers are high for medical uses (see 11/19/10 staff report) and also why many cities, including Beverly Hills, consider medical offices a higher intensity use that requires more parking than for general office use.

It is difficult to characterize each medical use or to categorize groups of medical uses for the purpose of regulation; however, one group, therapists and counselors (psychoanalysts, psychiatrists, nutritionists) stand out as possibly generating fewer traffic and parking impacts due to longer appointment times and fewer patients/clients waiting for appointments. Therapists or counselors typically schedule appointments for a minimum of one hour, have fewer employees and usually no more than one client/patient waiting for an appointment. According to the American Psychological Association, approximately half of psychologists are self employed. Therapist and other counseling offices often resemble non-medical professional offices and staff has noted a number of therapists' offices in buildings that are otherwise occupied by lawyers, accountants and other professionals with no other medical uses. Should the Planning Commission wish to consider regulating therapists/counselors differently than other medical uses, one note of caution is that some therapists/counselors have group sessions or classes that could result in negative traffic and parking impacts.

The Planning Commission raised the question as to whether surgi-centers should be regulated differently than other medical offices. It is noted that surgi-centers may operate differently from medical offices and the average daily number of trips and parking required for surgi-centers may be less than for medical clinics; however, the ITE guide for parking generation shows that traffic and parking rates at peak times are similar to medical clinics. The ITE information was based on a small sample and additional studies may be needed if the Planning Commission wishes to make a distinction between surgi-centers and other medical uses based on traffic and parking impacts.

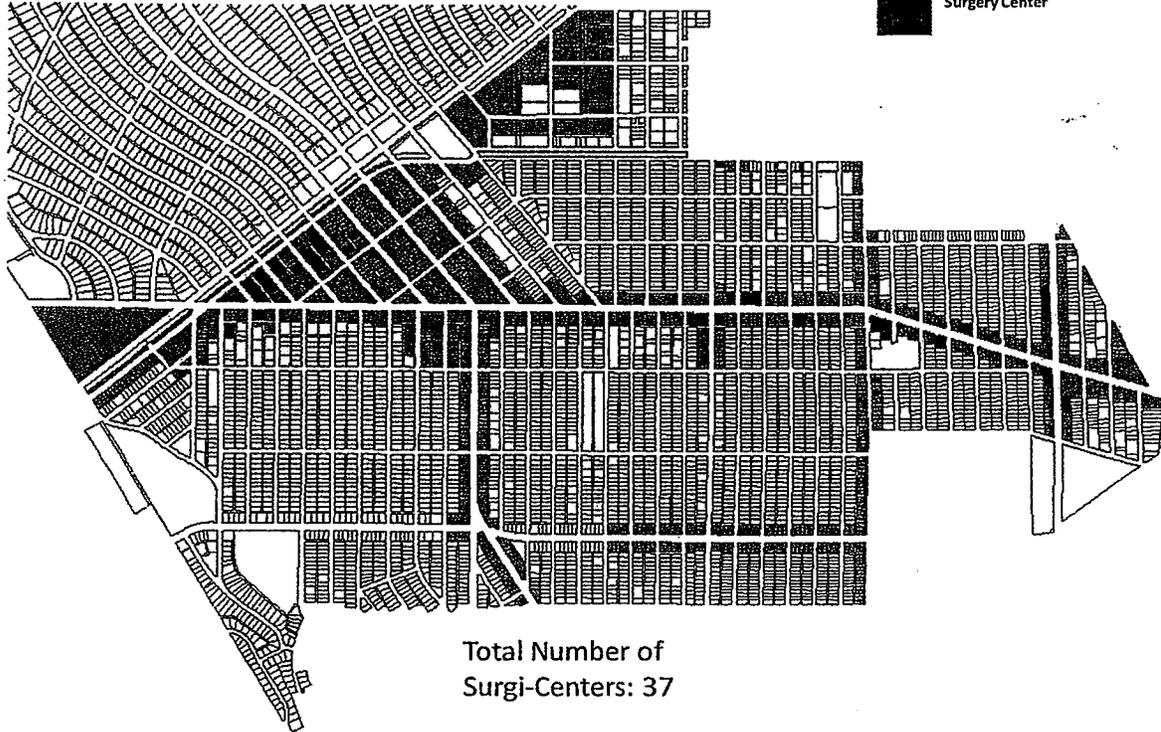
While there may be a difference in the parking and traffic impacts between medical offices/clinics and certain other types of uses such as therapists/counselors included in the City's definition of medical uses, the City has identified other potential negative impacts of medical uses that may be an issue across the spectrum of medical uses. These other impacts include how medical uses affect the City's retail/pedestrian vitality, the impact on the City's efforts to attract a variety of commercial uses including businesses such as talent agencies that have been specifically identified by the City as important to the City's image and

* ITE refers to the Institute of Transportation Engineers, considered to be an authoritative source of data regarding vehicle trip generation and parking.

AMBULATORY SURGICAL CENTERS IN BEVERLY HILLS

For Planning Commission Meeting 1/28/10

LEGEND



Prepared by the Planning Commission for the Planning Commission

economic future, and the impact of medical uses on the City's tax revenues. The Planning Commission may wish to consider these impacts when discussing whether the "medical office" definition in the Code needs further refinement. Please also see the 11/19/09 report for more information about the potential impacts of medical uses:

Tax

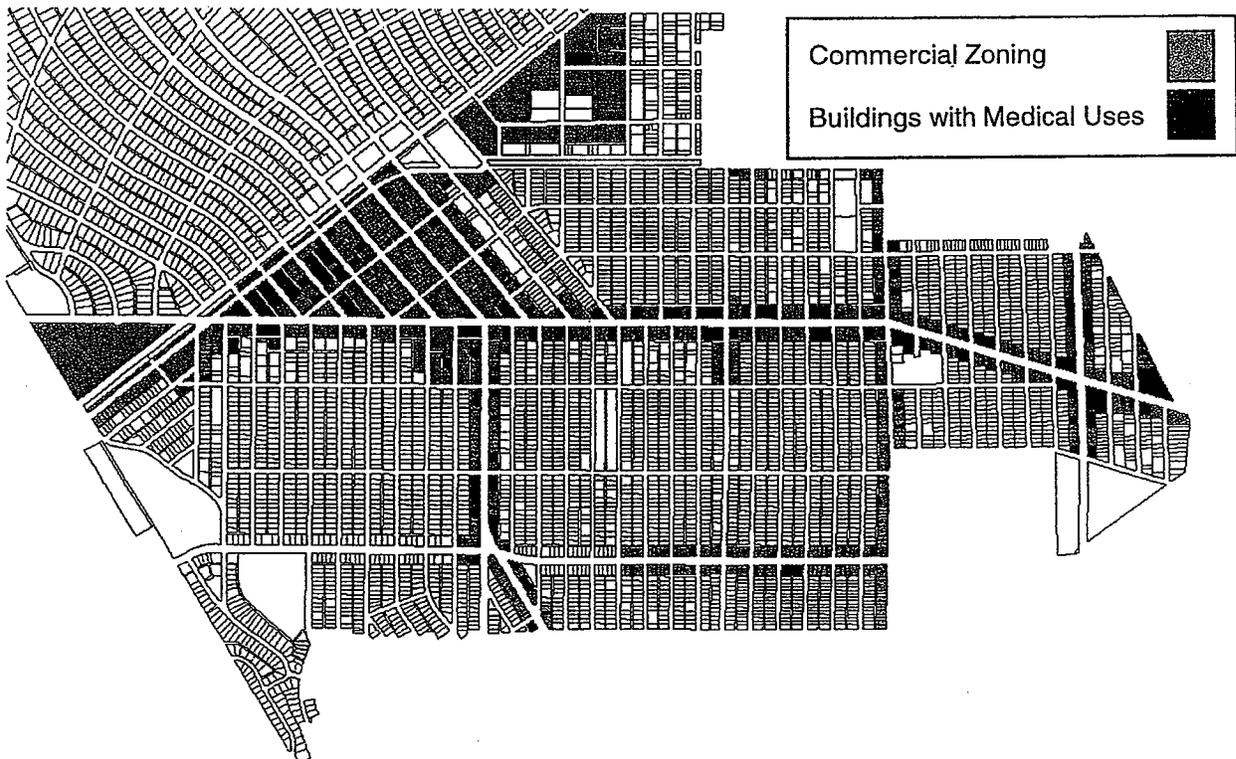
For tax purposes, the City categorizes uses in different classifications with different tax structures. Medical offices in Beverly Hills fall under the Class C, "Professions and Semiprofessions" category which taxes such businesses based on the annualized average number of professional and semiprofessional persons employed (See Attachment 2). Therapists usually fall under Class C but can fall under Class A, "Business and Personal Services" depending on the service provided. Under Class A registrants pay an annual basic tax plus a per employee tax for each employee. According to the City's Business Tax specialists, medical labs often fall under Class A because they are staffed by technicians rather than doctors or nurses. Surgi-centers can be Class B ("Retail, Wholesale, Manufacturing and Contractors"), Class C or Class F ("Commercial Property Renting and Leasing") depending on how the surgicenter bills activities. For example, if the surgicenter rents out space by the hour to a doctor, such activity could fall under Class F. The City's Business Tax specialists stated it is possible surgicenters bring in more revenue to the City than other medical uses but staff has

not noticed a major difference due to the small number of surgi-centers as compared to the total number of medical offices in the City. The real difference in tax revenue to the City occurs between business tax classifications that pay taxes per employee (Classes A and C) and classifications that pay taxes based on a percentage of gross receipts (Class B).

Existing medical uses in Beverly Hills

Medical use comprises 21%, or more than one fifth of the office space in Beverly Hills. According to the 2008 Economic Sustainability Background Report prepared for the City, the health care sector is the City's second largest industry with 904 Outpatient Health Care employers in the City. There are a total of approximately 794 commercial buildings in the City with staff identifying medical offices in 136 or 17% of the buildings. This is consistent with the 21% figure in that many of the buildings with medical uses include multiple medical offices and there may be a few buildings with a small amount of medical use not yet identified by staff. These buildings are spread throughout the City's commercial areas with concentrations on the west end of the Business Triangle, sections of Wilshire Boulevard, South Beverly Drive below Gregory Way and Robertson Boulevard. Medical offices are noticeably less prevalent in the pedestrian-designated areas located in the central portion of the Business Triangle and South Beverly Drive between Wilshire Boulevard and Gregory Way.

Buildings with Medical Uses



The maps above and below show existing medical uses in the City as could be determined by staff using City records, the County Tax Assessor's website; the City's business tax database, the internet and site visits. These maps do not necessarily represent permitted medical uses as it was time-prohibitive to review the permit status of each medical use in each of the 136 buildings shown, representing over 900 medical employers. The map below represents medical uses in existing buildings broken down into the following categories:

- Buildings that appear to be at least 85% medical use with medical at the ground floor
- Buildings that appear to be at least 85% medical use with ground floor retail uses including pharmacies. This category includes one-story buildings that have retail uses on the street and medical uses in the rear.
- Buildings that have a substantial number of medical offices/clinics.
- Buildings that have at least one or two medical offices (mostly therapists/counselors)

Medical Use Category Map

