

Formula Retail Subsidiary Working Group

January 28 - March 25, 2015 | | City Hall Room 278 | Office of Supervisor Mar & Planning Department

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San Francisco initiated formula retail regulations in 2004. After 10 years of experience with implementation of these controls and one year of study and dialog of the issue, [San Francisco recently updated the controls](#). These new controls now include increased rigor in conditional use review, specific regulation of signage and façade for formula retail, and an economic impact study for larger stores. One controversial topic was left outstanding: the regulation of subsidiaries. Both Supervisor Mar and Planning Department staff found the proposed regulation of subsidiaries to be problematic. Therefore, a working group is being established to further explore the topic and make recommendations to the City's Small Business and Planning Commission about the viability of further regulation.

Summary Meetings

- 1. Summary of January 28 Meeting.** At our meeting last week, we heard overview presentations by Supervisor Mar, the Planning Department, City Attorney's Office, and Economic Analysts. The group discussed the goals: some are ready to test ideas to regulate subsidiaries and some would still like to discuss whether FR should be regulated. The group confirmed the draft meeting schedule and tentative topics below. As the group explores the issues, we're interested in benefiting from the experience of the group's members.
- 2. Summary of February 25, 3:30PM. Exploration Meeting.**
At the start of the last meeting, we adopted ground rules (see the following page). We heard and discussed presentations from group members. The topics included 1) Ilene Dick and Dee Dee Workman—Exploring definitions: what is a subsidiary; 2) Peter Cohen & Paul Wermer—Exploring a path towards regulation; 3) Miriam Zouzounis—Experience of independent businesses; and 4) Paul Webber—Protecting neighborhood charm when the subsidiary is not, itself, a formula retailer. Three requests were raised at the end of the meeting. 1) A plea to remain respectful in our dialog; 2) request to invite Adriano Paganini; and 3) request for a presentation about a side topic, Community Business Priority Processing Program—the recently adopted Planning Commission policy.
- 3. March 11, 3:30PM. Idea Testing Meeting.**
Idea Testing Meeting. **This meeting began to discuss solutions.** While the members maintained diverse viewpoints as to whether subsidiaries present a significant problem, the group self-selected into small groups with shared values.

Small Group Work: Two groups were formed: one that thought subsidiary legislation is needed and one that was undecided. No group was certain that legislation was not needed. All groups were asked to answer three questions: 1) What are subsidiaries? 2) How are subsidiaries harmful or not to neighborhoods? 2) How large or small is the problem? In addition, the group that was undecided set out to discuss any issue related to subsidiaries. The group that believed further legislation is needed set out to articulate regulatory ideas.

BREAK: Community Business Priority Processing Program. A short break allowed for a presentation on the Planning Commission's recent action to assist small and mid-sized community businesses.

Reconvene for Presentations.

Group 1: This group stated that they understood the neighborhood wants control over character and agreed that the existing formula retail legislation is important. This group questioned how large of a threat subsidiaries are to character—and had a difficult time naming more than a handful of subsidiaries that could threaten neighborhood character. One member owned a number of restaurants and stated he would be okay with regulating his largest as a chain, if it reached the threshold. At the same time, he felt that his other restaurants are truly unique and very different. His expertise as a co-partner allows him to help others realize their restaurant dreams, but he doesn't see much benefit from economies of scale with his "one-offs". This group questioned the legality of any legislation that varied controls by the owner of the business.

Group 2: This group articulated several approaches to regulating subsidiaries. One member described how a new business sprung from a larger formula retailer is likely to be structured for quick expansion to multiple branches if the first is successful. During this group's discussion, the dialog centered on ideas for defining and regulating subsidiaries. (Summarized above and again below.)

1. Define subsidiaries by ownership 50% or more owned by formula retailer = subsidiary.
2. Define subsidiary by fiscal control, business model, and likelihood to become formula retail. (see Formula Retail, Subsidiaries, Control & Influence attachment)
3. Regulate subsidiaries who do not agree to restrict new locations as formula retail. (see attached flow chart). If owner agrees to restrict future locations, do not regulate as formula retail.
4. Regulate subsidiaries if the business has three or more locations, is owned by formula retailer, and itself has formula retail characteristics, as defined by the Planning Code.
5. Do not regulate subsidiaries; instead reduce formula retail threshold to five.
6. Do not regulate subsidiaries.

4. March 25, 3:00PM. Consensus Meeting.

The group sought to describe solutions that could be presented to the Planning Commission, the Small Business Commission, and the Board of Supervisors. Prior to the meeting, Planning staff and Supervisor Mar's staff distributed the ideas from the previous meeting to all members of the group. At the last meeting, the working group took two votes. The first vote was on the best proposed definition of "subsidiary." The second vote was on the best proposed regulatory structure, if any, for land use entitlement of a subsidiary. Thirteen members of the working group were present for voting. Prior to the vote, a protest was lodged stating concern that there was no subsidiary business owner seated on the working group. Staff responded that efforts were made to involve such business owners.

1. First Vote on the Best Definition of Subsidiary. Three choices were provided by the group:
 - A. **Define by ownership alone.** If a business is owned 50% or more by a company that meets the definition of formula retailer, then the business is a subsidiary. This definition received 3 votes.

- B. **Define subsidiary by fiscal control, business model, and likelihood to become formula retail.** (see Formula Retail, Subsidiaries, Control & Influence attachment) This definition received 5 votes.
- C. **None.** Neither of the above definitions is appropriate. The preference of neither definition received 5 votes.

Conclusion on Definitional Vote: Overall, the first vote showed that the group preferred a definition (8 votes) over no definition (5 votes). That said, individually, Option B (definition by fiscal control) tied with Option C (no definition) as the best solution for the definition.

2. Second Vote on the Best Regulatory Structure for Subsidiaries. Four choices were provided by the group:

- A. **Regulate subsidiaries in the same manner as formula retail if the subsidiary does not agree to limit future growth.** Do not regulate subsidiaries who sign an agreement restricting future growth. (See FR or Not decision flowchart). This regulatory structure received 5 votes.
- B. **Regulate a subsidiary if that new business has three or more locations and itself has the code defined characteristics of formula retail.** This regulatory structure received 4 votes.
- C. **Do not regulate subsidiaries; instead reduce the formula retail threshold to 3 or more businesses.** This regulatory structure received 0 votes.
- D. **Do not regulate subsidiaries. Keep existing the formula retail regulations as is.** This regulatory structure received 4 votes.

Conclusion on Regulatory Structure Vote: By one vote, the group preferred predicating regulation on the action of the business—subsidiaries that voluntarily agreed to limit future growth would not be regulated (5 votes for the flowchart structure vs. a tie for the two other vote getting options: 4 votes for starting regulation at three subsidiaries and 4 votes for no regulatory structure).

After the votes were tallied, the City Attorney asked the group members who may be interested in pursuit of legislation to describe a few issues. In particular, the following issues should be articulated: what is the harm of subsidiaries; what are the existing subsidiaries in San Francisco; and what are the negative impacts of subsidiaries on neighborhoods from a land use perspective.

Supervisor Mar's aide concluded the meeting with the following remarks. Supervisor Mar Appreciates the participation of all the attendees; it was not an easy discussion but it served the important function of informing us of a broad spectrum of ideas and opinions that will help shape whatever policies are developed. It was important to note all of the comments because we want to ensure that Supervisor Mar and all of the decision makers will have a clear idea of the breadth of the discussion and how different stakeholders feel about the various proposals. We do not have a solid timeline for drafting legislation but we will stay in contact with everybody in the working group and continue to elicit input as we move forward.

Working Group Ground Rules

1. **Formula Retail is newly regulated.** This group is not trying to change Formula Retail controls.
2. **Subsidiaries are not currently regulated.** This group is exploring if such regulation would be appropriate.
3. **Remember, we're learning from each other--** as such we ask for all to engage in open listening while others are sharing. All members have been invited because they have a contribution to make. Listen with openness to learning and empathy.
4. **Commit to work outside the group meetings.** Our work ahead is great and can best be tackled if we explore the issue and further our thinking in our time outside of the group meeting. Along these lines, we're asking that you consider the scope of the problem from your perspective. Which & how many categories of businesses currently are not considered formula retail? What problems, if any, are raised by this omission? What would you like to address?
5. **Be mindful of three legal concepts that may apply:**
 - i. Restrictions should *regulate the use*, not the user. Land use regulations should "run with the land" and should be focused on the land use, not on the user or the holder of the land use entitlement. Any proposed formula retail regulations should be able to be characterized as regulating a land use, not the user itself.
 - ii. Government regulation should *not be used solely or primarily to suppress economic competition*. While government regulation may have incidental anti-competitive effects, if the primary purpose of the government regulation is an anti-competitive one, courts will scrutinize the regulations very carefully.
 - iii. *Commerce Clause Concerns*: Under the Commerce Clause of the United States Constitution, local governments may not inhibit interstate commerce by prohibiting non-local businesses, or by using regulations to make it more difficult for non-local businesses to locate or do business in an area. Any legislation should not, on its face, discriminate against out-of-state businesses, or "local" vs. "non-local" businesses.
6. **Public Comment.** Public comment will occur at the end of the meeting. Each speaker will be allotted a three minute maximum comment time, with a maximum public comment of 20 minutes. Comments shall pertain to the topic of subsidiaries.