
A BILL FOR AN ACT

RELATING TO TAXATION.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF HAWAII:

1 SECTION 1. The legislature finds that, despite recent laws
2 to address the problems associated with the general excise tax,
3 many unresolved issues remain that adversely affect the business
4 community, especially small businesses.

5 A major concern involves the administration of wholesale
6 sales of services under the general excise tax. Presently, the
7 law is unclear as to the distinction between what is consumed as
8 overhead and what is an "identifiable element" benefiting a
9 customer. This distinction is important for two reasons.

10 First, the distinction determines whether additional
11 general excise tax assessments are added onto a service before
12 it reaches the consumer. Since most small businesses are not
13 vertically integrated (part of a larger corporate structure) and
14 therefore contract-out many services, the general excise tax
15 assessed on these services raises the overall cost of doing
16 business.



1 Second, the lack of a distinction has led to confusion in
2 the business community because of arbitrary interpretations of
3 the law, as well as enforcement and tax compliance problems.

4 The purpose of this Act is to clarify the general excise
5 tax law by expanding the treatment of wholesale sales of
6 services, by eliminating the requirement that the cost of
7 services does not constitute overhead and by providing a
8 definition of "identifiable element".

9 SECTION 2. Section 237-1, Hawaii Revised Statutes, is
10 amended by adding a new definition to be appropriately inserted
11 and to read as follows:

12 "Identifiable element" means direct and indirect costs of
13 tangible personal property that must be capitalized with respect
14 to property that is produced, manufactured, or acquired for
15 resale. Direct costs of tangible personal property include
16 costs that become an integral part of the subject matter that is
17 produced, manufactured, or acquired for resale and are not
18 consumed as overhead. Indirect costs of tangible personal
19 property include all costs of tangible personal property other
20 than direct costs and include parts, supplies, office supplies,
21 fuel, and other indirect costs subject to the uniform
22 capitalization rules of section 263A (with respect to

1 capitalization and inclusion in inventory costs of certain
2 expenses) of the Internal Revenue Code of 1986, as amended."

3 SECTION 3. Section 237-4, Hawaii Revised Statutes, is
4 amended by amending subsection (a) to read as follows:

5 "(a) "Wholesaler" or "jobber" applies only to a person
6 making sales at wholesale. Only the following are sales at
7 wholesale:

8 (1) Sales to a licensed retail merchant, jobber, or other
9 licensed seller for purposes of resale;

10 (2) Sales to a licensed manufacturer of materials or
11 commodities that are to be incorporated by the
12 manufacturer into a finished or saleable product
13 (including the container or package in which the
14 product is contained) during the course of its
15 preservation, manufacture, or processing, including
16 preparation for market, and that will remain in such
17 finished or saleable product in such form as to be
18 perceptible to the senses, which finished or saleable
19 product is to be sold and not otherwise used by the
20 manufacturer;

21 (3) Sales to a licensed producer or cooperative
22 association of materials or commodities that are to be

1 incorporated by the producer or by the cooperative
2 association into a finished or saleable product that
3 is to be sold and not otherwise used by the producer
4 or cooperative association, including specifically
5 materials or commodities expended as essential to the
6 planting, growth, nurturing, and production of
7 commodities that are sold by the producer or by the
8 cooperative association;

9 (4) Sales to a licensed contractor, of materials or
10 commodities that are to be incorporated by the
11 contractor into the finished work or project required
12 by the contract and that will remain in such finished
13 work or project in such form as to be perceptible to
14 the senses;

15 (5) Sales to a licensed producer, or to a cooperative
16 association described in section 237-23(a)(7) for sale
17 to a licensed producer, or to a licensed person
18 operating a feed lot, of poultry or animal feed,
19 hatching eggs, semen, replacement stock, breeding
20 services for the purpose of raising or producing
21 animal or poultry products for disposition as
22 described in section 237-5 or for incorporation into a



1 manufactured product as described in paragraph (2) or
2 for the purpose of breeding, hatching, milking, or egg
3 laying other than for the customer's own consumption
4 of the meat, poultry, eggs, or milk so produced;
5 provided that in the case of a feed lot operator, only
6 the segregated cost of the feed furnished by the feed
7 lot operator as part of the feed lot operator's
8 service to a licensed producer of poultry or animals
9 to be butchered or to a cooperative association
10 described in section 237-23(a)(7) of such licensed
11 producers shall be deemed to be a sale at wholesale;
12 and provided further that any amount derived from the
13 furnishing of feed lot services, other than the
14 segregated cost of feed, shall be deemed taxable at
15 the service business rate. This paragraph shall not
16 apply to the sale of feed for poultry or animals to be
17 used for hauling, transportation, or sports purposes;

18 (6) Sales to a licensed producer, or to a cooperative
19 association described in section 237-23(a)(7) for sale
20 to the producer, of seed or seedstock for producing
21 agricultural and aquacultural products, or bait for
22 catching fish (including the catching of bait for



1 catching fish), which agricultural and aquacultural
2 products or fish are to be disposed of as described in
3 section 237-5 or to be incorporated in a manufactured
4 product as described in paragraph (2);

5 (7) Sales to a licensed producer, or to a cooperative
6 association described in section 237-23(a)(7) for sale
7 to such producer; of polypropylene shade cloth; of
8 polyfilm; of polyethylene film; of cartons and such
9 other containers, wrappers, and sacks, and binders to
10 be used for packaging eggs, vegetables, fruits, and
11 other agricultural and aquacultural products; of
12 seedlings and cuttings for producing nursery plants or
13 aquacultural products; or of chick containers; which
14 cartons and such other containers, wrappers, and
15 sacks, binders, seedlings, cuttings, and containers
16 are to be used as described in section 237-5, or to be
17 incorporated in a manufactured product as described in
18 paragraph (2);

19 (8) Sales of tangible personal property:
20 (A) To a licensed seller engaged in a service
21 business or calling; provided that:

1 (i) The property is not consumed or incidental
2 to the performance of the services;

3 (ii) There is a resale of the article at the
4 retail rate of four per cent; and

5 (iii) The resale of the article is separately
6 charged or billed by the person rendering
7 the services;

8 (B) Where:

9 (i) Tangible personal property is sold upon the
10 order or request of a licensed seller for
11 the purpose of rendering a service in the
12 course of the person's service business or
13 calling, or upon the order or request of a
14 person subject to tax under section 237D-2
15 for the purpose of furnishing transient
16 accommodations;

17 (ii) The tangible personal property becomes or is
18 used as an identifiable element of the
19 service rendered; and

20 (iii) The cost of the tangible personal property
21 does not constitute overhead to the licensed
22 seller;



1 the sale shall be subject to section 237-13.3; or

2 (C) Where the taxpayer is subject to both
3 subparagraphs (A) and (B), then the taxpayer
4 shall be taxed under subparagraph (A).

5 Subparagraphs (A) and (C) shall be repealed on
6 January 1, 2006;

7 (9) Sales to a licensed leasing company of capital goods
8 that have a depreciable life, are purchased by the
9 leasing company for lease to its customers, and are
10 thereafter leased as a service to others;

11 (10) Sales of services to a licensed seller engaging in a
12 business or calling whenever:

13 (A) [~~Either:~~] Any of the following is the case:

14 (i) In the context of a service-to-service
15 transaction, a service is rendered upon the
16 order or request of a licensed seller for
17 the purpose of rendering another service in
18 the course of the seller's service business
19 or calling;

20 (ii) In the context of a service-to-tangible
21 personal property transaction, a service is
22 rendered upon the order or request of a



1 licensed seller for the purpose of
2 manufacturing, producing, or preparing
3 tangible personal property to be sold;

4 (iii) In the context of a services-to-contracting
5 transaction, a service is rendered upon the
6 order or request of a licensed contractor as
7 defined in section 237-6 for the purpose of
8 assisting that licensed contractor; or

9 (iv) In the context of a services-to-transient
10 accommodations rental transaction, a service
11 is rendered upon the order or request of a
12 person subject to tax under section 237D-2
13 for the purpose of furnishing transient
14 accommodations;

15 (B) The benefit of the service passes directly or
16 indirectly to the customer of the licensed
17 seller, licensed contractor, or person furnishing
18 transient accommodations [~~as an identifiable~~
19 ~~element of the other service or property to be~~
20 ~~sold, the contracting, or the furnishing of~~
21 ~~transient accommodations;~~



1 ~~(C)~~ ~~The cost of the service does not constitute]; or~~
2 the benefit of the service is consumed as
3 overhead to the licensed seller, licensed
4 contractor, or person furnishing transient
5 accommodations;

6 [~~(D)~~] (C) The gross income of the licensed seller is
7 not divided between the licensed seller and
8 another licensed seller, contractor, or person
9 furnishing transient accommodations for
10 imposition of the tax under this chapter;

11 [~~(E)~~] (D) The gross income of the licensed seller is
12 not subject to a deduction under this chapter or
13 chapter 237D; and

14 [~~(F)~~] (E) The resale of the service, tangible personal
15 property, contracting, or transient
16 accommodations is subject to the tax imposed
17 under this chapter at the highest tax rate.

18 Sales subject to this paragraph shall be subject to
19 section 237-13.3;

20 (11) Sales to a licensed retail merchant, jobber, or other
21 licensed seller of bulk condiments or prepackaged
22 single-serving packets of condiments that are provided



1 to customers by the licensed retail merchant, jobber,
2 or other licensed seller;

3 (12) Sales to a licensed retail merchant, jobber, or other
4 licensed seller of tangible personal property that
5 will be incorporated or processed by the licensed
6 retail merchant, jobber, or other licensed seller into
7 a finished or saleable product during the course of
8 its preparation for market (including disposable,
9 nonreturnable containers, packages, or wrappers, in
10 which the product is contained and that are generally
11 known and most commonly used to contain food or
12 beverage for transfer or delivery), and which finished
13 or saleable product is to be sold and not otherwise
14 used by the licensed retail merchant, jobber, or other
15 licensed seller;

16 (13) Sales of amusements subject to taxation under section
17 237-13(4) to a licensed seller engaging in a business
18 or calling whenever:

19 (A) ~~[Either:]~~ Any of the following is the case:

20 (i) In the context of an amusement-to-service
21 transaction, an amusement is rendered upon
22 the order or request of a licensed seller



1 for the purpose of rendering another service
2 in the course of the seller's service
3 business or calling;

4 (ii) In the context of an amusement-to-tangible
5 personal property transaction, an amusement
6 is rendered upon the order or request of a
7 licensed seller for the purpose of selling
8 tangible personal property; or

9 (iii) In the context of an amusement-to-amusement
10 transaction, an amusement is rendered upon
11 the order or request of a licensed seller
12 for the purpose of rendering another
13 amusement in the course of the person's
14 amusement business;

15 (B) The benefit of the amusement passes to the
16 customer of the licensed seller as an
17 identifiable element of the other service,
18 tangible personal property to be sold, or
19 amusement;

20 (C) The cost of the amusement does not constitute
21 overhead to the licensed seller;



1 (D) The gross income of the licensed seller is not
 2 divided between the licensed seller and another
 3 licensed seller, person furnishing transient
 4 accommodations, or person rendering an amusement
 5 for imposition of the tax under chapter 237;

6 (E) The gross income of the licensed seller is not
 7 subject to a deduction under this chapter; and

8 (F) The resale of the service, tangible personal
 9 property, or amusement is subject to the tax
 10 imposed under this chapter at the highest rate.

11 As used in this paragraph, "amusement" means
 12 entertainment provided as part of a show for which
 13 there is an admission charge. Sales subject to this
 14 paragraph shall be subject to section 237-13.3; and

15 (14) Sales by a printer to a publisher of magazines or
 16 similar printed materials containing advertisements,
 17 when the publisher is under contract with the
 18 advertisers to distribute a minimum number of
 19 magazines or similar printed materials to the public
 20 or defined segment of the public, whether or not there
 21 is a charge to the persons who actually receive the
 22 magazines or similar printed materials."

1 SECTION 4. Statutory material to be repealed is bracketed
2 and stricken. New statutory material is underscored.

3 SECTION 5. This Act shall take effect upon its approval
4 and shall apply to taxable years beginning after December 31,
5 2005.

6

INTRODUCED BY:

A handwritten signature in cursive script, appearing to read "Gus Hawkins", is written over a horizontal line.

JAN 25 2006



HB 2817

Report Title:

General Excise Tax; Identifiable Element

Description:

Expands the treatment of wholesale sales of services by eliminating the requirement that the cost of services provided does not constitute overhead and provides a definition of "identifiable element" to provide consistent and fair administration of the general excise tax.

