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## HOUSE COMMITTEE ON FINANCE

### TESTIMONY REGARDING SB 1678 SD 3 RELATING TO TAXATION

TESTIFIER: KURT KAWAFUCHI, DIRECTOR OF TAXATION (OR DESIGNEE)

DATE: MARCH 25, 2009

TIME: 4PM

ROOM: 308

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The intent of this bill is to conform Hawaii law to the requirements of the Streamlined Sales and Use Tax Agreement ("SSUTA"). The Streamlined Sales and Use Tax Agreement is a method developed by the states and businesses primarily to have internet and catalogue sellers voluntarily collect the sales and use tax from consumers on behalf of the States for those sellers who did not have nexus with the state. Currently, people who buy from catalogues and the internet are supposed to pay use tax on their purchases, however in practice, few do.<sup>1</sup> This bill would provide a *voluntary* mechanism for internet and catalogue sellers to collect this tax from the consumers and pass it on to the Department, thereby resulting in a net revenue gain to the State.

The Department of Taxation ("Department") **opposes this bill in the current economy and opposes its current referral and amendments to divert revenue from the general fund.**

The Department also **proposes an alternative mechanism to capture the same revenue more effectively and efficiently.**

#### I. **CONCERN OVER THIS LEGISLATION IN A SLOWING ECONOMY**

Initially, the Department points out that it is a well-settled principle of economics that when an economy is slowing, increasing taxes is strongly discouraged because people are already struggling to make ends meet financially. During economic slowing, economics suggests that money should remain with the people and in the economy in order to boost economic performance. The Department cautions further consideration of this legislation during a slowing economy based upon these economic concepts.

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<sup>1</sup> However, businesses generally comply with the use tax more than individuals.

**II. OPPOSED TO PASSING THIS MEASURE WITHOUT A HEARING BEFORE THE ECONOMIC REVITALIZATION COMMITTEE**

The Department strongly opposes that this measure did not receive a referral, nor a hearing before the House Committee on Economic Revitalization, Business & Military Affairs. As the House committee charged with managing the legislative affairs of those measures that directly impact businesses and the economy, this measure should be held and re-referred to the Economic Revitalization committee for its consideration and input. Just as this measure was considered before the Senate Committee on Economic Development & Technology, so too should this measure be fairly heard before the House economic and business committee.

**III. OPPOSED TO REVENUE DIVERSION FROM THE GENERAL FUND**

This measure was amended on the Senate floor to provide a portion of the revenues received from the streamlined sales tax project to fund higher education. The Department opposes revenue diversions, especially from the general fund during the budget shortfall currently facing the State. Though funding education is important, balancing a budget is critical this session.

The Department cannot support GET revenue diversions. The Department is always cautious about policy that redirects general excise tax revenue away from the general fund and into specific special funds. The Department routinely opposes funding mechanisms such as this because the general excise tax represents over one-half of the State's overall operating revenue stream. The Department strongly prefers that a direct appropriation be the means for funding the programs of the University of Hawaii so that the amount may be budgeted and prioritized just as any other program.

**IV. CONCERNS REGARDING IMPLEMENTATION OF SSUTA IN HAWAII.**

1. **Adds Complexity.** Because Hawaii has a general excise tax imposed on the seller rather than a sales tax, which is imposed on the buyer, the provisions of the SSUTA do not fit neatly into Hawaii's general excise tax regime. Therefore, the SSUTA provisions need to be modified to take Hawaii's different tax structure into account.

In addition, to comply with the SSUTA's requirement that the State and each local taxing jurisdiction have only one rate, except in certain circumstances not applicable in Hawaii, the different tax rates applicable under Hawaii general excise tax law need to be removed from the general excise tax chapter and shifted into another taxing chapter. The creation of three new chapters also adds complexity to Hawaii's tax law and may prove to be another source of confusion to taxpayers.

In addition, whether the approach taken in the bill would be considered a "replacement tax" is an issue. It is also unclear at this time whether replacement taxes are permitted under the SSUTA.

2. **Provides Amnesty.** The SSUTA requires the State to provide amnesty to out-of-state

sellers that may or may not have nexus with the State. The State will be giving up its right to pursue these sellers for general excise tax on their operations in the State.

3. **Vendor Compensation.** The SSUTA requires the State to compensate out-of-state vendors who voluntarily participate in the SSUTA for collecting the Hawaii tax. However, in-state businesses that are obligated to pay the Hawaii tax are not compensated for collecting and paying the tax.
4. **Voluntary.** Currently, participation by sellers pursuant to the SSUTA is voluntary. While hundreds of companies have agreed to participate, Amazon.com and eBay have indicated that they will not participate at this time. Therefore, it is unclear how much potential revenue will be generated for Hawaii by participating in SSUTA. Federal legislation could also change this.
5. **"Home Rule" Concerns.** Participation in SSUTA requires the State to annually certify to the national governing board that the state's laws are in compliance with SSUTA. Therefore, **any tax law changes in the future must meet the requirements of SSUTA** in order for the State to continue to comply with SSUTA. Therefore, **the State is limiting its ability to adopt legislation in favor of decisions made by a national governing board regarding a state's tax law.**

In addition, now that the City and County of Honolulu has enacted the county surcharge, the City and County of Honolulu must be bound to follow the SSUTA with respect to the surcharge.

6. **Appropriations.** The Department will need an appropriation to implement the SSUTA compliance, which, among other things, requires the development of a database of zip codes and tax rates. The Department is currently working on developing an accurate and comprehensive cost estimate for implementing this legislation. The complexity associated with updating the Department's current tax collection systems and the required labor and incidental costs require further analysis. The resource cost has not been factored into the budget and will provide additional stress on budgeting and the financial plan this legislative session.
7. **Further Study.** The Department believes that further study is warranted on this issue. The general excise tax is a major revenue source for the State and any substantial revisions, such as those contained in this bill, should only be enacted after a thorough and thoughtful analysis can be done. In addition, time would also enable the Department to learn from other states' experiences with the SSUTA. Other states did not actually begin implementing SSUTA until late 2005. On this date, nineteen states<sup>2</sup> have become full members of SSUTA and begun implementing SSUTA. If the State waits, it could

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<sup>2</sup> The full member states are Arkansas, Indiana, Iowa, Kansas, Kentucky, Michigan, Minnesota, Nebraska, Nevada, New Jersey, North Carolina, North Dakota, Oklahoma, Rhode Island, South Dakota, Vermont, Washington, West Virginia, Wyoming.

learn from the problems the other states' experience. Some states remain cautiously guarded about implementing the SSUTA. For example, New York issued a report that cautioned joining the project because it was unclear whether the project would yield net benefits to taxpayers and local businesses. Again, further study of these paramount issues is advised.

### III. GENERAL COMMENTS.

**Delayed Effective Date**—The delayed effective date of the bill is appreciated, but the delay may not be long enough to allow these changes to be fully integrated into the computer systems of the Department. A longer delayed effective date would give time for practitioners and businesses to adjust to these changes. When the corporate statutes were substantially revised, the effective date was delayed one year to allow professional associations, businesses, and practitioners sufficient time to analyze the changes in the law, prepare conferences, or other industry analysis. Given the challenges the Department would face integrating such large, wholesale changes into its operations, longer than two years may be more realistic of a time frame. The delayed effective date would also provide time to obtain approval from the National SSTP Governing Board to assure that Hawaii's amendments conform to the SSUTA. This is very important since Hawaii's general excise tax is not a sales tax.

**Frequent Changes to the SSUTA Will Require Legislative Action.** The legislature needs to be aware that the SSUTA is not a static document. It has undergone substantial and frequent changes since it was adopted on November 12, 2002. It has been amended 16 times.<sup>3</sup> It has been amended 12 times since the SSUTA became effective on October 3, 2005. Each change requires member States to amend its law in order to remain in conformity with the SSUTA. The debate at the Governing Board meetings currently includes allowing intra-state origin based taxes, the extension of associate member status beyond the original deadline, and very relevant to this bill, the issue of using "replacement taxes" by States to circumvent the provisions of the SSUTA, such as New Jersey's fur tax.<sup>4</sup>

### IV. REVENUE IMPACT & START UP COSTS

**Joining the SSUTA would entail start-up costs in the first year and annual ongoing costs.**

The bill will have little revenue impact, unless Congress enacts required legislation. However, the expense of the oversight committee would be incurred. If the required Congressional legislation is enacted, the effect on revenues is indeterminate, but it could be \$25 million annually in additional GET and Use Tax collections. Without the federal legislation, the revenue gain is estimated to be \$1-\$5 million. The exemption for blind, deaf, and disabled taxpayers would cost

<sup>3</sup> November 19, 2003, November 16, 2004, April 16, 2005, October 1, 2005, January 13, 2006, April 18, 2006, August 30, 2006, December 14, 2006, June 23, 2007, September 20, 2007, December 12, 2007, April 2, 2008, June 18, 2008, September 5, 2008, December 6, 2008, and February 26, 2009.

<sup>4</sup> As of January 1, 2009, New Jersey repealed its fur tax, delaying resolution of the replacement tax issue.



about \$500,000 annually.

**V. POTENTIAL ALTERNATIVE TO COLLECT USE TAX**

In the interest of shoring up revenue collections without implementing a tax increase, the Department suggests that, in lieu of SSTP, the Legislature consider enacting a use tax amnesty provision in the income tax law that would require taxpayers to answer on their income tax return whether they imported internet or other tax-free purchases into Hawaii.

If the taxpayer answers "YES" on the return, they could be given the opportunity to insert the actual amount of tax owed, or as is more likely the case, where taxpayers do not have records, the legislation could provide for a use tax amnesty/settlement amount based upon adjusted gross income or other measurement that could be added to the income tax return as tax owed. In short, the legislation could utilize the income tax return, which nearly all Hawaii residents file, as a means of educating taxpayers of the use tax liability, giving them the simple means of payment through the income tax regime, and where records do not exist, the legislation could provide an amnesty amount (*i.e.*, a \$10 amnesty is equal to approximately \$250 in imported purchases). Therefore, for example, in exchange for a \$10 payment on their income tax return, a taxpayer would be treated as having satisfied their use tax liability for the year. Exceptions could be provided if the taxpayer purchased items subject to the use tax with a large cost, such as cars, boats, and jewelry. All of this revenue would be additional revenue to the general fund without all of the costs that are required with the SSUTA.



# UNIVERSITY OF HAWAII SYSTEM

## Legislative Testimony

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Testimony Presented Before the  
House Committee on Finance  
March 25, 2009 at 4:00 pm

by  
Howard Todo  
Vice President for Budget & Finance/CFO, University of Hawai'i

SB 1678 SD3 – RELATING TO TAXATION

Chair Oshiro, Vice Chair Lee, and Members of the Committee:

The University of Hawaii is in support of Section 19 of the bill which provides that

(4) A sum equal to \_\_\_ per cent of all tax revenues realized by the State under chapters A, B, and C, respectively, from the effective date of this Act through December 31, 2014, shall be deposited in the state treasury in each fiscal year to the credit of the University of Hawaii to fund high-priority higher education programs; provided that any moneys received under this section shall augment and not replace existing operating or capital improvement budgets; provided further that beginning January 1, 2015, all revenues realized by the State under chapters A, B, and C shall be deposited in the state treasury.

This provision will provide an additional source of funding for high-priority higher education programs.

Thank you for the opportunity to present testimony and for your continuing support of the University of Hawaii.



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**Roger K. Takabayashi**  
President

**Wil Okabe**  
Vice President

**Karolyn Mossman**  
Secretary-Treasurer

**Mike McCartney**  
Executive Director

TESTIMONY BEFORE THE HOUSE COMMITTEE ON  
FINANCE

RE: SB 1678, SD3 – RELATING TO TAXATION.

March 25, 2009

ROGER TAKABAYASHI, PRESIDENT  
HAWAII STATE TEACHERS ASSOCIATION

Chair Oshiro and Members of the Committee:

The Hawaii State Teachers Association support SB 1678, SD3, which adopts amendments to Hawaii tax laws to implement the streamlined sales and use tax agreement.

Given the current economic situation in which budget cuts are jeopardizing our education system, HSTA believes this bill will generate the funds needed to relieve the State's budget shortfall and restore cuts made to education. We also believe it is unfair that brick-and-mortar retail businesses must bear the burden of state taxes on their sales transactions when internet merchants do not. We believe internet businesses should pay the same taxes as their traditional retail counterparts.

Thank you for the opportunity to testify.



## HAWAII GOVERNMENT EMPLOYEES ASSOCIATION

AFSCME Local 152, AFL-CIO

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### The Twenty-Fifth Legislature, State of Hawaii House of Representatives Committee on Finance

Testimony by  
Hawaii Government Employees Association  
March 25, 2009

### S.B. 1678, S.D. 3 – RELATING TO TAXATION

The Hawaii Government Employees Association supports the purpose and intent of S.B. 1678, S.D. 3, which is to make specific changes to Hawaii's tax law that will enable the State to participate in the Streamlined Sales and Use Tax Agreement to permit the taxation of Internet-based transactions. There are several reasons for taxing Internet-based transactions.

Retail trade has been transformed by the Internet. As the popularity of "e-commerce" grows, fairness dictates that Internet-based transactions should be treated in the same manner as other retail transactions. Retail transactions that are taxable by "bricks and mortar" retailers should also be taxable when sold through the Internet.

Hawaii has already lost millions of dollars in Internet-based sales, and the losses will likely increase as the importance of the Internet continues to grow. Therefore, we support S.B. 1678, S.D. 3 that makes necessary changes to the tax code to comply with the Streamlined Sales and Use Tax Agreement. The ongoing loss of millions in tax revenue from e-commerce is a problem that will get worse over time unless we take appropriate action. The revenues gained through the Streamlined Sales and Use Tax Agreement may be used to fund public education and other important priorities.

Thank you for the opportunity to testify in support of this important measure.

Respectfully submitted,

Nora A. Nomura  
Deputy Executive Director



March 25, 2009

Relating to SB 1678 SD 3  
Testifying in Support  
On Behalf of  
The Democratic Party of Hawai'i

Dear Chair Oshiro, Vice-Chair Lee, and Members of the House Finance Committee,

Mahalo for this opportunity to present testimony in strong support of Senate Bill 1678, Senate Draft 3 relating to taxation.

This is a bill that would allow the State to collect millions of additional tax dollars that it is currently unable to collect. Nationally, it has been estimated that the loss of revenue resulting from sales and use taxes not collected by state and local governments was in the range of \$21.5 to \$33.6 billion in 2008.

Hawai'i is one of ten states whose estimated revenue losses are projected to be more than 6% of its total GET/use tax revenues. Against actual FY07 revenues of \$2.55 billion in GET/use tax revenues, this amount would have been \$153.34 million. Hawai'i's participation in the SSUTA could result in an estimated \$174 million in additional tax revenues for the State budget for fiscal year 2010, and even larger amounts in subsequent years.

In Congress, Streamlined Sales Tax legislation has been co-sponsored by Senator Daniel Inouye and Congressman Neil Abercrombie. Such legislation authorizes states that fully comply with the Streamlined Sales and Use Tax Agreement (SSUTA) to require sellers to collect sales and use taxes owed on all remote transactions. Currently, 22 states, representing over 30% of the country's population have already been certified as being in compliance with the SSUTA.

What's more, the state legislature has already laid the foundation for becoming a participating member of the SSUTA by enacting Act 173 SLH 2003 and Act 3 Special SLH 2005.

In these difficult economic times, participation in the SSUTA would only help increase tax revenues for the State of Hawai'i, and thus help close the gap on the fiscal shortfall the state currently faces.

Mahalo for your time and consideration.

Aloha,  
Brian Schatz  
Chair, Democratic Party of Hawai'i  
1050 Ala Moana Blvd. #2660  
Honolulu, HI 96814



For: Public Hearing on Wednesday, 3/25/09, 4:00 am Room 308

Re: Testimony in Support of SB1678

From: Democratic Party of Hawai'i

Dear Chair Marcus Oshiro, Vice Chair Marilyn Lee and members of the House Finance Committee:

Thank you for the opportunity to testify before this committee. The Democratic Party of Hawai'i supports SB1678 SD3, which would allow Hawaii to participate in the streamlined sales and use tax agreement.

At its 2008 State Convention the Democratic Party, with support of delegates assembled, declared its support for the implementation of the streamlined sales and use tax agreement (resolution Busin 08-16 attached). By collecting a tax that is technically already owed, this implementation could help close the budget gap during these tough economic times. It could also help local businesses stay competitive with those out of state who do not currently charge excise taxes.

Respectfully submitted,

Rachel Orange, Co-Chair  
Legislation Committee of the State Central Committee,  
Democratic Party of Hawai'i



## **BUSIN 08-16 URGING THE STATE OF HAWAI'I TO ADOPT LEGISLATION TO PARTICIPATE IN THE STREAMLINED SALES AND USE TAX AGREEMENT**

**Whereas**, state and local governments lost at least \$16.7 to \$20.4 billion in 2004 in uncollected sales and use taxes for remote transactions, and the loss is estimated to grow to \$21.5 to \$33.6 billion by 2008; and

**Whereas**, the National Streamlined Sales and Use Tax Agreement (SSUTA) substantially simplifies state and local sales tax systems, improves the burdens to interstate commerce that were of concern to the Supreme Court, protects state sovereignty, and "levels the playing field" between local and out-of-state merchants; and

**Whereas**, 22 states—representing over 30% of the country's population—have already been certified as being in compliance with the Streamlined Sales and Use Tax Agreement and approximately 1,100 remote sellers have voluntarily collected almost \$115 million in previously-uncollected sales tax revenues from these volunteer sellers; and

**Whereas**, in order to participate in the SSUTA, Hawai'i must amend its tax law in conformity with the broad principles of the agreement and has laid the foundation for becoming a participating member by enacting Act 173, SLH 2003 and Act 3, Special SLH 2005; and

**Whereas**, federal legislation co-sponsored by U.S. Senator Daniel Inouye (U.S. Senate), and by U.S. Congressman Neil Abercrombie (U.S. House of Representatives) was introduced last fall, which authorizes states that fully comply with the Streamlined Sales and Use Tax Agreement to require out-of-state sellers to collect sales and use taxes owed on catalog, mail-order and online sales to its residents; and

**Whereas**, federal legislation endorsing SSUTA is anticipated to pass in 2009, which will enable states participating in the SSUTA to immediately being collected uncollected sales and use tax revenues from out-of-state retailers; and

**Whereas**, Hawai'i's participation in the SSUTA could result in an estimated \$174 million in additional tax revenues for the State budget for fiscal year 2010, and even larger amounts in subsequent years; and

**Whereas**, recent versions of Hawai'i SSUTA legislation proposed to distribute %100 of the additional tax revenues collected under the SSUTA to the Department of Education and the University of Hawai'i, on an equal basis, to fund educational programs and capital improvement projects between 2010 and 2015; now, therefore

**Be It Resolved** by the Democratic Party of Hawai'i that the Legislature is urged to adopt legislation for the State of Hawai'i to implement the Streamlined Sales and Use Tax Agreement; and

**Be it Further Resolved** that beginning in calendar year 2014, the Department of Education and the University of Hawai'i are requested to assess the adequacy of the tax revenues collected under the SSUTA in meeting their educational and infrastructure needs and to report their findings to the Legislature no later than 20 days prior to the convening of the Regular Session of 2015; and

**Be It Further Resolved** that certified copies of this resolution be transmitted to the Governor of the State of Hawai'i, Board of Education, University of Hawai'i Board of Regents, Democratic members of the Hawai'i State Legislature, appropriate committee(s) of the State Democratic Convention, the Director of Taxation, and candidates for Hawai'i State Legislative offices.

# TAXBILLSERVICE

126 Queen Street, Suite 304

TAX FOUNDATION OF HAWAII

Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: MISCELLANEOUS, Streamlined sales and use tax

BILL NUMBER: SB 1678, SD-3

INTRODUCED BY: Senate Floor Amendment No. 1

BRIEF SUMMARY: Adds a new chapter to the law to set out sections of HRS chapter 237 which establish transactions subject to the 0.5% general excise tax rate.

Adds a new chapter to the law to set out sections of HRS chapter 238 which establish transactions subject to the 0.5% use tax rate.

Adds a new chapter to the law to set out sections of HRS chapter 237 which establish transactions subject to the 0.15% general excise tax rate. The measure delineates provisions governing commissioned sellers of insurance to replace reference to agents, general agents, subagents, or solicitors with the term "insurance producers."

Adds several new sections to HRS chapter 237 to establish sourcing rules to determine when a product or service is taxed, including telecommunication services. The measure delineates provisions defining "direct mail" and how the sourcing of direct mail transactions will be ascertained.

Adds a new section to HRS chapter 237 to allow a seller to take a deduction from taxable sales for bad debts.

Adds several sections to HRS chapter 255D to establish provisions relating to the determination of the proper general excise or use tax rates between different tax jurisdictions, rounding on tax computations, amnesty for registered sellers who pay, collect, or remit general excise or use taxes in accordance with the terms of the streamlined sale and use tax agreement, tax rate changes by a county, certified service provider, confidentiality of records, liability for uncollected tax and rate changes, and customer refund procedures.

Amends HRS sections 237-8.6 and 238.2.6 to prohibit a county to conduct an independent audit of sellers registered under the streamlined sales and use tax agreement.

Amends HRS section 237-24.3 to redefine the term "prosthetic device."

Amends HRS section 237-31 to provide that \_\_\_% of all tax revenues realized under the newly restructured chapters (formerly HRS chapter 237) shall be deposited into the state treasury to the credit of the University of Hawaii to fund high-priority higher education programs; provided that such moneys shall augment and not replace existing operating or capital improvement budgets from the effective date of this act through December 31, 2014. Beginning on January 1, 2015 all tax revenues realized under the newly restructured chapters (formerly HRS chapter 237) shall be deposited into the state treasury.

Establishes a committee to oversee the department of taxation's implementation, administration, and compliance of the streamlined sales and use tax agreement. The committee shall be administratively attached to the department of taxation. Requires the committee to hold meetings to carry out this act and serve as the state's official delegation to the streamlined sales and use tax agreement governing board when establishing the state's criteria for compliance.

Permits the department of taxation to seek technical assistance with legal professionals that have a background and practice in taxation. Allows the department of taxation to secure services in an expeditious manner as soon as possible without regard to HRS chapter 103D. The legislative reference bureau shall assist the department of taxation or contractor in drafting any legislation.

It shall be unlawful for any person or employee of the state to make known information imparted by any tax return or permit any tax return to be seen or examined by any person. Also provides that it shall be lawful to allow a private contractor to inspect any tax return of any taxpayer, or to furnish the private contractor with any information concerning any item on a return only for the purposes of conforming the state's general excise and use taxes to be operative for the Streamlined Sales Tax Project's Model Agreement and Act.

This act shall take effect on the later of January 1, 2010 or when the U.S. Congress enacts legislation overturning *Quill v. North Dakota*, 504 U.S. 298 (1002) by consenting to the Streamlined Sales and Use Tax Agreement.

**EFFECTIVE DATE:** Upon approval as noted in the measure

**STAFF COMMENTS:** The Streamlined Sales Tax Project's Model Agreement and Act is a project undertaken with other states that is intended to simplify sales and use tax administration as it relates to multiple sales and use tax rates, definitions, and taxing jurisdictions.

Goals of the project include the establishment of a single sales tax rate, uniform definitions of sales and use tax terms, requiring states to administer any sales and use taxes, and a central electronic registration system to allow a seller to register to collect and remit sales and use taxes for all states.

At the national level, there appears to be a number of difficulties in the negotiations and unanimous agreement is far from reality. Before jumping on the band wagon, lawmakers should exercise care as it should be remembered that Hawaii does not have a sales tax as found in other states. To the contrary, the general excise tax, while viewed as a sales tax, is a far cry from the retail sales tax structure found on the mainland.

The 2005 legislature had approved a measure to direct the department of taxation to identify issues that need to be resolved to effectuate the orderly enactment and operation of a streamlined sales and use tax based on the Streamlined Sales Tax Project's Model Agreement and Act. The act also repealed the streamlined sales and use tax advisory committee council which was to consult with the department of taxation on the implementation of the streamlined sales and use tax agreement in Hawaii. When this measure was sent to the governor, the governor vetoed it due to the repeal of the advisory council, unrealistic deadlines in the measure, and concerns of allowing a third party to access confidential tax return information. A special session of the legislature overrode the governor's veto and the measure passed as Act 3 of the Special Session of 2005.

Basically the measure attempts to turn Hawaii's gross receipts tax imposed for the privilege of doing business in Hawaii into a retail sales tax structure with respect to where the tax is imposed. Much of the bill is devoted to separating the wholesale imposition of the tax from the retail and then reworking where the tax is applied otherwise known as "sourcing." The general excise tax, as we know it today, would be radically changed to accommodate the format adopted by the Streamline Sales Tax Project (SSTP).

What is not evident in the measure is that by participating in the consortium known as the SSTP, Hawaii businesses will be required to collect the sales taxes of other states when purchases are made by residents of that state. The cost of collecting, accounting, and remitting those taxes will add even more overhead costs to operating a business in Hawaii. So why is there such enthusiasm on the part of the legislature to participate in the SSTP? Lawmakers have been promised hundreds of millions of dollars that could be had if the state would just participate in the project. The suggestion came to the 2001-2003 Tax Review Commission on the recommendation of their consultant who was already an advocate of the project.

Of course, no thought was given to how this would affect Hawaii businesses and what additional costs there would be. Given the fact that Hawaii businesses will now have to operate in a different mode insofar as the general excise/SSTP sales tax, will lawmakers compensate businesses for undertaking the collection of other state's retail sales taxes? Indeed, the law being proposed in this measure is a hybrid of the current general excise tax law and a retail sales tax. It retains the two-tiered wholesale/retail system and keeps the tax imposed on services as well as on business-to-business transactions. So the measure attempts to have the best of both worlds - to force other states to collect our general excise tax while retaining the pyramiding features of the general excise tax. This is a major change in the state's largest source of general fund revenues. Care should be taken in making this transition as it could alter not only the past interpretation of the general excise tax, but it may also have a major impact on the revenue producing capacity of the tax.

One of the key issues still under discussion amongst the members who have already signed on is "where" does the sale occur. For a number of the larger states like California, Illinois, and Texas which have much at stake since they are states that manufacture goods shipped to other states, the sourcing rules they adopted use "origin" based rules, that is the tax that is imposed at the place from which the goods are shipped and not where the purchaser takes possession. The proposed bill here is ambiguous at best as in some cases being origin based as long as the purchaser takes possession of the goods at the place of the business but provides, on the other hand, for the taxation at the address to which the goods are delivered. It is this destination rule that causes the most problems for businesses as they must now deal with a plethora of rates depending on the number of states from which they receive orders for their goods. While some states may elect destination, there is no doubt that the larger states will elect origin sourcing as they are probably net exporters of goods. That being the case, Hawaii residents will probably end up paying the Illinois or California sales tax on their purchases from out-of-state vendors and in the long run, the purported windfall will turn into a disaster for Hawaii. Under current law, the use tax would otherwise have been due on those sales and while it has been difficult to enforce and collect on individual sales, more of an effort should be placed on the collection of the use tax where Hawaii already has jurisdiction.

Again, a main area of concern is whether the states can afford the streamlined system itself. Given the promises that have been made and not delivered upon such as the software that is supposed to facilitate the collection and remittance of the various states' sales taxes, to the promise to pay the cost of funding the administrative structure of the governing board, it appears that all of these are promises with no intent

to make it happen. As such, it is premature for Hawaii to jump on the throttling locomotive engine that appears to be headed for a brick wall. This proposal needs more discussion in the interim and further clarification as well as a discussion with taxpayers who must carry out the duty of the actual collection.

Curiously, this is what the 2005-2007 Tax Review Commission recommended, that until the member states of the SSTP Agreement come to a definitive conclusion, it is premature for Hawaii to jump on board. With this latest development, it appears that Hawaii will be a net loser as its residents will end up paying other state's sales taxes.

While the proposed measure attempts to conform Hawaii's general excise and use tax laws to the streamlined sales and use tax agreement, due to its complexity and technical aspects, it is questionable whether members of the legislature are qualified to determine whether this measure will be sufficient to comply with the Streamlined Sales and Use Tax Agreement.

In 2006 a bill that would adopt the streamline sales tax agreement was introduced and nearly passed the legislature but for a small glitch in the closing moments of the session. This, despite the fact that the State Auditor had a consultant assess the revenue potential of participating in the project. Instead of the hundreds of millions of dollars the promoters of the project had promised, the consultant estimated that Hawaii would benefit at the very least by about \$10 million and at the most \$50 million.

At the same time, when the department of taxation was asked what it estimated it would cost the department to implement the project for Hawaii, the price tag was set at \$15 million. Thus, it came as no surprise that when the Tax Review Commission looked at the issue, the decision was a no brainer, Hawaii would stand to gain about \$10 million in revenue, but it would cost the state \$15 million to implement. And that doesn't include the cost to businesses in Hawaii that would be required to collect the sales taxes of other states.

So the Commission's advice to the legislature and administration was to wait. In its recommendation it was noted that "the largest states (by economic size) have failed to sign on to the project, jeopardizing the chances of becoming an effective vehicle for collecting the Use Tax. Until the Project shows greater promise of producing results, it is premature for Hawaii to incur the expense to join it."

In 1992, in *Quill Corp. v. North Dakota*, the U.S. Supreme Court reaffirmed that the power of states to impose taxes on interstate commerce is limited by their geographic border. Although some academics resent this "physical presence rule," it remains the law of the land and is essential to prevent revenue officials from wreaking havoc on national markets by reaching beyond their borders for tax revenues. Since no working alternative to the physical presence rule has been developed, abandoning it would result in states harming themselves by harming the whole.

The SSTP was formed in reaction to *Quill*, though not necessarily to create an alternative to the physical presence rule. The SSTP is a working group of revenue officials and experts with the stated purpose of bringing simplicity and uniformity to sales taxes in the United States. (The governance structure raises some questions of democratic accountability and whether SSTP receives or seeks genuine public input.) Member states must adopt reforms to align their tax code with the SSTP. The hope is that simple and uniform sales tax statutes will allow the collection of interstate sales taxes without placing burdens on interstate commerce.



Simplicity and uniformity are both important goals, but the SSTP has, at best, mixed success in achieving them. There are nearly 8,000 sales taxing jurisdictions in the United States, each with their own bases and rates, and the enormous complexity involved in tracking borders and changes is a huge stumbling block to state efforts to impose tax on online sales.

While the SSTP has made some progress on uniformity (they have succeeded, for instance, in a single accepted definition of “candy”-something everyone defined differently before), the SSTP appears to be giving up the effort on simplicity. At their New Orleans meeting in July 2008, for instance, the SSTP panel was asked if any effort was being made to reduce the number of sales taxing jurisdictions, and/or to align them with 5-digit zip codes. “No and no,” was the short, but honest answer.

Rather than requiring that states simplify before reaching out beyond their borders to tax out-of-state companies, the SSTP seems content to let states continue the status quo. One panelist noted that far from requiring substantial reforms, “States still get to do 99.9% of what they want to do” under the SSTP agreement. This demonstrates either disingenuousness or how little the SSTP recognizes that many existing sales taxes are in need of substantial reform.

The SSTP already abandoned the notion of taxing like transactions alike when they adopted “destination sourcing” for online sales, but permitted states to adopt “origin sourcing” for intrastate sales. This in effect requires Internet companies to collect sales taxes based on where their customer is located, but allows brick-and-mortar stores to collect sales taxes based on where the store is located. In this way, the SSTP prevents a level playing field between Internet businesses and brick-and-mortar businesses.

Coupled with the SSTP’s non-worry about reducing the number of jurisdictions (they spoke optimistically of providing maps of sales tax jurisdictions, having rejected even aligning jurisdictions with 9-digit zip codes), full implementation of the SSTP, at this time, without serious reforms, could result in a serious and inequitable burden on e-commerce.

Another recent example involves clothing taxes. The SSTP requires that all states have a uniform definition of clothing, and tax all of it (or none of it) at the same rate. Minnesota did so, but then imposed a “separate” fur tax on fur sales. Rather than recognizing this as an end-run around tax uniformity, the SSTP upheld Minnesota’s action.

The SSTP is attempting to persuade Congress to permit SSTP member states to begin collecting sales taxes on online purchases, premised on the belief that the SSTP’s simplification and uniformity mission has been accomplished. **The SSTP has not accomplished its mission.** The SSTP should look again at serious simplification efforts before declaring themselves a success and seeking to expand state taxing power.

States should be willing to adopt uniform definitions worked out by the SSTP, so as to reduce transaction costs between state statutes. However, the ability of any state to collect sales tax on online transactions is wholly dependent on the willingness of other states to simplify their laws and adopt uniform definitions as well. It is also dependent on the creation of a working alternative to the physical presence standard that provides certainty and prevents multiple taxation. Neither the wholesale adoption nationwide of uniform sales tax statutes, nor the development of a working alternative that provides the certainty needed for long-term investment, are likely in the foreseeable future.



For these reasons, lawmakers and other states should understand that SSTP membership does not lead to a sudden influx of free tax money. In any event, this money will come from Hawaii residents and should be looked at as a tax increase notwithstanding the existing liability under the use tax laws. The SSTP's goals are good ones, but their success is mixed at best, and whatever effect it has will not be seen in the short-term.

This measure also proposes to earmark a portion of the revenues that are basically general excise tax revenues into the state treasury and credit those revenues to the University of Hawaii, from the effective date of this act to December 31, 2014 and would result in a substantial loss of general fund revenues to fund necessary state programs, including capital improvement requests statewide. From January 1, 2015, the earmarking would terminate and the revenues will be deposited to the state treasury.

The long and short of this measure is that it is nothing more than a tax increase that will probably end up benefitting other states if the majority of states adopt "origin" based sourcing and continuing a tradition of passing the cost to administer and complying with the proposal on to businesses in Hawaii, adding yet another nail in the coffin for businesses in Hawaii. It is certainly a reflection of the lack of understanding of Hawaii's unique general excise tax and how generous it is in producing revenues for the state and is an effort driven by greed.

Digested 3/24/09



House FIN Cmte  
Wed, Mar 25, 2009  
4:00 pm  
room 308

National Association of Social Workers

Hawaii Chapter

March 24, 2009

TO: Rep. Marcus Oshiro, Chair  
Members of the House Finance Committee

FROM: Debbie Shimizu, LSW  
National Association of Social Workers, Hawaii Chapter

RE: SB 1678 SD3 Relating to Taxation- **SUPPORT**

Chair Oshiro and members of the House Finance Committee, I am Debbie Shimizu, Executive Director of the National Association of Social Workers (NASW), Hawaii Chapter. NASW is the largest professional organization for social workers in Hawaii. **NASW SUPPORTS SB 1678 SD3 to amend Hawaii's tax laws to implement the streamlined sales and use tax agreement.**

22 states, representing over 30 percent of the country's population, have already been certified as being in compliance with the Streamlined Sales and Use Tax Agreement. This year, ten additional states are considering legislation to join the agreement. Hawaii should join these states so we can capture our share of sales and use taxes from remote transactions including online purchases. It is estimated that our e-commerce revenue losses are projected to be more than 6% of our total GET/use tax revenues. In FY07, this amount would have been \$153.34 million dollars.

This is not a "new" tax but a tax that is due to our state for purchases made by our residents. During this time of economic crisis, this is a good source of revenue for our state. We urge your support of SB 1678 SD3.

Thank you for this opportunity to testify.



Representative Marcus Oshiro, Chair  
Representative Marilyn Lee, Vice Chair  
Committee on Finance

HEARING      Wednesday, March 25, 2009  
                    4:00 pm  
                    Conference Room 308  
                    State Capitol, Honolulu, Hawaii 96813

**RE:    SB1678, SD3, Relating to Taxation**

Chair Oshiro, Vice Chair Lee, and Members of the Committee:

Retail Merchants of Hawaii (RMH) is a not-for-profit trade organization representing about 200 members and over 2,000 storefronts, and is committed to support the retail industry and business in general in Hawaii.

**RMH supports SB1678, SD3**, which adopts amendments to Hawaii's tax laws to implement Streamlined Sales and Use Tax Agreement.

Through our affiliation with the National Retail Federation, the world's largest retail trade association, and a major participant in the Streamlined Sales Tax Project, RMH has watched the development and progress of this program over the past eight years and has supported Hawaii's initiatives to participate in the multi-state discussions. As electronic commerce increased dramatically in recent years, traditional brick and mortar retailers, which are required by law to collect taxes for government, have experienced an erosion of their sales base to remote sellers, which, under most circumstances, are not subject to tax mandates. The Streamlined Sales and Use Tax Project will level the playing field.

Retailers nationally are encouraged that current initiatives in Congress hold greater promise to ameliorate this unfair situation, and there is consensus that federal legislation will be enacted soon. SB1678, SD3, makes the necessary amendments to Hawaii tax laws to facilitate our compliance.

We respectfully request that your support of SB1678, SD3. Thank you for your consideration and for the opportunity to comment on this measure.

Carol Pregill, President

RETAIL MERCHANTS OF HAWAII  
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March 25, 2009

Testimony to: House Committee on Finance  
Rep. Marcus R. Oshiro, Chair  
Rep. Marilyn B. Lee, Vice Chair

By: Richard C. Botti, President

Re: SB 1678 SD3 RELATING TO TAXATION

**Chairs & Committee Members:**

We support SB 1678, SD3

The Legislature has had the so called Streamlined sales and use tax issue on the table of many years. We feel it is the least line of resistance to accomplishing its intended purpose, which is to level the playing field.

There are two alternate approaches that would provide the same desired result. One would be to create new definitions of "nexus" with the other being to force everyone purchasing imports for consumption to pay the 4% tax annually on their tax return. We believe both would cost more to enforce than would be gained, and one would be challenged as illegal.

We simply can't see a downside with this measure, thus support it as being the line of least resistance.



**SB1678 SD3 Relating to Taxation**

**DATE:** March 25, 2009  
4:00pm  
Conference Room 308

**TO:** House Committee on Finance  
Representative Marcus R. Oshiro, Chair  
Representative Marilyn B. Lee, Vice Chair

**FROM:** Lisa H. Gibson  
President  
Hawaii Science & Technology Council

**RE:** Testimony In Support of the Intent of SB1678 SD3

Aloha Chair, Vice Chair, and Members of the Committee:

The Hawaii Science & Technology Council supports SB1678 SD3, the Streamlined Sales Tax Bill, which would adopt changes to Hawaii's tax law that will allow Hawaii to participate in the Streamlined Sales and Use Tax Agreement. HiSciTech supports legislation such as this because:

1. It assists in the collection of taxes already due to State of Hawaii;
2. It will enhance state tax revenue in a time of economic turmoil;
3. It will level the playing field for local businesses with out of state vendors.

The Hawaii Science & Technology Council is a private tax-exempt 501(c)6 industry association with a 28-member board. The council serves Hawaii companies engaged in ocean sciences, agricultural biotechnology, astronomy, defense aerospace, biotech/life sciences, information & communication technology, energy, environmental technologies, and creative media.

Thank you for the opportunity to testify on this important bill.

Lisa H. Gibson  
President



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March 24, 2009

**The Honorable Marcus R. Oshiro, Chair**  
House Committee on Finance  
State Capitol, Room 308  
Honolulu, Hawaii 96813

**RE: S.B. 1678, S.D.3, Relating to Taxation**

**HEARING DATE:** Wednesday, March 25, 2009 at 4:00 p.m.

Aloha Chair Oshiro and Members of the Committee on Finance:

I am Craig Hirai, a member of the Subcommittee on Taxation and Finance of the Government Affairs Committee of the Hawai'i Association of REALTORS® ("HAR"), here to testify on behalf of the HAR and its 9,600 members in Hawai'i. HAR **supports** S.B. 1678, S.D.3, which adopts amendments to Hawaii tax laws to implement the streamlined sales and use tax agreement.

The Report of the 2001-2003 Tax Review Commission states that Hawaii would potentially achieve not only the benefit of better definitions, uniformity, and certainty, but also increase tax compliance by interstate vendors (primarily mail order and e-commerce merchants) who agree to pay state taxes under the Streamlined Sales Tax Project. The Report goes on to state that because of Hawaii's uniquely broad based General Excise and Use Tax system, by joining the Streamlined Sales Tax Project, Hawaii may be able to better maintain the viability of its broad revenue base.

The Report of the 2005-2007 Tax Review Commission, however, states that while the Commission believes that the goal of coordinating the collection of taxes on interstate sales, such as via the internet, is desirable, and that Hawaii should remain involved in discussions on the Streamlined Sales Tax Project, ultimately, the Commission did not think that Hawaii should make a formal commitment yet.

HAR believes that the delayed effective date contained in Section 36 of S.B. 1678, S.D.3, should help alleviate the concerns of the 2005-2007 Tax Review Commission, and that S.B. 1678, S.D.3, should eventually level the playing field for local merchants who must deal with the high cost of doing business in Hawaii and still compete with mail order and e-commerce merchants from outside of the State.

HAR looks forward to working with our state lawmakers in building better communities by supporting quality growth, seeking sustainable economies and housing opportunities, embracing the cultural and environmental qualities we cherish, and protecting the rights of property owners.

Mahalo for the opportunity to testify.



March 24, 2009

Representative Marcus Oshiro, Chair  
House Finance Committee  
Hawaii State Capitol  
Honolulu, HI 96813

Re: SB1678, Relating to Streamlined Sales and Use Tax Amendment

Dear Representative Oshiro:

I am Gail Breakey, Director of the Hawaii Family Support Institute testifying in support of SB 1678.

The primary benefits of this bill are to simplify doing business in Hawaii, to conform with Federal legislation, to level the playing field for local business and to enable Hawaii to collect substantial cumulative revenues from remote transactions.

Sincerely,

Gail Breakey, Director,  
Hawaii Family Support Institute

## FINTestimony

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**From:** mailinglist@capitol.hawaii.gov  
**Sent:** Tuesday, March 24, 2009 5:09 PM  
**To:** FINTestimony  
**Cc:** thirr33@gmail.com  
**Subject:** Testimony for SB1678 on 3/25/2009 4:00:00 PM

Testimony for FIN 3/25/2009 4:00:00 PM SB1678

Conference room: 308  
Testifier position: support  
Testifier will be present: Yes  
Submitted by: Arvid Tadao Youngquist  
Organization: Spokesman & Founder: The Mestizo Association (est. 1982)  
Address:  
Phone:  
E-mail: thirr33@gmail.com  
Submitted on: 3/24/2009

Comments:  
House Finance Committee  
Chair Marcus oshiro  
Vice chair Marilyn Lee  
The Right Honorable Members of the Majority & Minority on the Finance Committee

Ladies and Gentlemen,

Good afternoon! My name is Arvid Tadao Youngquist.

I submit this brief testimony in support of SB 1678 submitted by the Hawaii Senate Majority and the Bi-Partisan Keiki Caucus of the Legislature.

Though it has gone through three drafts and some defections as well as "excused absences", the bill has a method to its purpose.

The measure has merit and should be supported by the House Finance & the House Chamber.

Thank you for accepting this testimony in support of SB 1678.

Arvid T. Youngquist  
Spokesman  
The Mestizo Association