

**HB 1180**

**HD 1**

NEIL ABERCROMBIE  
GOVERNOR



KAREN SEDDON  
EXECUTIVE DIRECTOR

**STATE OF HAWAII**

DEPARTMENT OF BUSINESS, ECONOMIC DEVELOPMENT AND TOURISM  
HAWAII HOUSING FINANCE AND DEVELOPMENT CORPORATION  
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IN REPLY REFER TO:

Statement of  
**Karen Seddon**  
Hawaii Housing Finance and Development Corporation  
Before the

**SENATE COMMITTEE ON WAYS AND MEANS**

March 17, 2011 at 9:00 a.m.  
Room 211, State Capitol

In consideration of  
**H.B. 1180, H.D. 1**  
**RELATING TO TAXATION.**

The HHFDC **offers the following comments on and requested amendment to** H.B. 1180, H.D. 1. We defer to the Department of Taxation on the overall merits of the bill.

HHFDC is concerned that the controlling interest transfer tax proposed in this bill may affect projects developed using Federal and State Low-Income Housing Tax Credits (LIHTCs). If it does, it could adversely affect investor interest in Federal and State LIHTCs for affordable rental projects located in the State of Hawaii.

The LIHTC program is a major financing tool to construct or rehabilitation affordable rental housing. The LIHTC provides a credit against income tax liability for 10 years. These credits are typically syndicated to investors to generate project equity. Projects awarded LIHTCs must remain affordable for a minimum of 30 years.

It appears that H.B. 1180, H.D. 1 could apply to a transfer from a limited partner to the general partner of a Limited Partnership (LP) that owns an affordable rental housing project for which LIHTCs have been issued under Section 42 of the Internal Revenue Code or sections 235-110.8 or 241-4.7, Hawaii Revised Statutes. Typically, the non-profit housing developer/owner is the general partner of the LP. Tax credit investors are limited partners of the LP. Limited partners eventually transfer back their partnership interests to the general partner, who will continue to operate the project as an affordable rental project.

Accordingly, to clarify that these particular transfers are not intended to trigger the controlling interest transfer tax, we respectfully request that the Committee amend Section 2 of the H.D. 1 by amending proposed section 247-A(a) as follows:

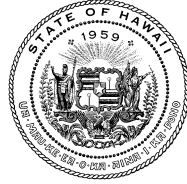
"§247-A Transfer of a controlling interest; applicability.

(a) Notwithstanding any provision to the contrary, the tax imposed by section 247-1 shall apply to the transfer or acquisition, or a series of transfers or acquisitions, including those combined with otherwise exempt transfers, by any person or entity, either acting alone or in concert, within any twelve-month period, that result in the transfer of a controlling interest in an entity with an interest in real property located in this State for valuable consideration and which also results in the transfer of control or ownership of the real property located in this State; provided that (1) this section shall not apply to any transfer or acquisition that consists of the mere change in identity or form of ownership of an entity where there is no change in the beneficial ownership, including transfers to an entity wholly owned, directly or indirectly, by the same common ownership as the transferor; or (2) any transfer from a limited partner to the general partner of a limited partnership that owns an affordable rental housing project for which low-income housing tax credits have been issued under Section 42 of the Internal Revenue Code or sections 235-110.8 or 241-4.7, Hawaii Revised Statutes."

Thank you for the opportunity to testify.

NEIL ABERCROMBIE  
GOVERNOR

BRIAN SCHATZ  
LT. GOVERNOR



STATE OF HAWAII  
**DEPARTMENT OF TAXATION**  
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FREDERICK D. PABLO  
DIRECTOR OF TAXATION

RANDOLF L. M. BALDEMOR  
DEPUTY DIRECTOR

## SENATE COMMITTEE ON WAYS AND MEANS

### TESTIMONY OF THE DEPARTMENT OF TAXATION REGARDING HB 1180, HD 1 RELATING TO TAXATION

**TESTIFIER:** **FREDERICK D. PABLO**, DIRECTOR OF TAXATION (OR  
DESIGNEE)  
**COMMITTEE:** WAM  
**DATE:** MARCH 17, 2011  
**TIME:** 9:00AM  
**POSITION:** **CONCERNS**

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This bill amends the conveyance tax to capture the tax on the sale of stock in entities that own Hawaii real property.

**NEW TAX TYPE** -- The Department of Taxation (Department) is concerned that the complexity of these new provisions would be difficult to administer. Although technically part of the conveyance tax, this tax represents a new type of tax for the Department to collect. While the Department administers the conveyance tax, the Department does not collect the conveyance tax. Therefore, the Department's computer system would need to be updated to reflect this new law.

**PROPORTION OF REAL PROPERTY AND INTENT OF SALE** -- In addition, the Department is concerned that the new tax would apply to the sale of a controlling interest in an entity, even if the entity's assets were comprised mostly of property other than real estate. For example, an operating business such as a construction company may own the real property upon which the company's headquarters is located, which could represent only a small fraction of the value of the entire business. If a controlling interest in the construction company is sold, the controlling interest transfer tax would be triggered even though the primary purpose of the sale was to sell the construction business, not the real property.

**REVENUE IMPACT**—For the special funds, the revenue impact for this bill is approximately \$1.2 million of revenue per year in fiscal year 2012, and \$1.4 million in fiscal year 2013 and thereafter. For the general fund, the revenue impact is approximately \$0.8 million in fiscal year 2012 and \$0.6 million in fiscal year 2013 and thereafter.

# TAXBILLSERVICE

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TAX FOUNDATION OF HAWAII

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SUBJECT: CONVEYANCE, Transfer of a controlling interest

BILL NUMBER: HB 1180, HD-1

INTRODUCED BY: House Committee on Finance

**BRIEF SUMMARY:** Add a new section to HRS chapter 247 to provide that the conveyance tax shall be applicable to the transfer or acquisition, or a series of transfers or acquisitions, including those combined with otherwise exempt transfers, by any person or entity, either acting alone or in concert, within any 12-month period, that result in the transfer of a controlling interest in an entity with an interest in real property located in this state for valuable consideration and which also results in the transfer of control or ownership of the real property located in this state.

This section shall not apply to any transfer or acquisition that consists of the mere change in identity or form of ownership of an entity where there is no change in the beneficial ownership, including transfers to an entity wholly owned, directly or indirectly, by the same common ownership as the transferor.

In determining whether a controlling interest was transferred or acquired within a 12-month period, the date that the option agreement was executed shall be the date on which the transfer or acquisition of the controlling interest is deemed to occur. For all other purposes, the date upon which the option is exercised is the date of the transfer or acquisition of the controlling interest.

Stipulates that for the purposes of this section with regard to persons acting in concert: (1) all acquisitions of persons acting in concert shall be aggregated for the purpose of determining whether a transfer or acquisition of a controlling interest has taken place; (2) persons shall be considered as acting in concert when they have a relationship with each other such that one person influences or controls the actions of another through common ownership; (3) persons shall be considered to be acting in concert only when the unity with which the purchasers negotiate and consummate the transfer of ownership interests supports a finding that the persons are acting as a single entity; and (4) if acquisitions are completely independent and each purchaser purchases without regard to the identity of the other purchasers, then the acquisitions shall be considered separate acquisitions.

“Controlling interest” shall mean: (1) in the case of a corporation, either 50% or more of the total combined voting power of all classes of stock of the corporation entitled to vote, or 50% or more of the capital, profits, or beneficial interest in the voting stock of the corporation; and (2) in the case of a partnership, association, trust, or other entity, 50% or more of the capital, profits, or beneficial interest in the partnership, trust, or other entity.

Directs the director of taxation to adopt rules pursuant to HRS chapter 91 to implement this section, including rules for determining whether persons are acting in concert for the purpose of transferring or acquiring a controlling interest.

Adds a new section to HRS chapter 247 to provide that the conveyance tax imposed by HRS section 247-1 shall apply to the following at the lowest rate regardless of the value of the real property: (1) any document or instrument conveying real property, or any interest therein, from an entity that is a party to a merger or consolidation under HRS chapters 414, 414D, 415A, 421, 421C, 425, 425E, or 428 to the surviving or new entity; (2) any document or instrument conveying real property, or any interest therein, from a dissolving limited partnership to its corporate general partner that owns, directly or indirectly, at least a ninety percent interest in the partnership, determined by applying section 318 (with respect to constructive ownership of stock) of the federal Internal Revenue Code of 1986, as amended, to the constructive ownership of interests in the partnership; (3) any document or instrument conveying real property to any nonprofit or for-profit organization that has been certified by the Hawaii housing finance and development corporation for low-income housing development; and (4) any document or instrument conveying real property, or any interest therein, to or from a wholly-owned corporation or limited liability company.

Makes conforming amendments to HRS section 247-1 and HRS section 247-3.

EFFECTIVE DATE: July 1, 2011

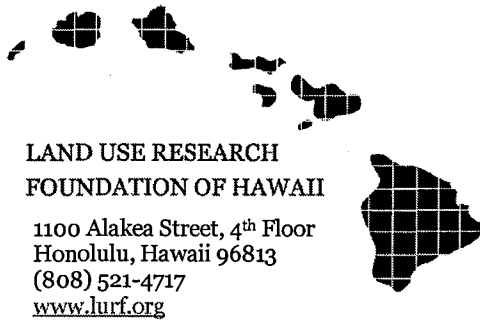
**STAFF COMMENTS:** The proposed measure would subject to the conveyance tax rates “complex transactions” involving the transfer of real property to ensure that the transactions are taxed, even though they are not currently taxable under the conveyance tax as the real property is owned by a legal entity like a corporation or partnership. While it is the intent of the measure to close this loophole as the measure argues that these transfers attempt to evade taxation, it should be noted that the current conveyance tax was never established to be a source of revenue. Only in recent years as lawmakers sought to fund their favorite programs did the conveyance tax come under fire as a way to raise new sources of revenue to fund favored programs. With rates as high as \$1.25 per hundred dollars of value transferred, lawmakers now believe that transfers of real property, albeit as part of the acquisition of a company or partnership, are an intentional evasion of the tax. Thus, it is not hard to believe that while the measure proposes that the conveyance tax at the lowest rate shall be imposed on these transfers, there is not doubt that this policy may be amended and the rate will mushroom in a few years as the legislature may target these transfers as another way to raise additional revenue.

Unfortunately, the imposition of the conveyance tax on these transfers may add another nail in the economic coffin of Hawaii as it is just one more cost that an investor must weigh in deciding whether or not the return on an investment in Hawaii is attractive or reasonable.

It should be remembered that the conveyance tax was initially enacted by the 1966 legislature after the repeal of the federal law requiring stamps for transfers of real property. It was enacted for the sole purpose of providing the department of taxation with additional data for the determination of market value of properties transferred. This information was also to assist the department in establishing real property assessed values and at that time the department stated that the conveyance tax was not intended to be a revenue raising device. The conveyance tax is imposed each time property changes title or ownership. However, over the years the tax has been increased and conveyance tax revenues have been tapped to provide revenue for the land conservation fund, rental housing trust fund, and the natural area reserve fund.

While this proposal tries to address what looks like a sale of an entity or organization that has as part of its portfolio real property in Hawaii, there are other ways of transferring a company and the controlling interest of such an entity without the appearance that the organization or entity is being sold or transferred. The measure attempts to carve or exempt transactions between entities wholly owned by the same common ownership that results in no change in the beneficial ownership. Whether or not this would cover instances where partnerships are dissolved should be questioned. If a partnership dissolves and each of the parties takes some or all of the portfolio of real estate, will that meet the "related entity" transfer that this clause of the bill attempts to address?

Digested 3/15/11



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March 17, 2011

Senator David Y. Ige, Chair, and Senator Michelle N. Kidani, Vice Chair  
Senate Committee on Ways and Means

**Comments Relating to HB 1180, HD1, Relating to Taxation; Conveyance Tax; Controlling Interest Transfer**

**Thursday, March 17, 2011 at 9:00 a.m. in CR 211**

My name is **Dave Arakawa**, and I am the Executive Director of the Land Use Research Foundation of Hawaii (LURF), a private, non-profit research and trade association whose members include major Hawaii landowners, developers and a utility company. One of LURF's missions is to advocate for reasonable, rational and equitable land use planning, legislation and regulations that encourage well-planned economic growth and development, while safeguarding Hawaii's significant natural and cultural resources and public health and safety.

**HB 1180, HD1.** This bill proposes to impose the conveyance tax on the transfer of a controlling interest of an entity with an interest in real property, however, stipulates that the imposition of the conveyance tax on transfers of entity ownership shall not apply to any transfer of interest or acquisition between entities wholly owned by the same common ownership that results in no change in beneficial ownership.

**LURF's Position.** LURF understands the intent of this bill (to apply the conveyance tax to transfers of entity ownership when such transfer is essentially equivalent to the sale of an interest in land), however, despite the non-imposition of the proposed tax upon transfers effectuated by a member of an affiliated group to another member of the same group, must request this Committee to note and consider the following:

- The proposed imposition of the conveyance tax on transfers of controlling interests in entities will drive up the cost of lands for agricultural production, affordable and market homes, and commercial development.
  - Proposed imposition of the conveyance tax onto transfers which affect agricultural lands will be passed on to farmers and other agricultural operators, making it even harder for agriculture to survive in Hawaii;
  - Proposed imposition of the conveyance tax onto transfers which affect land intended for housing developments will be passed on to home buyers, will increase the price of homes, and will exacerbate the affordable housing problem in Hawaii; and



# Hawaii Housing Finance, LLC

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Testimony of  
**Stacy L. Sur**  
Hawaii Housing Finance, LLC  
Before the

**SENATE COMMITTEE ON WAYS AND MEANS**

March 17, 2001 at 9:00 a.m.  
Room 211, State Capitol

In consideration of  
**H.B. 1180, H.D. 1**  
**Relating to Taxation**

We **concur** with the **comments** and the recommended amendment provided by the Hawaii Housing Finance and Development Corporation regarding H.B. 1180, H.D. 1.

The impact of this bill may have negative consequences for the financing and development of affordable rental housing in the state. Over the past two decades, the only reliable source of new rental housing in the state has been the low-income housing tax credit program.



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March 17, 2011

**The Honorable David Y. Ige, Chair**  
Senate Committee on Ways and Means  
State Capitol, Room 211  
Honolulu, Hawaii 96813

**RE: H.B. 1180, H.D.1, Relating to Taxation**

**HEARING: Thursday, March 17, 2011 at 9:00 a.m.**

Aloha Chair Ige, Vice Chair Kidani and members of the Committee:

I am **Craig Hirai**, Chair of the Subcommittee on Affordable Housing, here to testify on behalf of the Hawai'i Association of REALTORS® ("HAR"), the voice of real estate in Hawai'i, and its 8,500 members. HAR would like to make the following **comments** with respect to H.B. 1180, H.D.1, Relating to Taxation, which: (a) imposes Conveyance Tax on the transfer of a controlling interest of an entity with an interest in Hawaii real property; (b) stipulates that the imposition of the Conveyance Tax on transfers of entity ownership shall not apply to any transfer of interest or acquisition between entities wholly owned by the same common ownership that results in no change in the beneficial ownership; and (c) imposes the Conveyance Tax on certain other transfers of real property to or from related persons at the lowest tax rate.

The purpose of this H.B. 1180, H.D.1, is to apply the Conveyance Tax to transfers of entity ownership when the transfer of entity ownership is essentially equivalent to the sale of an interest in Hawaii real property.

HAR believes that the transfer of control of a business entity is comparable to the sale of an interest in the real property held by the entity. HAR further believes that all transfers of possession or use of real property in Hawaii should be subject to the same Conveyance Tax obligations and that the burden of the Hawaii Conveyance Tax currently falls primarily on smaller Hawaii business and property owners and Hawaii homeowners who generally convey title to real property itself and not controlling interests in entities that own Hawaii real property.

HAR would note favorably that: (i) the transfer of a controlling interest under H.B. 1180, H.D.1, is subject to Conveyance Tax receipts of which, among other things, supports the Rental Housing Trust Fund; and (ii) the conveyance of real property interests among related entities under H.B. 1180, H.D.1, will be exempt from Conveyance Tax or only be subject to Conveyance Tax at the lowest rate.

Mahalo for the opportunity to testify.