

NEIL ABERCROMBIE  
GOVERNOR



STATE OF HAWAII  
DEPARTMENT OF TRANSPORTATION  
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IN REPLY REFER TO:

February 14, 2011

TESTIMONY OF THE DEPARTMENT OF TRANSPORTATION

HOUSE BILL NO. 1266

COMMITTEE ON TRANSPORTATION

House Bill No. 1266 proposes to amend Chapter 266-13, HRS, to provide the department with the authority to waive fifty percent of dockage charges incurred by an inter-island ferry in the first twelve months of operations. We have no objections so long as the waiver is at the sole discretion of the department. As the issuer of harbors system revenue bonds, our bond certificate requires that we maintain rates and fees sufficient to cover operating expenses and meet rate covenant tests in our bond certificate.

**NEIL ABERCROMBIE**  
GOVERNOR

**BRIAN SCHATZ**  
LT. GOVERNOR



STATE OF HAWAII  
**DEPARTMENT OF TAXATION**  
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DEPUTY DIRECTOR

## **HOUSE COMMITTEE ON TRANSPORTATION**

### **TESTIMONY OF THE DEPARTMENT OF TAXATION REGARDING HB 1266 RELATING TO FERRIES**

**\*\*\*WRITTEN TESTIMONY ONLY\*\*\***

**TESTIFIER:** FREDERICK D. PABLO, INTERIM DIRECTOR OF  
TAXATION (OR DESIGNEE)

**COMMITTEE:** TRN

**DATE:** FEBRUARY 14, 2011

**TIME:** 9AM

**POSITION:** DEFER TO DOT

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This legislation, among other things, creates a non-refundable income tax credit for companies operating inter-island ferries.

The Department of Taxation (Department) defers to the Department of Transportation on the merits of this legislation.

The revenue impact is indeterminate.

If you have any questions please call (808) 587-1530.



**TESTIMONY OF  
THE DEPARTMENT OF THE ATTORNEY GENERAL  
TWENTY-SIXTH LEGISLATURE, 2011**

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**ON THE FOLLOWING MEASURE:**

H.B. NO. 1266, RELATING TO FERRIES.

**BEFORE THE:**

HOUSE COMMITTEE ON TRANSPORTATION

**DATE:** Monday, February 14, 2011 **TIME:** 9:00 a.m.

**LOCATION:** State Capitol, Room 309 .

**TESTIFIER(S):** David M. Louie, Attorney General, or  
Cynthia M. Johiro, Deputy Attorney General

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Chair Souki and Members of the Committee:

The Department of the Attorney General has the following comments on this bill, which proposes to provide an income tax credit for inter-island ferry operations.

This bill may be subject to constitutional challenge because the bill is facially discriminatory in that it restricts the tax credit it creates to Hawaii residents.

A court may conclude that the tax credit is unconstitutional because the bill does not expressly articulate a legitimate government interest served by the legislation, sufficient to withstand constitutional challenge based on the Equal Protection and/or Privileges and Immunities Clauses of the United States Constitution.

The Equal Protection Clause prohibits discrimination against a nonresident based solely on residency. See, e.g., Williams v. Vermont, 472 U.S. 14 (1985) (use tax credit for sales taxes paid on cars purchased in other states invalidated because it was only available to Vermont residents). The Hawaii Supreme Court has recognized that the Equal Protection Clause applies where a tax operates unequally on persons or property of

the same class. In re Swann, 7 Haw. App. 390, 776 P.2d 395 (1989).

Similarly, under the Privileges and Immunities Clause, a state may not impose higher taxes on a nonresident individual than it imposes on its own citizens.<sup>1</sup> However, a discriminatory tax could be sustained if legitimate reasons for the tax exist and the discrimination bears a substantial relation to those reasons. Lunding v. New York Tax Appeals Tribunal, 522 U.S. 287 (1998) (alimony deduction for residents only struck down as violating Privileges and Immunities Clause).

The language in the bill that creates this potential constitutional problem is the word "resident" in the definition of "principal operator" on page 2, line 20, of the bill.

The residency requirement in the bill arguably violates the Equal Protection and Privileges and Immunities Clauses because it expressly favors residents over nonresidents.<sup>2</sup>

To insulate the bill from possible constitutional challenge, we recommend either of two possible remedies:  
(1) that the bill be amended to delete the word "resident"; or  
(2) that a legitimate government purpose substantially related to that purpose be articulated within the preamble of the bill.

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<sup>1</sup> The Privileges and Immunities Clause does not apply to corporations. Toomer v. Witsell, 334 U.S. 385 (1948).

<sup>2</sup> We are aware that a few existing tax statutes have residency requirements. To date, these statutes have not been subject to constitutional challenge.

# TAXBILLSERVICE

126 Queen Street, Suite 304

TAX FOUNDATION OF HAWAII

Honolulu, Hawaii 96813 Tel. 536-4587

**SUBJECT:** INCOME, Ferry vessel tax credit

**BILL NUMBER:** HB 1266

**INTRODUCED BY:** Chong, Awana, Hashem, Herkes, Ito, Mizuno, Nakashima, Nishimoto, B. Oshiro, Tsuji, Yamashita and 3 Democrats

**BRIEF SUMMARY:** Adds a new section to HRS chapter 235 to allow a principal operator of an inter-island ferry to claim an income tax credit of 5% of the taxpayer's individual or corporate income tax liability.

Tax credits in excess of a taxpayer's tax liability shall be applied to any subsequent tax liability. Requires all claims, including amended claims, to be filed on or before the end of the twelfth month following the close of the taxable year for which the credit may be claimed. Failure to comply with the foregoing provision shall constitute a waiver of the right to claim the credit. Directs the director of taxation to prepare the necessary forms to claim a credit under this section

Defines "inter-island ferry" and "principal operator" for purposes of the measure.

Amends HRS section 266-13 to allow the department of transportation to waive 50% of the harbor fees for the first year of the operation of an inter-island ferry.

**EFFECTIVE DATE:** Tax years beginning after December 31, 2010

**STAFF COMMENTS:** While the proposed measure would merely grant a tax credit to the principal operator of an inter-island ferry, it should be noted that the tax credit proposed in this measure does not have any bearing on the taxpayer's ability to pay state income taxes that might be due. Thus, this measure would merely use the tax system to hand out a rebate to such individuals at the cost of all taxpayers.

It is interesting to note that the drafter of the bill assumes there will be a tax credit in excess of liability which can then be carried forward. However, the tax credit is equal to 5% of the ferry operator's tax liability. If that is the case, then the 5% tax credit means that there is 95% of the tax liability still owed after applying the credit so there would never be an excess amount of tax credit. That said, since the tax credit is a percent of taxes owed, that means that the ferry was operated at a profit in any one year. If that is case then why would the ferry operator need a subsidy in the form of the tax credit when the operation made a profit? It is those businesses that aren't making profits that need the state's assistance. Thus, this nothing more than a hand out for certain taxpayers.

The proposed tax credit amounts to nothing more than an appropriation of taxpayer dollars through the back door by way of the tax credit. It represents an uncontrolled cost to state government for a program over which lawmakers will have no opportunity to review and approve the level of these "back door" expenditures. Due to the current fiscal condition of the state, the adoption of this measure cannot be justified.

Digested 2/11/11