

# TAXBILLSERVICE

126 Queen Street, Suite 304

TAX FOUNDATION OF HAWAII

Honolulu, Hawaii 96813 Tel. 536-4587

**SUBJECT:** GENERAL EXCISE, Repeal Act 155, SLH 2010

**BILL NUMBER:** SB 2238, SD-1

**INTRODUCED BY:** Senate Committee on Ways and Means

**BRIEF SUMMARY:** Repeals Act 155, SLH 2010.

**EFFECTIVE DATE:** Upon approval

**STAFF COMMENTS:** The legislature by Act 155, SLH 2010, required all businesses that enjoy a general excise tax benefit to obtain a general excise tax license and file an annual general excise tax reconciliation tax return. While Act 155 extols the virtue of being registered as it provides valuable information that may be used for compliance efforts by the department of taxation, it is questionable whether the Act will ensure the proper payment of taxes. These provisions are aimed, no doubt, at those entities which enjoy exemptions or unique treatment under the general excise tax laws. This would include everyone from nonprofit organizations that enjoy exemptions from the tax on related activities, to for-profit entities that are allowed to treat their gross income as provided for by law. In this latter case, these could include travel related entities where the gross income is divided between commissioned sales and the provider of travel related activities otherwise known as gross-up to hotel operators who are contracted to manage a hotel on behalf of a hotel property owner where the amounts disbursed as compensation and employee benefits are not subject to tax by the hotel operator as they are viewed as pass-through expenditures.

While the intent of this Act is to catch so-called abusers and scofflaws who enjoy these special provisions, it appears that its provisions are overkill, creating an administrative and compliance nightmare, in an attempt to entice businesses who do not have the funds, due to an ailing economy, to pay their fair share of the general excise tax. In this case, this Act violates one of the principles of a good tax policy, that a tax should be easy to administer and with which to comply insuring that the cost of administration and compliance does not exceed the amount of the tax collected.

While Act 155 was an administration-sponsored measure by the state department of taxation, if the department of taxation believes that every taxpayer should be conscientious and honest about paying their general excise taxes, then the department needs to do its part to insure that it is providing guidance and the tools taxpayers need to comply with the law. For example, in recent years the department has gone in the direction of paperless forms, encouraging taxpayers to download the appropriate forms to file their taxes but offering the option for the taxpayer to request hard paper copies of the forms to be filed. Unfortunately, the department has, in many cases, not complied with the request for hard paper copies to be mailed to taxpayers. How can taxpayers be expected to comply with the law if it is difficult to secure the necessary forms? Many taxpayers do not have computers or do not know how to access the department's forms via the Internet and in many cases have forgotten to file their returns on time, if at all. The turnover of personnel at the department has given rise to inexperienced staff who hand out

erroneous information and interpretations of the law leading to confusion and frustration on the part of the taxpayer and the tax practitioner. If the pot is to call the kettle black, that examination needs to begin with the department where customer service has deteriorated in recent years. One cannot expect taxpayers to comply when the department is not doing its utmost to make filing and payment of taxes convenient.

As such, Act 155 should be repealed and the effort to encourage and insure compliance should begin from scratch as obviously it is not being effective in helping taxpayers understand the importance of complying with the law.

Digested 3/9/12



**Testimony to the House Committee on Economic Revitalization and Business  
Tuesday, March 13, 2012 at 8:30 a.m.  
Conference Room 312, State Capitol**

**RE: SENATE BILL NO. 2238 SD1 RELATING TO TAXATION**

Chair McKelvey, Vice Chair Choy, and Members of the Committee:

The Chamber of Commerce of Hawaii ("The Chamber") **supports SB 2238 SD1 relating to Taxation**. We appreciate the committee for scheduling this bill.

The Chamber is the largest business organization in Hawaii, representing more than 1,100 businesses. Approximately 80% of our members are small businesses with less than 20 employees. As the "Voice of Business" in Hawaii, the organization works on behalf of its members, which employ more than 200,000 individuals, to improve the state's economic climate and to foster positive action on issues of common concern.

SB 2238 SD1 repeals Act 155, Session Laws of Hawaii 2010, which requires all businesses with excise tax exemptions to register to do business in Hawaii, file their tax returns in a timely manner, and expressly claim their entitlement, and creates a personal trust liability for businesses that use the general excise tax as the basis for increasing their prices and ensures that those funds are paid to the State for the benefit of consumers and businesses.

Act 155 severely penalizes taxpayers who inadvertently fail to file general excise tax ("GET") returns, even if those taxpayers would not otherwise owe any tax. It therefore created an unnecessary technical requirement, violation of which could result in massive tax liability for innocent taxpayers. The taxpayers most likely to unintentionally violate this technical requirement are **small businesses, individuals, and non-profit organizations**--those who are least likely to have access to sophisticated tax advice, and least able to bear the burden of such severe penalties. This result is contrary to fair tax administration.

The Act created needless administrative complexity both for taxpayers and for the government. It forces even taxpayers who have no GET liability to obtain a GET license and file periodic GET returns. It may also result in inadvertent attempts to tax income that is beyond the State's power and authority to tax. This could lead to unnecessary and expensive tax audits and litigation, which would be a waste of both taxpayer and government resources.

The Act also imposed personal trust fund liability on taxpayers, which is inappropriate for GET. Personal trust fund liability is generally imposed on items such as withholding of employee payroll taxes, which are the liability the employee. Unlike payroll tax withholding, however,

businesses do not hold the GET in trust for any other party. Rather, GET is a tax liability of the business itself. The imposition of personal liability for GET is inappropriate in these circumstances.

Because the Act created unfair and unwarranted burdens for businesses, individuals and non-profit organizations, we support the repeal of the Act through SB 2238 SD1.

Thank you for the opportunity to provide testimony.

ANDREW V. BEAMAN  
ANDREW R. BUNN  
ANDREW W. CHAR  
LEROY E. COLOMBE  
RAY K. KAMIKAWA  
DANTON S. WONG  
ADRIENNE S. YOSHIHARA

BETHANY C.K. ACE  
ANNE E. LOPEZ  
CHASE T. TAJIMA

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WILLIAM H. DODD

GEORGE L. T. KERR  
1933-1998

GREGORY P. CONLAN  
1945-1991

**THE SENATE  
THE TWENTY-SIXTH LEGISLATURE  
Regular Session of 2012**

**COMMITTEE ON ECONOMIC REVITALIZATION & BUSINESS  
Chair McKelvey, Vice Chair Choy, Members of the Committee**

**Hearing date: Tuesday, March 13, 2012  
Testimony on SB 2238 SD 1  
(Relating to Taxation)  
Act 155 Repeal**

Chair McKelvey, Vice Chair Choy, Members of the Committee:

Thank you for scheduling this bill for hearing. We urge passage of this bill which would repeal Act 155 (SLH 2010). Act 155 was introduced by the administration in 2010, passed by the Legislature, and signed into law by Governor Lingle. The Act is too heavy handed in its approach to foster tax compliance, and was passed without much notice to the public.

Act 155 applies to gross income received on or after July 1, 2010. Act 155 upsets decades of settled expectations on how the GET is administered by: (1) providing for the forfeiture of GET exemptions, deductions, income splitting, wholesale rates, and any other such GET benefit just because the annual Form G-49 reconciliation is not filed within 12 months of its due date; and (2) imposing personal liability on responsible persons who willfully fail pay over unpaid GET, whether or not the GET was passed on and collected.

**Forfeiture of GET benefits**

As to the forfeiture of GET benefits, this sanction is out of line with the stated purpose of Act 155, i.e., to obtain information about taxpayers' claims of GET benefits. This forfeiture can occur even if all monthly or other periodic Form G-45 returns are filed, and taxes paid and benefits reported thereon. There are enough penalties on the books to penalize taxpayers for not filing the annual Form G-49, e.g., statute of limitations does not begin to run until the Form G-49 is filed even if all periodic Forms G-45 are filed, and monetary penalties for failure to file the Form G-49 on time.

The forfeiture of GET benefits can even prevent a taxpayer from raising exemptions or deductions in an audit, to counter assessments by the department. A taxpayer already has the burden to prove the department wrong when being assessed additional tax, and should be permitted to raise any defenses available.

Committee On Economic Revitalization & Business  
March 13, 2012  
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Many taxpayers will be caught unawares when their GET benefits are forfeited due to Act 155. For example, a wholesaler can lose the benefit of the .5% wholesale GET rate on its gross income and be subject to the 4% retail rate instead just because it forgets to file the annual Form G-49.

Another example is an exempt school that is required to file the IRS Form 990 but forgets to file the Form G-49. This school is now subject to the GET on all of its tuition income. Since the GET liability will be significant, the school's fiscal situation may be such that the GET cannot be paid. However, Act 155 also provides that unpaid GET will now become the personal liability of officers and directors of the school even if it dissolves.

That the department needed to issue TIR 2010-5 to take back the harshness of Act 155 speaks volumes. However, a TIR is only an administrative pronouncement, not the law, and can be withdrawn at any time.

The department has enough powers at its disposal to enforce the tax laws without Act 155. However, if the Legislature feels that the GET forfeiture provision should remain law, then I respectfully ask that you consider amending the Act as follows:

1. Delay its effective date to provide more time and resources to educate the public about Act 155.
2. In lieu of forfeiture of GET benefits, impose civil penalties of a dollar amount per month capped at a dollar amount. See, e.g, IRC § 6652(c)(per diem penalty up to \$5,000 for failure to file information returns); Act 206 (SLH 2007)(per month penalty of \$1,000 up to \$6,000 for failure to file QHTB annual survey).
3. Give taxpayers the right to assert any GET benefit when audited to offset any assessments under the GET or income tax.
4. Provide an exemption for small businesses.
5. Provide an exemption for exempt organizations that have registered for exemption from the GET.
6. Provide that the statute of limitations on assessments is to run from the periodic Form G-45 periodic return filings, not the annual Form G-49.

#### Personal Liability for Unpaid GET

This will be another trap for the unwary and one that will impose significant personal liabilities due to the GET being imposed on gross income. The GET, being unlike most other states' sales taxes, applies to virtually all economic activity, it pyramids, and is complex. Repeal of this provision of

Committee On Economic Revitalization & Business  
March 13, 2012  
Page 3

Act 155 is recommended. However, if the Legislature sees fit to retain this provision, I respectfully ask that you consider amending the Act to provide as follows:

1. Delay the effective date of Act 155 to provide for more time and resources to educate the public about Act 155.
2. Limit personal liability only to the amount of the GET visibly passed on and collected from the taxpayer's customers.
3. Permit the responsible person to challenge any assessments against the taxpayer entity within 30 days of being notified of the personal assessment.
4. Give immunity for volunteer board members of tax-exempt organizations.
5. Permit the right of contribution among responsible persons, as provided under federal law for employment tax liabilities.
6. Afford prior notice procedures for personal assessments, as provided under federal law.
7. Provide a statute of limitations on personal assessments (remarkably, none provided now!).
8. Conform to IRC § 7491(c) on the burden of production being on the government.
9. Permit taxpayers to direct that payments be applied first to satisfy GET taxes, then to penalties and interest.
10. On liquidation, limit personal liability to the value of assets distributed to the responsible person being assessed.

Very truly yours,

CHUN, KERR, DODD, BEAMAN & WONG,  
a Limited Liability Law Partnership



Ray Kamikawa

TESTIMONY OF THE AMERICAN COUNCIL OF LIFE INSURERS  
IN SUPPORT OF SENATE BILL 2238, SD 1, RELATING TO TAXATION

March 13, 2012

Via e mail: [erbtestimony@capitol.hawaii.gov](mailto:erbtestimony@capitol.hawaii.gov)

Hon. Representative Angus L. K. McKelvey, Chair  
Hon. Representative Isaac Choy, Vice-Chair  
Committee on Economic Revitalization and Business  
State House of Representatives  
Hawaii State Capitol, Room 312  
415 South Beretania Street  
Honolulu, Hawaii 96813

Dear Chair McKelvey, Vice-Chair Choy and Committee Members:

Thank you for the opportunity to testify in Support of SB 2238, SD1, relating to Taxation.

Our firm represents the American Council of Life Insurers (“ACLI”), a national trade association, who represents more than three hundred (300) legal reserve life insurer and fraternal benefit society member companies operating in the United States. These member companies account for 90% of the assets and premiums of the United States Life and annuity industry. ACLI member company assets account for 91% of legal reserve company total assets. Two hundred thirty-five (235) ACLI member companies currently do business in the State of Hawaii; and they represent 93% of the life insurance premiums and 92% of the annuity considerations in this State. Four fraternal benefit society member companies operate in the State of Hawaii.

SB 2238, SD1, repeals Act 155 which requires all businesses that are exempt from Hawaii’s general excise tax to register to do business in the State and file their general excise tax returns and affirmatively claim their exemptions.

A fraternal benefit society is exempt from Hawaii’s general excise tax under Section 237-23(a) and (b), HRS.

Under Act 155, if a fraternal benefit society fails to file its annual general excise tax return (form G-49) within 12 months of its due date it forfeits its excise tax exemption.

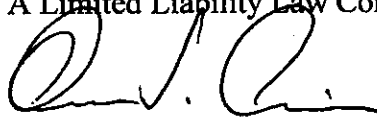
The severe penalty of the forfeiture of a fraternal’s exemption solely because it fails to file the required return and to claim its exemption is unwarranted and is out of proportion to the Act’s stated purpose – to capture relevant information on claims for the general excise tax benefits. The loss of a fraternal society member company’s exemption would reduce its ability to provide the kinds and level of services and programs to its members and the members of their communities in which they live.



On behalf of its fraternal benefit society member companies, therefore, ACLI supports the repeal of Act 155 and respectfully requests that this Committee pass SB 2238, SD1, into law.

Again, thank you for the opportunity to testify in support of SB 2238, SD1.

LAW OFFICES OF  
OREN T. CHIKAMOTO  
A Limited Liability Law Company



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737 Bishop Street, Suite 2100  
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February 22, 2012

Representative Angus McKelvey  
Chair, Committee on Economic Revitalization and Business  
Hawaii State House of Representatives  
State Capitol, Room 312  
Honolulu, HI 96813

RE: SB 2238, SD 1, Relating to General Excise Tax

Dear Chair McKelvey, Vice-Chair Choy and members of the House Committee on Economic Revitalization and Business:

The Hawai'i Alliance of Nonprofit Organizations (HANO) supports SB 2238, SD 1, which repeals Act 155. HANO is a statewide, sector-wide professional association for nonprofits. HANO member nonprofits provide essential services to every community in the state. Our mission is to unite and strengthen the nonprofit sector as a collective force to improve the quality of life in Hawai'i.

Act 155 stipulates possible tax-exemption revocation for a nonprofit that willfully neglects to file the annual G-49 form within 12 months of the due date. This policy does not provide sufficient due process, as it is a significant departure from the existing tax law and will most likely cause confusion among nonprofits in terms of their tax reporting requirements and tax obligations.

The proposed sec. 237(c) of Act 155 gives the Director the power to "waive the denial of the GET benefit....if the failure to comply is due to reasonable cause and not willful neglect." It is not clear how "reasonable cause" is defined. At the very least, it should be clear to nonprofit organizations what constitutes reasonable cause.

Section 237(b) holds "any officer, member, manager, or other person.." personally liable who does not fulfill the organization's general excise tax obligation.. It is not clear whom this broad application extends to. More specificity is required. Personal liability will hinder board volunteerism in our sector when it is already very challenging for nonprofits to find good volunteers.

Personal liability and possible revocation of an organization's tax-exempt status are disproportionate and severe ramifications for an unclear tax policy and will distract from our ability to deliver on our missions to improve the quality of life in our community.

Thank you for the opportunity to provide testimony on SB 2238, SD 1.

Mahalo,  
Lisa Maruyama  
President and CEO



The Voice of Small Business®

**Before the House Committee on  
Economic Revitalization and Business**

DATE:	Thursday, March 15, 2012
TIME:	9:45 A.M.
PLACE:	Conference Room 312

**Re: SB 2238, SD1 Relating to Taxation**

**Testimony of Melissa Pavlicek for NFIB Hawaii**

We are testifying on behalf of the National Federation of Independent Business (NFIB) in support to SB 2238, SD1 relating to taxation. NFIB Hawaii supports this measure.

SB2238, SD1 Repeals Act 155, Session Laws of Hawaii 2010, which requires all businesses with excise tax exemptions to register to do business in Hawaii, file their tax returns in a timely manner, and expressly claim their entitlement, and creates a personal trust liability for businesses that use the general excise tax as the basis for increasing their prices and ensures that those funds are paid to the State for the benefit of consumers and businesses.

The NFIB Hawaii Leadership Council has identified this as the most important issue impacting Hawaii's small business community this session. Act 155 has imposed unnecessary and cumbersome burdens on small business owners by requiring them to obtain GET licenses and file GET tax returns even if they do not have GET liability. Most significantly, the Act exposes business owners to personal trust fund liability even though GET is not held in trust for other parties. These mandates are inappropriate and impose unreasonable burdens upon Hawaii's small business community. NFIB Hawaii supports the repeal of Act 155 through SB 2238, SD1.

The National Federation of Independent Business is the largest advocacy organization representing small and independent business in Washington, D.C., and all 50 state capitals. In Hawaii, NFIB represents more than 1,000 members. NFIB's purpose is to impact public policy at the state and federal level and be a key business resource for small and

independent business in America. NFIB also provides timely information designed to help small businesses succeed.

Mahalo for your consideration.

Ronald I. Heller  
700 Bishop Street, Suite 1500  
Honolulu, Hawaii 96813

phone 808 523 6000 fax 808 523 6001  
rheller@torkildson.com

**TESTIMONY BEFORE THE COMMITTEE ON ECONOMIC  
REVITALIZATION & BUSINESS**

**In Support of Senate Bill 2238, SD 1**  
*(repeal of Act 155, 2010)*

**Tuesday, March 13, 2012 at 8:30 am**  
**State Capitol, Conference Room 312**

Chair McKelvey, Vice-Chair Choy, and Members of the Committee:

Thank you for the opportunity to testify. My name is Ronald Heller. I am a practicing attorney, and also licensed as a Certified Public Accountant. In 2010, I opposed House Bill 2595, which became Act 155. I am now supporting Senate Bill 2238, which would repeal Act 155.

In 2010, I said:

Overall, I think that passing this bill would create a number of serious problems. If we are going to consider changes as drastic as these – and I don't think we should – it ought to be given far more study first.

We are now seeing that Act 155 has indeed caused a great deal of confusion and concern. Some of that has been alleviated by the Department of Taxation announcing that it will NOT take away tax benefits in certain situations (see Tax Information Release 2010-5) but that is a mere announcement, without the force of law and subject to change at any time.

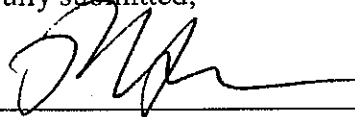
As actually written, Act 155 creates consequences for taxpayers that are totally out of proportion to any error by the taxpayer. For example, suppose you own an apartment that you rent out, and you pay \$60 or \$70 per month in General Excise Tax. You file all of your monthly GET returns on time, and pay your taxes in full and on time. During the tax year, you sell the

apartment for \$300,000. That sale is not subject to General Excise Tax, because the sale of land and improvements to land is exempt. However, you forget to file your annual reconciliation return. (You filed all of the monthly returns, on time – you just forgot about the annual return form.) Under Act 155, you lose the “tax benefit” of the exemption on the sale, and you owe 4% tax (or 4.5% on Oahu) on the entire \$300,000 – a \$12,000 tax (or \$13,500 if you’re on Oahu). **The bottom line is effectively a penalty of \$12,000 (or \$13,500) even though you filed all of your monthly returns on time and paid all of your tax on time, just for forgetting to submit the annual form.** This is grossly unreasonable – the punishment is completely out of proportion to the “offense.”

The Department of Taxation may say that they would not impose such a drastic and unreasonable penalty, but the law says that they can do it.

This is just one example – many others are possible. The point is that Act 155, as actually adopted by the Legislature, creates the potential for punishments that are absurd and excessive. Relying on the Department of Taxation to NOT enforce the law is a poor solution. Repealing it makes more sense.

Respectfully submitted,



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Ronald I. Heller

RICHARD PAUL McCLELLAN III

LAWYER

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TESTIMONY IN SUPPORT OF SB 2238, SD 1

(Repeal of Act 155 of 2010)

Tuesday, March 13, 2012, 8:30 a.m., Committee on Economic  
Revitalization & Business

March 10, 2012

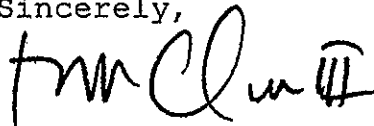
Dear Honorable Chair Angus L.K. McKelvey, Vice-Chair Isaac W.  
Choy, And Committee Members:

As a lawyer with a primary practice representing taxpayers  
before our Department of Taxation and the Internal Revenue  
Service, I urge your support of SB 2238 which repeals Act 155 of  
2010 in its entirety.

Our tax system is founded upon a concept of voluntary compliance  
and voluntary self-assessment. Provisions in our tax code that  
are perceived as unfair by taxpayers undermine respect for the  
law and inevitably affect the efficiency of our system of tax  
administration. While most taxpayers would understand paying  
penalties and interest for being late, few would understand  
paying a higher tax rate plus penalties and interest for filing  
late. This would be considered grossly unfair and overreaching.

Act 155 also creates a personal liability for general excise  
taxes. The Department of Taxation asserted that this was to  
impose liability upon unscrupulous business owners. Act 155's  
main victims, however, are likely to be volunteers and  
inexperienced, start-up businesses. Again, this can only serve  
to discourage and penalize persons attempting to better our  
economy and society.

Sincerely,



Richard McClellan

PETER L. FRITZ  
414 KUWILI STREET, #104  
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**HOUSE OF REPRESENTATIVES  
THE TWENTY-SIXTH LEGISLATURE  
REGULAR SESSION OF 2012**

**COMMITTEE ON  
COMMITTEE ON ECONOMIC REVITALIZATION & BUSINESS**

**Hearing March 13, 2012  
Testimony on S.B. 2238 SD1  
(Relating to Taxation)**

Chair McKelvey, Vice-Chair Choy and Members of the Committee, my name is Peter Fritz. I am an attorney specializing in tax matters. I am testifying **in support** of S.B. 2238.

Act 155, Session Laws of Hawaii 2010 added two new sections to Chapter 237, Hawaii Revised Statutes §237-9.3 and §237-41.5 created new and disproportionate penalties for the simple failure to file a General Excise Tax (“GET”) return and personal liability for unpaid GET.

Act 155 classified GET taxes as trust fund taxes. A responsible person has personal liability for unpaid trust fund taxes. Examples of responsible persons are directors, officers, an employee with check signing privileges or responsible for preparing the forms to remit the taxes. When the Internal Revenue Service asserts personal liability for trust fund taxes, personal liability is often asserted against all directors. The director of the company will have to prove that he/she is not a responsible person.

This potential for personal liability has made it difficult for nonprofit organizations to recruit qualified directors. People are reluctant to serve on the board because they can have personal liability for taxes that they did not think were owed. For example, a nonprofit organization holds a fund raising dinner at \$500.00 a ticket. It calculates that contribution portion of the ticket’s price is \$600.00. If the Department of Taxation (“Department”) audits the organization and determines that the deductible portion of the ticket should have been \$400.00, the director/responsible person would have personal liability for the GET on the \$200.00 for each ticket that was sold.

The lack of guidance from the Department makes the risk even greater. For example, a taxpayer, after examining all of the available guidance determined that the tax was .05% on a transaction. However, if the Department of Taxation disagrees and imputes a rate of 4%, the taxpayer would be personally liable for 4%. Considering that the Department has been working on some GET rules projects for more than 10 years, it is unfair to impose personal liability without providing guidance to taxpayers. It is a trap for the unwary. Under §237-9.3, a nonprofit that fails to file the annual general excise tax return “not later than twelve months from the due date prescribed for the return” forfeits the right to claim any excise tax exemption or benefit under the General Excise Tax (GET) law. As currently written, a taxpayer that failed to



Testimony of Peter L. Fritz on S.B. 2238

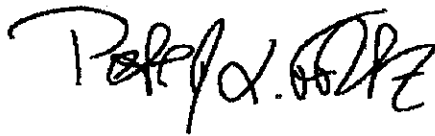
Hearing Date - March 13, 2012

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file the return is estopped from filing the return and may have to file a new G-6 to requalify as a nonprofit organization

These benefits are forfeited even though the taxpayer filed every periodic return required under the GET law. This is a draconian penalty. There is no basis for this harsh penalty. The harshness is not ameliorated by the Department of Taxation's Tax Information Release 2010-5 as it does not have the force of law and is subject to change at any time.

Respectfully Submitted,

A handwritten signature in black ink, appearing to read "Peter L. Fritz". The signature is written in a cursive, somewhat stylized font.