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LATE TESTIMONY

To: The Honorable Angus McKelvey, Chair,
and Members of the House Committee on Economic Revitalization and Business

Date: Thursday, March 15, 2012
Time: 9:45 A.M.
Place: Conference Room 312, State Capitol

From: Frederick D. Pablo, Director
Department of Taxation

Re: S.B. 2947, S.D. 2, Proposed H.D. 1 Relating to Taxation

The Department of Taxation (Department) appreciates the intent of S.B. 2947 S.D. 2, Proposed H.D. 1 and offers the following comments for the Committee's consideration.

S.B. 2947 S.D. 2, Proposed H.D. 1 contains four main parts. The first part, comprised of the proposed bill's section 1, creates an award for whistleblowers who provide information that is the basis for a Department of Taxation proceeding with an administrative or judicial action for a violation of any tax law under Title 14 of the Hawaii Revised Statutes. The second part, comprised of the proposed bill's section 2, authorizes the Director of Taxation to appoint an administrative appeals officer. The third part, comprised of sections 3, 4 and 5 of the proposed bill, prohibits the stacking of the penalties for willful failure to collect and pay over, for substantial understatement or misstatements, and for erroneous refund claims. The fourth part, comprised of section 6 of the proposed bill, requires all advertisements and solicitations for transient accommodations to display the registration identification number or the website address containing the registration identification number.

PART ONE: Regarding the whistleblower portion of the bill, the Department notes its contents are similar to that of H.B. 1672, H.D. 1. The Department supports both that measure and this part of this proposed H.D.1, however recommends that the bill be amended to more closely resemble the federal whistleblower incentive under Internal Revenue Code section 7623. In amending H.B. 1672, the committee on Judiciary used language from IRC § 7623 to give the Director of Taxation authority to modify the amount of rewards where the basis of an administrative or judicial action is principally derived sources other than the individual. The Department recommends the committee further examine IRC § 7623, in particular subsection (a) and its provisions:

- Relating to the types of administrative actions that entitle the individual to the incentive. For instance, IRC § 7623(a) specifies that awards will be paid for detecting underpayments of tax , or detecting and bringing to trail persons who commit tax crimes.
- Specifying that the award is not available in cases where other financial incentives are provided by law.
- Specifying that the award be paid from proceeds of amounts collected.

PART TWO: The Department is in strong support of providing the Director of Taxation the ability to appoint an administrative appeals officer. The ability to appoint an individual to this position will enable the Department to move forward with implementing HRS Section 231-7.5.

PART THREE: Regarding the penalty stacking portion of the bill, the Department appreciates the intent to prevent stacking of certain penalties. However, the Department has concerns with the bill as currently written. The Department believes the intent of the bill is to prevent the stacking of civil penalties for understatements and erroneous refund and credit claims, which would bring the State more into conformity with the IRS's civil penalty stacking procedures.

However, the proposed draft may have the unintended consequence of preventing criminal prosecution in cases of fraud and willful failure to collect and pay over tax. The Department defers to the Department of the Attorney General for a final analysis, but relays its potential concerns below:

HRS §§ 231-36 and 231-36.4 are not civil penalty sections. Rather, they impose criminal penalties which can be imposed only upon conviction in a court of law. By preventing the imposition of these penalties in cases where civil penalties have already been assessed under HRS § 231-36.6 or 231-36.8, this bill would prevent these prosecutions in cases where the Department has already imposed a civil fine.

If the Committee's intent is to only prevent the stacking of civil penalties, and not prevent criminal prosecution in cases of fraud or willful failure to collect and pay over, the Department recommends the Committee amend the bill to only affect HRS §§ 231-36.6 and 231-36.8.

The Department also notes that, even if the committee amends the bill to only contain the anti-stacking provisions in HRS §§ 231-36.6 and 231-36.8, this would not bring the State into conformity with the IRS's civil penalty stacking procedures. Under federal law, willful failure to collect and pay over is subject to both civil penalties (IRC § 6672) and criminal penalties (IRC § 7202). Under IRC § 6672, willful failure to collect and pay over tax may result in a penalty of up to 100% of the underpayment. Such a strong penalty is the reason there is a corresponding anti-stacking provision. If a taxpayer has been subjected to a 100% fine, there is perhaps little need to assess additional penalties for substantial understatement or erroneous claim for refund.

Under Hawaii State tax law, however, there is no such 100% civil penalty for willful failure to collect and pay over; there is merely the criminal penalty. Thus, the lack of anti-stacking protection is less of an issue. If it the bill is meant to bring Hawaii's penalty provisions more in line with the federal provisions, the bill would also need to be amended to create a new section imposing a civil willful failure to collect and pay over penalty.

PART FOUR: Regarding the transient accommodations advertisement portion of the bill, the Department is in support as it will aid transient accommodations tax compliance.

Thank you for the opportunity to provide comments.