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To: The Honorable David Y. Ige, Chair
and Members of the Senate Committee on Ways and Means

Date: Monday, February 4, 2013
Time: 10:00 a.m.
Place: Conference Room 211, State Capitol

From: Frederick D. Pablo, Director
Department of Taxation

Re: S.B. No. 1289 Relating to Taxation

The Department of Taxation (Department) appreciates the intent of S.B. 1289 and provides the following information and comments for your consideration.

S.B. 1289 requires payors of non-wage payments for construction services to report the payments to the Department of Taxation and to the provider of construction services. The measure is effective upon approval, and applies to taxable years beginning after December 31, 2012.

The Department suggests the following amendments to this measure:

- Electronic filing of such a report will allow the Department to be able to efficiently analyze the data received and ease the burden of administration.
- Change the due date of the report in subsection (b) to the last day of the third month following the close of the taxable year. This will provide ample time for the taxpayer to comply with the report filing requirements and accommodate taxpayers who operate on different fiscal years.
- In subsection (c) have the payor submit the report directly to the Department of Labor and Industrial Relations instead of having the Department of Taxation forwarding the report. This prevents any issues regarding disclosure of confidential tax information.
- Clarify that subsection (d) assesses a civil penalty for late filing.
- Clarify that subsection (e) subjects willful acts of nonfiling to criminal penalties under section 231-35, Hawaii Revised Statutes.

- Change Section 3 of this measure, by applying this measure to taxable years beginning after December 31, 2013. This will give the Department and taxpayers sufficient time to prepare for the new reporting requirements.

Thank you for the opportunity to provide comments.

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The Pacific Resource
PARTNERSHIP



Testimony of Cindy McMillan
The Pacific Resource Partnership

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

SB 1289 – Relating to Taxation
Monday, February 4, 2013
10:00 am
Conference Room 211

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

My name is Cindy McMillan, and I'm representing The Pacific Resource Partnership (PRP), a labor-management consortium representing over 240 signatory contractors and the Hawaii Regional Council of Carpenters.

PRP supports SB 1289, Relating to Taxation which requires payors of non-wage payments for construction services to report the payments to the department of taxation and the provider of construction services.

This bill will close a tax loophole allowing the state to raise revenues while ensuring a level playing field for law-abiding construction companies.

Unscrupulous construction companies can intentionally defraud the state of tax revenues because there is no federal or state law that tracks payments made by a business to an incorporated business. Form 1099 reporting is only required by federal law if the subcontractor, or service provider, is *un*incorporated. Most construction businesses are incorporated. Under the current law, if a contractor pays \$1million to a dishonest incorporated subcontractor, the subcontractor can report whatever it wants, or nothing at all to state taxing authorities.

This bill closes that loophole on the state level by requiring reporting of payments to construction businesses, whether or not they are incorporated. This will allow state taxing authorities to track payments to make sure that the construction business receiving the payment is paying all of its appropriate state taxes. Tax fraud detection and more efficient, focused auditing, can be achieved when there is reporting of transactions, rather than self-reporting by each single entity.

This bill also eliminates the unfair advantage dishonest companies have over those who play by the rules. Cheating contractors use subcontractors that break the law by paying their workers off the books. In this way, those contractors evade payments on state and federal income and employment taxes and workers' compensation premiums. This allows them to underbid and steal work away from honest, tax-paying contractors. The current loophole favors the cheaters while denying our state government much needed revenue.

Formalizing the reporting requirement will cost honest businesses much less than the income lost from jobs stolen by corrupt contractors. Form 1099 reporting is already required if the independent contractor is an individual or other unincorporated entity. Honest businesses are also indirectly paying higher unemployment insurance and other taxes to make up for cheating contractors who are not paying into the system.

Reporting encourages proper declaration of income and payment of taxes. A similar measure is in place for payments to construction contractors in Canada, and it has raised revenue. This is a way of raising revenue by not raising taxes.

For these reasons we respectfully request that you support this measure.

Mahalo for the opportunity to share our views on this matter.