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JOSHUA WISCH
DEPUTY DIRECTOR

To: The Honorable Sylvia Luke, Chair
and Members of the House Committee on Finance

Date: Wednesday, February 26, 2014
Time: 11:15 a.m.
Place: Conference Room 308, State Capitol

From: Frederick D. Pablo, Director
Department of Taxation

Re: H.B. 2370 Relating to Taxation

Department of Taxation (Department) appreciates the intent of H.B. 2370, but is opposed to the application of partial payment of taxes equally to interest, penalties, and principal due to the impact it will have on the Department's limited budget and staffing resources, if adopted.

H.B. 2370 amends section 231-27, Hawaii Revised Statutes (HRS), to change the hierarchy of partial payment from first to interest, then to penalties, and then to principal, to prorated amount (in equal amounts). The measure, if adopted, will take effect upon its approval.

The measure as written will require immediate changes to the Department's procedures and computer system; significant resources would be needed to complete the substantial computer modifications. As the Legislature is aware, the Department has an outdated computer system with significant functionality issues. Staffing resources necessary to develop and implement modifications to the system also are insufficient.

The Department currently is embarking on procuring and developing a new computer system commonly referred to as Tax System Modernization. As a result, the Department's limited resources must be prioritized to address other significant projects that will occur over the next few years, and respectfully request that no new projects be imposed on the Department.

Finally, if at a later date, the Legislature wanted to revisit the allocation of partial payments, rather than follow the allocation proposed in H.B. 2370, the Department suggests following the federal method of partial payment allocation; payments are generally allocated to the earliest unpaid and collectible liability, owed and due as of the payment availability date. For example, the oldest open Collection Statute Expiration Date is applied in the following order: (1)

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Tax; (2) Tax Motivated Transaction (TMT) tax; (3) Penalties and fees; (4) Non-TMT interest; and (5) TMT interest. The Department generally supports conforming to the federal statutes, but respectfully requests that the Department be allowed to focus on its Tax System Modernization effort over the next few years.

Thank you for the opportunity to provide comments.

TAXBILLSERVICE

126 Queen Street, Suite 304

TAX FOUNDATION OF HAWAII

Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: ADMINISTRATION, Partial payment of taxes

BILL NUMBER: HB 2370

INTRODUCED BY: Fukumoto, Brower, Creagan, Fale, Kawakami, McKelvey and 3 Democrats

BRIEF SUMMARY: Amends HRS section 231-27 to provide that a partial payment of an assessment of taxes shall be credited to interest, penalties, then principal in equal amounts.

EFFECTIVE DATE: Upon approval

STAFF COMMENTS: Currently, when the department of taxation receives a partial payment for an assessment of taxes due, the payment is applied to interest, penalties, then principal. The proposed measure would allow payments to be applied to interest, penalties, then principal in equal amounts. A few years ago when a similar measure was proposed, the department of taxation stated that the adoption of this measure would be contrary to the state's fiscal interest since "state law dictates that tax payments are to be paid first to interest, then penalties, and principal which ensures payment so interest (reflecting time value of money) as the priority, followed by penalties, and then principal. By paying principal last, the State is ensured the optimal time value of money when the principal is paid last and payments are spread over time."

The department also states that to implement this legislation, it would require a substantial investment in the department's computer system.

But more importantly, the department also stated that the adoption of this measure would result in a revenue loss of \$1 million the first year; \$2 million in the second year; and \$3 million in the third year after implementation.

By comparison, for federal purposes Rev. Proc. 2002-26, section 3.02, provides that taxpayers are allowed to designate application of partial payments of tax, and if there is no designation, the payment is applied to tax, penalties and interest, in that order.

Digested 2/25/14

Gerald Gregory

95-201 Kui' kepa Place

Mililani Hi., 96789



Representative Sylvia Luke
Chair, Finance Committee
State Capitol, Room 306
Honolulu Hawaii., 96813

RE: HB 2370

SUBJECT: Move HB 2370

Dear Chair Luke,

This letter is in support of HB 2370 and ask that you move this bill. The Director of Taxation has stated that this already administratively possible to accommodate request to pay across the board on interest, penalties, and principal and in certain circumstances but yet what circumstances is not clarified by the Director of Taxation .Since march of 2008 I have personally made payments in person so I could meet other tax payers to talk and listen to their problems with their taxes. Also the Tax Department has always taken payments and applied them to the oldest tax because that is their policy (not the law) but that is not always beneficial to the taxpayer because is they are applying it to the oldest tax it has the higher interest, it is better to apply it to the most recent years because interest is smallest and you can move to the penalty and principal faster therefore paying off the year in questions faster and paying less interest. The longer you don't touch the recent years it lets a high amount of taxes owed gain a substantial amount of interest (%) before getting to it when it becomes the oldest tax. The Director of Taxation is aware of this practice at the Department of Taxation but does nothing about it because this would also be considered lost revenue. There is no law that allows this practice to gain revenue but yet they do it with no hesitation. This Bill HB (2370) is to encourage people to pay more revenue which would be worth the small amount of revenue the Department of Taxation is assuming it will lose. There is a time for change and fairness in the Department of Taxation and that time is now when change is taking place.

Hawaii, Revised Statute: Section 231-27 was enacted in 1949 (S.B. No. 412, Act 312, Session Laws of Hawaii 1949) and the distribution of partial payment of taxes has not been amended since the original enactment. Except for the Committee Reports issued by the Committee on Ways and Means (SSCR 387) and Committee on Finance (HSCR 86), there is no explanation for the rational or legislature intent in the enactment of the law the Committee on Ways and Means (SCCR) stated that.

The purpose of this bill is to require all partial payments of a particular assessment of taxes to be devoted first to delinquent interest, then to penalties and then to principal. At the time present time, a taxpayer has no choice. Since the delinquent interest only on principal and penalties, it is obvious that one devoting his partial payment first to principal or penalties is in a better position than the devoting his partial payment first to interest. The bill would remedy this inequality

Tax Foundation of Hawaii stated in testimony (no opposition or support of HB 2370), That the Federal Government implemented an additional payment option on Jan 17, 2005 known as the partial payment installment agreement (PPIA). The new payment option became possible of the American Jobs Creations Act of 2004.

The Director of Taxation has testified on record about leveling the field between Federal, State, and Taxpayer. He had referred to the Sarbanes-Oxley Act. He says penalties are drawn from the Internal Revenue Code (IRC) sections 6694 and 7407. Sometimes leveling the field such as SB 76 affects revenue. The people are in hard economic times in step with the State being in hard economic times. The Director has constantly stated fairness HB 2370 does not take away any money owed the state. Should SB76 allow taxpayers to pay off their taxes faster why would the Dept of Taxation oppose such a possibility of a taxpayer paying their debt faster. Why has the Department of Taxation become so addicted to penalties and interest? The taxpayer is also paying for the addition of penalties, because they cannot deduct the penalties from their income because they are not tax deductible and must leave them as income and are taxed again

I strongly support HB 2370 and encourage you to move this bill and support its passage. We are all in economic hard times let's do it together, a humble constituent

Very truly yours
Gerald Gregory
(Humble Constituent)



Chamber of Commerce HAWAII

The Voice of Business

**Testimony to the House Committee on Finance
Wednesday, February 26, 2014 at 11:15 A.M.
Conference Room 308, State Capitol**

LATE

RE: HOUSE BILL 2370 RELATING TO TAXATION

Chair Luke, Vice Chairs Nishimoto and Johanson, and Members of the Committee:

The Chamber of Commerce of Hawaii ("The Chamber") **supports** HB 2370 Relating to Taxation.

The Chamber is the largest business organization in Hawaii, representing over 1,000 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 members and the entire business community to improve the state's economic climate and to foster positive action on issues of common concern.

The Chamber believes that the amendments provided in HB 2370 is more equitable for both businesses and taxpayers. The bill would alleviate tax burdens to all parties.

Thank you for the opportunity to testify.