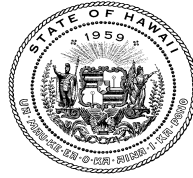


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To: The Honorable Jill N. Tokuda, Chair
and Members of the Senate Committee on Ways and Means

Date: February 25, 2016

Time: 1:00 P.M.

Place: Conference Room 211, State Capitol

From: Maria E. Zielinski, Director
Department of Taxation

Re: S.B. 2924, S.D. 1, Relating to the Disclosure of Tax Return Information.

The Department of Taxation (Department) strongly supports S.B. 2924, S.D. 1, an Administration measure, and provides the following comments for your consideration.

S.B. 2924, S.D. 1, amends section 231-18, Hawaii Revised Statutes (HRS), to allow disclosure of tax return information to the Department of the Attorney General for certain court proceedings, to federal or state officials for federal or state judicial or administrative tax proceedings, to federal, state, or local law enforcement officials for investigation or prosecution of identity theft or fraudulent tax refund claims, or to other persons, such as hardware and software contractors, to the extent necessary to provide services to the department for purposes of tax administration. S.B. 2924, S.D. 1, also clarifies that all information filed under chapter 235, HRS, with any state agency is confidential. S.D. 1 has a defective effective date of January 7, 2059.

The Department believes that the amendments to section 231-18, HRS, will help clarify some of the common, specific instances where the Department may disclose tax return information. These amendments are modeled after the exemptions codified in section 6103 of the Internal Revenue Code.

The Department notes that the proposed amendment to section 235-116, HRS, is necessary to clarify that the information filed with other state agencies is confidential. Hawaii income tax credits are often certified prior to filing of the credit claim with the Department in order to determine whether the taxpayer qualifies for the credit and to administer aggregate caps of such tax credits. The information being submitted to the other state agencies contains personal identifying information as well as business and trade information that is not for public dissemination.

In addition, it is important to note that this amendment would not preclude the Legislature from enacting legislation that specifically states that certain information provided by a taxpayer would be made public. For example, a new tax credit could contain language that would require a taxpayer to submit a report to a state agency, which would be published, as a prerequisite to claiming a tax credit.

Thank you for the opportunity to provide comments.

TAX FOUNDATION OF HAWAII

126 Queen Street, Suite 304

Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: INCOME, ADMINISTRATION, Disclosure of Tax Return Information

BILL NUMBER: SB 2924, SD-1

INTRODUCED BY: Senate Committee on Judiciary and Labor

EXECUTIVE SUMMARY: Technical amendments to allow explicitly certain forms of interagency disclosure, and to specify that income tax information is confidential even in the hands of another agency.

BRIEF SUMMARY: Amends section 231-18, Hawaii Revised Statutes, to allow disclosure of tax return information to the Department of the Attorney General, federal, state, or local officials, and other persons in specified situations. Amends section 235-116, Hawaii Revised Statutes, to clarify that all information filed under chapter 235, Hawaii Revised Statutes, with any state agency is confidential.

EFFECTIVE DATE: January 7, 2059.

STAFF COMMENTS: This bill is sponsored by the Department of Taxation TAX-04 (16).

According to the Department's justification sheet accompanying the bill, the amendment to section 231-18 will allow disclosure of tax return information to the Department of the Attorney General for certain court proceedings, to federal or state officials for federal or state judicial or administrative tax proceedings, to federal, state, or local law enforcement officials for investigation or prosecution of identity theft or fraudulent tax refund claims, or to other persons to the extent necessary to provide services to the department for purposes of tax administration. This provision appears to be comparable to federal provisions allowing disclosure of tax information (section 6103, Internal Revenue Code).

Also, the Department asserts that the amendment to section 235-116, HRS, is needed to clarify that all information filed under the Income Tax Law with any state agency is confidential. The proposed amendment extends this protection to any tax returns and return information required to be filed, submitted, collected, or maintained under the Income Tax Law. Perhaps some clarification is necessary to make sure that records kept in the ordinary course of business, which are required to be maintained under the tax laws, are not unduly constrained.

Digested 2/23/2016

PETER L. FRITZ

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THE SENATE
THE TWENTY-EIGHTH LEGISLATURE
REGULAR SESSION OF 2016

COMMITTEE ON WAYS AND MEANS
Testimony on S.B. 2924 SD1
Hearing: February 25, 2016
Time: 1:00 PM

(RELATING TO THE DISCLOSURE OF TAX RETURN INFORMATION)

Chair Tokuda, Vice Chair Dela Cruz, and members of the Committee. My name is Peter Fritz. I am an attorney and a former Rules Specialist for the Department of Taxation. I am offering comments and respectfully submit that this bill needs to be amended to include adequate safeguards for taxpayers whose privacy interests are implicated.

Senate Bill 2924 SD1 takes language from Internal Revenue Code ("I.R.C.") § 6103 and amends § 231-18, Hawaii Revised Statutes, to expand disclosure of tax return information to the Department of the Attorney General, federal, state, or local officials, and other persons in specified situations. Unfortunately, administration bill SB 2924 SB1 did not take the language of I.R.C. § 6103 that safeguards the information.

Safeguards were important to the conferees when considering I.R.C. § 6103. The conferees keenly recognized that the taxpayer's right to privacy was extremely important: "[T]he privacy of the taxpayer who is the subject of the advice must be protected. Any procedure for making such advice public must therefore include adequate safeguards for taxpayers whose privacy interests are implicated." Bill Archer et al., Conference Report on H.R. 2676, Internal Revenue Service Restructuring and Reform Act of 1998, H.R. Rep No. 105-599, at 299 (1998). Technical, administrative, and physical safeguard provisions to prohibit recipients of returns or return information from using or disclosing the information in an unauthorized manner, and accounting, recordkeeping, and reporting requirements that detail the purposes for which certain disclosures were made. See I.R.C. § 6103(p).

Section 6103 provides that the IRS may not furnish returns and return information to another agency unless that agency establishes procedures satisfactory to the IRS for safeguarding the returns or return information it receives. Disclosure to other agencies is conditioned on the recipient: maintaining a secure place for storing the information; restricting access to the information to people to whom disclosure can be made under the law; restricting the use of the information to the purpose for which it was provided; providing other safeguards necessary to keeping the information confidential; and, returning or destroying the information when the agency is finished with it. The IRS must review, on a regular basis, safeguards established by other agencies.

If there are any unauthorized disclosures by employees of the other agency, the IRS may discontinue disclosures of returns or return information to that agency until it is satisfied that the agency took adequate protective measures to prevent a repetition of the unauthorized disclosure.

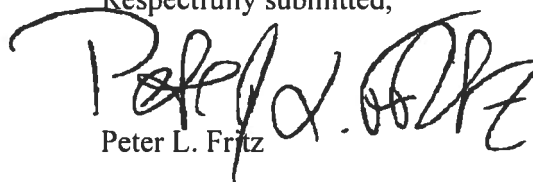
Testimony of Peter L. Fritz
S.B. 2924 SB1
February 25, 2016

In addition, the IRS may terminate disclosure to any agency if the IRS determines that adequate safeguards are not being maintained by the agency in question.

There must be public confidence with respect to the confidentiality of personal and financial information given to the Department of Taxation for tax administration purposes. To ensure public confidence safeguards are needed. The Department of Taxation should draft an amendment to SB 2924 SD1 to incorporate safeguards similar to those in I.R.C. 6103(p).

A copy of I.R.C. § 6103(p) is attached to my testimony.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Peter L. Fritz". The signature is stylized and cursive, with a large initial "P" and "F".

Peter L. Fritz

1141(h)(2) of the Social Security Act) in the possession of the Department of the Treasury upon completion of their use in making the disclosure required under subparagraph (A), so as to make such records undisclosable.

(7) Social security account statement furnished by Social Security Administration

Upon written request by the Commissioner of Social Security, the Secretary may disclose the mailing address of any taxpayer who is entitled to receive a social security account statement pursuant to section 1143(o) of the Social Security Act, for use only by officers, employees or agents of the Social Security Administration for purposes of mailing such statement to such taxpayer.

(n) Certain other persons

Pursuant to regulations prescribed by the Secretary, returns and return information may be disclosed to any person, including any person described in section 7513(a), to the extent necessary in connection with the processing, storage, transmission, and reproduction of such returns and return information, the programming, maintenance, repair, testing, and procurement of equipment, and the providing of other services, for purposes of tax administration.

(o) Disclosure of returns and return information with respect to certain taxes

(1) Taxes imposed by subtitle E

(A) In general

Returns and return information with respect to taxes imposed by subtitle E (relating to taxes on alcohol, tobacco, and firearms) shall be open to inspection by or disclosure to officers and employees of a Federal agency whose official duties require such inspection or disclosure.

(B) Use in certain proceedings

Returns and return information disclosed to a Federal agency under subparagraph (A) may be used in an action or proceeding (or in preparation for such action or proceeding) brought under section 625 of the American Jobs Creation Act of 2004 for the collection of any unpaid assessment or penalty arising under such Act.

(2) Taxes imposed by chapter 35

Returns and return information with respect to taxes imposed by chapter 35 (relating to taxes on wagering) shall, notwithstanding any other provision of this section, be open to inspection by or disclosure only to such person or persons and for such purpose or purposes as are prescribed by section 4424.

(p) Procedure and recordkeeping

(1) Manner, time, and place of inspections

Requests for the inspection or disclosure of a return or return information and such inspection or disclosure shall be made in such manner and at such time and place as shall be prescribed by the Secretary.

(2) Procedure

(A) Reproduction of returns

A reproduction or certified reproduction of a return shall, upon written request, be fur-

nished to any person to whom disclosure or inspection of such return is authorized under this section. A reasonable fee may be prescribed for furnishing such reproduction or certified reproduction.

(B) Disclosure of return information

Return information disclosed to any person under the provisions of this title may be provided in the form of written documents, reproductions of such documents, films or photoimpressions, or electronically produced tapes, disks, or records, or by any other mode or means which the Secretary determines necessary or appropriate. A reasonable fee may be prescribed for furnishing such return information.

(C) Use of reproductions

Any reproduction of any return, document, or other matter made in accordance with this paragraph shall have the same legal status as the original, and any such reproduction shall, if properly authenticated, be admissible in evidence in any judicial or administrative proceeding as if it were the original, whether or not the original is in existence.

(3) Records of inspection and disclosure

(A) System of recordkeeping

Except as otherwise provided by this paragraph, the Secretary shall maintain a permanent system of standardized records or accountings of all requests for inspection or disclosure of returns and return information (including the reasons for and dates of such requests) and of returns and return information inspected or disclosed under this section and section 6104(c). Notwithstanding the provisions of section 552a(c) of title 5, United States Code, the Secretary shall not be required to maintain a record or accounting of requests for inspection or disclosure of returns and return information, or of returns and return information inspected or disclosed, under the authority of subsections⁶ (c), (e), (f)(5), (h)(1), (3)(A), or (4), (1)(4), or (8)(A)(ii), (k)(1), (2), (6), (8), or (9), (l)(1), (4)(B), (5), (7), (8), (9), (10), (11), (12), (13), (14), (15), (16), (17), or (18), (m), or (n). The records or accountings required to be maintained under this paragraph shall be available for examination by the Joint Committee on Taxation or the Chief of Staff of such joint committee. Such record or accounting shall also be available for examination by such person or persons as may be, but only to the extent, authorized to make such examination under section 552a(c)(3) of title 5, United States Code.

(B) Report by the Secretary

The Secretary shall, within 90 days after the close of each calendar year, furnish to the Joint Committee on Taxation a report with respect to, or summary of, the records or accountings described in subparagraph (A) in such form and containing such information as such joint committee or the Chief

⁶So in original. Probably should be "subsection".

of Staff of such joint committee may designate. Such report or summary shall not, however, include a record or accounting of any request by the President under subsection (g) for, or the disclosure in response to such request of, any return or return information with respect to any individual who, at the time of such request, was an officer or employee of the executive branch of the Federal Government. Such report or summary, or any part thereof, may be disclosed by such joint committee to such persons and for such purposes as the joint committee may, by record vote of a majority of the members of the joint committee, determine.

(C) Public report on disclosures

The Secretary shall, within 90 days after the close of each calendar year, furnish to the Joint Committee on Taxation for disclosure to the public a report with respect to the records or accountings described in subparagraph (A) which—

(I) provides with respect to each Federal agency, each agency, body, or commission described in subsection (d), (i)(3)(B)(i) or (7)(A)(ii), or (l)(6), and the Government Accountability Office the number of—

(I) requests for disclosure of returns and return information,

(II) instances in which returns and return information were disclosed pursuant to such requests or otherwise,

(III) taxpayers whose returns, or return information with respect to whom, were disclosed pursuant to such requests, and

(ii) describes the general purposes for which such requests were made.⁷

(4) Safeguards

Any Federal agency described in subsection (h)(2), (h)(5), (i)(1), (2), (3), (5), or (7), (j)(1), (2), or (5), (k)(8) or (10), (l)(1), (2), (3), (5), (10), (11), (13), (14), (17), or (22) or (o)(1)(A), the Government Accountability Office, the Congressional Budget Office, or any agency, body, or commission described in subsection (d), (i)(3)(B)(i) or 7(A)(ii),⁸ or (k)(10), (l)(6), (7), (8), (9), (12), (15), or (16), any appropriate State officer (as defined in section 6104(c)), or any other person described in subsection (l)(10), (16), (18), (19), or (20), or any entity described in subsection (l)(21), shall, as a condition for receiving returns or return information—

(A) establish and maintain, to the satisfaction of the Secretary, a permanent system of standardized records with respect to any request, the reason for such request, and the date of such request made by or of it and any disclosure of return or return information made by or to it;

(B) establish and maintain, to the satisfaction of the Secretary, a secure area or place in which such returns or return information shall be stored;

(C) restrict, to the satisfaction of the Secretary, access to the returns or return infor-

mation only to persons whose duties or responsibilities require access and to whom disclosure may be made under the provisions of this title;

(D) provide such other safeguards which the Secretary determines (and which he prescribes in regulations) to be necessary or appropriate to protect the confidentiality of the returns or return information;

(E) furnish a report to the Secretary, at such time and containing such information as the Secretary may prescribe, which describes the procedures established and utilized by such agency, body, or commission, the Government Accountability Office, or the Congressional Budget Office for ensuring the confidentiality of returns and return information required by this paragraph; and

(F) upon completion of use of such returns or return information—

(i) in the case of an agency, body, or commission described in subsection (d), (i)(3)(B)(i), or (l)(6), (7), (8), (9), or (16), any appropriate State officer (as defined in section 6104(c)), or any other person described in subsection (l)(10), (16), (18), (19), or (20) return to the Secretary such returns or return information (along with any copies made therefrom) or make such returns or return information undisclosable in any manner and furnish a written report to the Secretary describing such manner.

(ii) in the case of an agency described in subsections⁶ (h)(2), (h)(5), (i)(1), (2), (3), (5) or (7), (j)(1), (2), or (5), (k)(8) or (10), (l)(1), (2), (3), (5), (10), (11), (12), (13), (14), (15), (17), or (22), or (o)(1)(A) or any entity described in subsection (l)(21)...⁹ the Government Accountability Office, or the Congressional Budget Office, either—

(I) return to the Secretary such returns or return information (along with any copies made therefrom),

(II) otherwise make such returns or return information undisclosable, or

(III) to the extent not so returned or made undisclosable, ensure that the conditions of subparagraphs (A), (B), (C), (D), and (E) of this paragraph continue to be met with respect to such returns or return information, and

(iii) in the case of the Department of Health and Human Services for purposes of subsection (m)(6), destroy all such return information upon completion of its use in providing the notification for which the information was obtained, so as to make such information undisclosable;

except that the conditions of subparagraphs (A), (B), (C), (D), and (E) shall cease to apply with respect to any return or return information if, and to the extent that, such return or return information is disclosed in the course of any judicial or administrative proceeding and made a part of the public record thereof. If the Secretary determines that any such agency, body, or commission, including an agency, an appropriate State officer (as de-

⁷ So in original. The comma probably should be a period.

⁸ So in original. Probably should be "(7)(A)(ii)".

⁹ So in original.

lined in section 6104(c)), or any other person described in subsection (l)(10), (16), (18), (19), or (20) or any entity described in subsection (l)(21),⁹ or the Government Accountability Office or the Congressional Budget Office, has failed to, or does not, meet the requirements of this paragraph, he may, after any proceedings for review established under paragraph (7), take such actions as are necessary to ensure such requirements are met, including refusing to disclose returns or return information to such agency, body, or commission, including an agency, an appropriate State officer (as defined in section 6104(c)), or any other person described in subsection (l)(10), (16), (18), (19), or (20) or any entity described in subsection (l)(21),⁹ or the Government Accountability Office or the Congressional Budget Office, until he determines that such requirements have been or will be met. In the case of any agency which receives any mailing address under paragraph (2), (4), (6), or (7) of subsection (m) and which discloses any such mailing address to any agent or which receives any information under paragraph (6)(A), (10), (12)(B), or (16) of subsection (l) and which discloses any such information to any agent, or any person including an agent described in subsection (l)(10) or (16), this paragraph shall apply to such agency and each such agent or other person (except that, in the case of an agent, or any person including an agent described in subsection (l)(10) or (16), any report to the Secretary or other action with respect to the Secretary shall be made or taken through such agency). For purposes of applying this paragraph in any case to which subsection (m)(6) applies, the term "return information" includes related blood donor records (as defined in section 1141(h)(2) of the Social Security Act).

(5) Report on procedures and safeguards

After the close of each calendar year, the Secretary shall furnish to each committee described in subsection (f)(1) a report which describes the procedures and safeguards established and utilized by such agencies, bodies, or commissions, the Government Accountability Office, and the Congressional Budget Office for ensuring the confidentiality of returns and return information as required by this subsection. Such report shall also describe instances of deficiencies in, and failure to establish or utilize, such procedures.

(6) Audit of procedures and safeguards

(A) Audit by Comptroller General

The Comptroller General may audit the procedures and safeguards established by such agencies, bodies, or commissions and the Congressional Budget Office pursuant to this subsection to determine whether such safeguards and procedures meet the requirements of this subsection and ensure the confidentiality of returns and return information. The Comptroller General shall notify the Secretary before any such audit is conducted.

(B) Records of inspection and reports by the Comptroller General

The Comptroller General shall—

(i) maintain a permanent system of standardized records and accountings of returns and return information inspected by officers and employees of the Government Accountability Office under subsection (i)(8)(A)(ii) and shall, within 90 days after the close of each calendar year, furnish to the Secretary a report with respect to, or summary of, such records or accountings in such form and containing such information as the Secretary may prescribe, and

(ii) furnish an annual report to each committee described in subsection (f) and to the Secretary setting forth his findings with respect to any audit conducted pursuant to subparagraph (A).

The Secretary may disclose to the Joint Committee any report furnished to him under clause (i).

(7) Administrative review

The Secretary shall by regulations prescribe procedures which provide for administrative review of any determination under paragraph (4) that any agency, body, or commission described in subsection (d) has failed to meet the requirements of such paragraph.

(8) State law requirements

(A) Safeguards

Notwithstanding any other provision of this section, no return or return information shall be disclosed after December 31, 1978, to any officer or employee of any State which requires a taxpayer to attach to, or include in, any State tax return a copy of any portion of his Federal return, or information reflected on such Federal return, unless such State adopts provisions of law which protect the confidentiality of the copy of the Federal return (or portion thereof) attached to, or the Federal return information reflected on, such State tax return.

(B) Disclosure of returns or return information in State returns

Nothing in subparagraph (A) shall be construed to prohibit the disclosure by an officer or employee of any State of any copy of any portion of a Federal return or any information on a Federal return which is required to be attached or included in a State return to another officer or employee of such State (or political subdivision of such State) if such disclosure is specifically authorized by State law.

(q) Regulations

The Secretary is authorized to prescribe such other regulations as are necessary to carry out the provisions of this section.

(Aug. 16, 1954, ch. 736, 68A Stat. 753; Pub. L. 88-563, §3(c), Sept. 2, 1964, 78 Stat. 844; Pub. L. 89-44, title VI, §601(a), June 21, 1965, 79 Stat. 153; Pub. L. 89-713, §4(a), Nov. 2, 1966, 80 Stat. 1109; Pub. L. 93-406, title II, §1022(h), Sept. 2, 1974, 88 Stat. 941; Pub. L. 94-202, §8(g), Jan. 2, 1976, 89 Stat. 1139; Pub. L. 94-455, title XII, §1202(a)(1), Oct. 4, 1976, 90 Stat. 1667; Pub. L. 95-210, §5, Dec. 13, 1977, 91 Stat. 1491; Pub. L. 95-600, title V, §503,