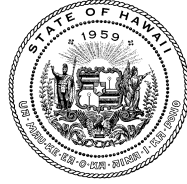


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To: The Honorable Sylvia Luke, Chair
and Members of the House Committee on Finance

Date: Thursday, February 9, 2017

Time: 2:00 P.M.

Place: Conference Room 308, State Capitol

From: Maria E. Zielinski, Director
Department of Taxation

Re: H.B. 1412, Relating to Tax Administration

The Department of Taxation (Department) strongly supports H.B. 1412 and provides the following comments for your consideration.

H.B. 1412 authorizes the Department to require taxpayers to file tax returns by electronic or similar means, subject to a reasonable cause exception. The bill also imposes a fine of two percent of the amount of the tax required to be shown on the return for failure to file by electronic or similar means. H.B. 1412 also lowers the threshold for mandatory electronic payment of taxes to \$40,000 in tax liability per year and clarifies that threshold is to be applied by tax type. The bill becomes effective immediately but applies to tax years beginning after December 31, 2017.

First, the Department believes that the best way to realize the full benefits of the Tax System Modernization (TSM) program is to expand electronic filing and electronic payment of taxes. Tax administration gains efficiency as electronic filing increases and TSM will enhance the Department's ability to accept electronic returns and payments. To achieve these efficiency gains, the Department must increase the proportions of electronic filing and payment. The Department believes this measure will accelerate the expansion of both electronic filing and electronic payment.

Furthermore, through TSM the Department will be able to accept electronic payments at no cost to taxpayers. Taxpayers can simply log into their respective Hawaii Tax Online (HTO) accounts and make electronic payments free of charge. Currently, taxpayers are able to file and pay their general excise; use; and rental motor vehicle, tour vehicle, and car-sharing vehicle surcharge taxes through HTO. Previously, electronic filing of returns for these taxes was free, but electronic payment cost \$1 per transaction. The improved efficiencies and the fact that electronic payment of taxes is now also free further justifies lowering the threshold for mandatory electronic payment of taxes.

Second, the Department notes that electronic payment of taxes, codified at section 231-9.9, Hawaii Revised Statutes, has been mandated for certain taxpayers since the mid-1990s. Since the requirement was first enacted, the threshold to trigger mandatory electronic payment has been \$100,000 in tax liability. Electronic payment has become the most efficient and safest form of payment for both the Department and taxpayers. The Department believes this justifies the lower threshold proposed by this measure.

Third, the Department notes that this measure would make the mandatory electronic payment thresholds consistent across tax types. Currently, the threshold is \$40,000 for withholding taxes but only \$100,000 for all other tax types. By making the thresholds consistent, this measure will simplify tax administration of the mandatory electronic payment system. The Department believes lowering this threshold would not present an undue burden for most affected taxpayers. Most entities with tax liabilities of \$40,000 or more are likely already using some means of electronic funds transfer. For perspective, taxpayers with \$40,000 in GET tax liability are taxpayers that have \$1,000,000 or more in gross revenues.

Finally, both amendments proposed in this measure allow the Department to exercise discretion and grant exceptions for cause. The proposal to require electronic filing does not mandate electronic filing, but merely allows the Department to require electronic filing at its own discretion. The proposal also includes a “reasonable cause” exception to be defined by administrative rules. The Department acknowledges that lack of internet access would qualify as a reasonable cause. During the rulemaking process, the Department will gather public testimony regarding additional exceptions. Additionally, the “good cause” exception to mandatory electronic payment will remain in the law. This will allow the Department to continue to use discretion when mandating electronic payment to avoid any undue hardship to taxpayers.

Thank you for the opportunity to provide comments.

TAX FOUNDATION OF HAWAII

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SUBJECT: ADMINISTRATION, Mandatory Electronic Filing of Tax Returns and Payment of Taxes

BILL NUMBER: SB 851; HB 1412 (Identical)

INTRODUCED BY: SB by TOKUDA; HB by LUKE

EXECUTIVE SUMMARY: Requires electronic filing of tax returns. The statute as drafted provides for a reasonable cause exception only if the department adopts rules, and can be improved if the reasonable cause exception is written into the law.

Requires electronic payment of tax if the annual tax is more than \$40,000 per tax type. This appears to be a reasonable means of cutting the time required for payment processing.

BRIEF SUMMARY: Amends HRS section 231-8.5 to allow the department of taxation to require electronic filing of any tax return, application, report, or other document required under title 14. The department may by rule allow exceptions for reasonable cause.

Provides that a taxpayer who is required to file but doesn't is penalized 2% of the amount of the tax required to be shown on the return.

Amends HRS section 231-9.9 to require electronic payment of any tax when the annual amount of the tax type is more than \$40,000.

Provides that a taxpayer who is required to pay electronically but doesn't is penalized 2% of the amount of the tax required to be shown on the return.

EFFECTIVE DATE: Upon approval provided section 2 shall apply to taxable years beginning after December 31, 2017.

STAFF COMMENTS: That part of this measure relating to electronic filing is similar to the administration measure submitted by the department of taxation TAX-02 (17) (SB 1003 / HB 1137) while the part relating to electronic payment is similar to TAX-03 (17) (SB 1004 / HB 1138).

The first part of the bill requires electronic filing for all or part of the tax base. Some of the tax base, however, might not be comfortable with electronic payment, let alone electronic filing. Electronic filing does seem to be the way of the future, with the potential for speeding up the processing of tax returns and at the same time slashing the error rates associated with scanned or manually entered returns.

There seems to be a reasonable cause exception for the penalties, and we suggest that it be written into the statute, with the department having the ability to interpret that term if it wishes.

As drafted, there is no reasonable cause exception unless the department adopts rules. We suggest language similar to HRS section 231-9.9(c).

"[§231-8.5] **Electronic filing of tax returns.** (a) The department may [allow] require filing by electronic, telephonic, or optical means of any tax return, application, report, or other document required under the provisions of title 14 administered by the department. The date of filing shall be the date the tax return, application, report, or other document is transmitted to the department in a form and manner prescribed by departmental rules adopted pursuant to chapter 91. The department may determine alternative methods for the signing, subscribing, or verifying of a tax return, application, report, or other document that shall have the same validity and consequences as the actual signing by the taxpayer. A filing under this section shall be treated in the same manner as a filing subject to the penalties under section 231-39.

(b) If a person who is required under subsection (a) to file a return electronically department fails to file electronically using an approved method on or before the date prescribed therefor, unless it is shown that the failure is due to reasonable cause and not to neglect, there shall be added to the tax required to be shown on the return a penalty of two per cent of the amount of the tax."

As the bill relates to e-payment, it requires electronic payment if the amount of the tax type is more than \$40,000, as is now provided for payroll withholding. The threshold for other tax types is \$100,000. Electronic payment does seem to be the way of the future, with the potential for slashing the wait times and confusion generated by manual processing of checks attached to returns.

PETER L. FRITZ

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HOUSE OF REPRESENTATIVES THE TWENTY-NINTH LEGISLATURE REGULAR SESSION OF 2017

LATE

COMMITTEE ON FINANCE

Testimony on H.B. 1412
Hearing: February 9, 2017

Relating To Tax Administration

Chair Luke, Vice Chair Cullen and members of the Committee. My name is Peter Fritz. I am offering comments on H.B. 1412 because requiring electronic filing for all taxpayers may discriminate against the disabled, kupuna and low income individuals that may not own a computer. Electronic filing can remove some barriers to disabled taxpayers, but it is likely that it will create new barriers for others.

State and federal disability laws require that state websites be accessible. Unfortunately, state websites are not always accessible and often not in compliance with laws. Because this bill authorizes the Department of Taxation (“Department of Taxation”) to require all to individuals to file tax returns electronically, it may present a hardship for disabled, kupuna and low income taxpayers who may not have the ability, knowledge or equipment to file electronically or those who may use a portal created on the Department’s website to file their return.

Software is available that will allow individuals with disabilities to access the internet. This software relies on websites complying with certain accessibility standards. However, many state websites do not comply with these accessibility standards. I am aware of accessibility problems with the Department’s website that would need to be addressed to remove barriers to the disabled. While many people may use third-party software, not everyone owns a computer nor is everyone able to afford the software. It is likely that the Department will develop a portal that will allow some individuals with simple tax returns to file their returns. H.B. 1412 does not provide much detail about the Department’s plans for electronic filing. However, the Departments recent efforts at electronic filling show that considerable problems can arise for all taxpayers.

The Department may consider it possible to address my concerns by promulgating rules for people, including individuals with disabilities, to request an exemption from electronic filing for reasonable cause. However, this approach may violate the Americans with Disabilities Act (“ADA”). Part of the ADA states that an individual does not have to identify that he/she has a disability unless the individual requires an accommodation. However, if a person must request a reasonable cause exception because the disabled taxpayer cannot use the Department’s website because it does not meet the requirements of the ADA, it is likely that this would violate the ADA because of the Department’s failure to satisfy the law. If the website had been accessible, a request would not be necessary.

A further concern is that calling to request an exemption may be very difficult given the recent call volume of calls and long wait times for the Department’s Taxpayer Services.

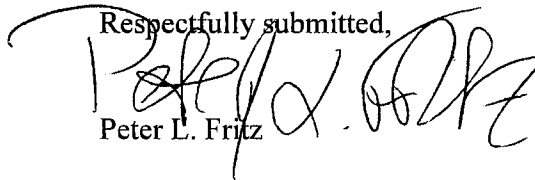
Testimony of Peter L. Fritz
H.B. 1412
February 10, 2017

There are possible solutions and different approaches that may facilitate a transition to electronic filing. For example, the Department may want to create a Task Force for each new type of return for which it wants to mandate electronic filing. The Task Force would be a forum where all individuals could raise concerns about such a mandate.

Alternatively, for income tax returns, the Department could exempt electronic filing for all individuals below the poverty level. A second would be to exempt all tax returns that are filed claiming an exemption for a disability. However, it is recommended that such changes be considered prior to requiring electronic filing, not after mandating electronic filing and after a public forums where individuals can provide feedback to the Department.

Electronic filing can benefit some people. However, implementation should have long lead times to allow problems such as accessibility and lack of equipment to file electronically to function for all individuals.

Thank you for the opportunity to testify.

Respectfully submitted,

Peter L. Fritz