



**STATE OF HAWAII
DEPARTMENT OF TAXATION**

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

Date: Thursday, March 1, 2018

Time: 2:30 P.M.

Place: Conference Room 308, State Capitol

From: Linda Chu Takayama, Director
Department of Taxation

Re: H.B. 1655, Relating to Tax on Sales of Tangible Personal Property

The Department of Taxation (Department) supports H.B. 1655 and offers the following comments for the Committee's consideration.

H.B. 1655, which is effective upon approval, deems a marketplace facilitator who provides customer service, processes payments, and controls the fulfillment process for sales made by a marketplace seller as the seller of tangible personal property (TPP) for purposes of the general excise tax (GET). The bill also subjects marketplace facilitators to the use tax at the wholesale rate for TPP sold to a purchaser in the State. Specifically, the bill amends the definitions of "person" and "representative" in Hawaii Revised Statutes (HRS) section 237-1 and amends the definition of "import" in HRS section 238-1.

The following is a summary of GET and use tax implications of this bill:

- (1) A marketplace facilitator doing business in the State will be subject to GET at the rate of four percent for its own sales as well as sales made on behalf of marketplace sellers for TPP delivered in the State;
- (2) A marketplace seller who is doing business in the State will be subject to GET at the half-percent rate if it sells TPP through a marketplace provider for delivery in the State; and
- (3) If a marketplace seller who is not doing business in the State makes a sale of TPP through a marketplace facilitator for delivery in the State, the marketplace facilitator will be subject to use tax at the rate of half a percent for the import of the TPP (in addition to being subject to GET at the rate of four percent for the sale of the TPP).

This proposal is the most efficient method of imposing and collecting GET on third-party sales made through a marketplace facilitator because instead of having to collect the retail rate of GET from numerous individual marketplace sellers, the Department would only need to collect from one seller—the marketplace facilitator. Additionally, even if a marketplace seller does not have nexus, all sales by a marketplace seller made through a marketplace facilitator who is engaged in business in the State will be subject to GET.

Thank you for the opportunity to provide comments.

TAX FOUNDATION OF HAWAII

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SUBJECT: GENERAL EXCISE, Deny Representative Treatment to Marketplace Sellers

BILL NUMBER: HB 1655

INTRODUCED BY: LUKE

EXECUTIVE SUMMARY: States that a person who sells or assists in the sale of tangible personal property, provides customer service, processes payments, and controls the fulfillment process is a “seller” rather than a “representative,” and therefore has primary liability for the GET. We advise caution because some of the terms in this definition are not tightly defined, are not internally consistent, and could have ramifications beyond the intended targets.

SYNOPSIS: Amends the definition of “person” in section 237-1, HRS, such that the last sentence is changed to, “Any person who sells or assists in the sale of tangible personal property on behalf of another seller by providing customer service, processing payments, and controlling the fulfillment process shall be deemed the seller of the property, when sold, and the seller on whose behalf the sale is made shall be deemed to have made a sale at wholesale pursuant to section 237-4.”

Amends the definition of “representative” in section 237-1, HRS, to exclude a “person who sells or assists in the sale of tangible personal property on behalf of another seller and who provides customer service, processes payments, and controls the fulfillment process.”

EFFECTIVE DATE: Upon approval.

STAFF COMMENTS: This bill appears to be an effort to target “marketplace sellers,” namely those sellers who provide a framework for smaller sellers, most of whom are likely out of state, to sell into Hawaii (among other places). We understand that the marketplace sellers are presently taking the position that even if the marketplace seller has nexus with and must pay tax to Hawaii, it has no responsibility to collect and remit taxes when it is merely representing another seller that otherwise has no nexus with Hawaii.

The United States Constitution has been interpreted as providing two limits on the states’ powers to tax. These limits come from at least two places: first, the Due Process Clause, requiring a person to have “minimum contacts” with a state before that state is allowed to exercise police powers, including the power to tax, against that person; and second, the Commerce Clause, where the Supreme Court held in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977), that if the Congress does not otherwise define the threshold for taxability, state tax may not be imposed upon a person unless there is “substantial nexus” with that person. Substantial nexus is more than minimum contacts, and *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992), appears to stand for the proposition that some physical presence is needed to establish substantial nexus.

In Hawaii, section 237-22(a) HRS, states that there shall be excepted or deducted from the values, gross proceeds of sales, or gross income so much thereof as, under the Constitution and laws of the United States, the state is prohibited from taxing, but only so long as and only to the extent that the state is so prohibited. *In re Grayco Land Escrow, Ltd.*, 57 Haw. 436, 559 P.2d 264, *cert. denied*, 433 U.S. 910 (1977), established that Hawaii already extends its general excise and use taxes to reach the limit of the Constitution (“Thus, in plain and unmistakable language, the statute evidences the intention of the legislature to tax every form of business, subject to the taxing jurisdiction, not specifically exempted from its provisions.”).

For marketplace sales, *Scripto, Inc. v. Carson*, 362 U.S. 207 (1960), and *Tyler Pipe Industries, Inc. v. Washington State Department of Revenue*, 483 U.S. 232 (1987), hold that substantial nexus can be established through an independently contracted sales agent who acts in a state on behalf of another. Thus, whether or not “economic nexus” is ultimately found to be constitutional, nexus can and should be attributed from a marketplace provider under current law.

Obviously, it is easier from a revenue administration perspective to shift the responsibility for collecting and remitting tax to a marketplace provider with nexus in the State, as opposed to trying to chase down a myriad of small and large sellers scattered throughout the nation, and that is what this bill is trying to accomplish.

Technically, the bill could be tightened up.

- The bill is now internally inconsistent because the definition of a marketplace provider in the definition of “seller” is slightly different from the definition of a provider that is excluded from the definition of “representative.” They should be made consistent.
- “Providing customer service, processing payments, and controlling the fulfillment process” strike us as vague terminology. The Committee should consider tightening up the terms or allowing the Department of Taxation regulatory authority to do so.

Digested 3/1/2018