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

Date: Thursday, February 1, 2018
Time: 2:00 P.M.
Place: Conference Room 308, State Capitol

From: Linda Chu Takayama, Director
Department of Taxation

Re: H.B. 2416, Relating to Tax on Intangible Property

The Department of Taxation (Department) supports H.B. 2416 and offers the following comments for the Committee's consideration.

H.B. 2416 clarifies that for purposes of the general excise tax (GET), intangible property is sourced to the location where it is used. Specifically, the bill adds an exemption to GET for intangible property used outside the State and imposes the use tax on intangible property acquired from an unlicensed seller that is imported or used in the State. The bill is effective on July 1, 2018.

First, the Department notes that this bill is consistent with its position that intangible property is sourced to the location where it is used. For example, if a taxpayer creates custom software and licenses it to a customer for use in the State, the taxpayer will be subject to GET on the income it receives. If, on the other hand, the customer will be using the software outside the State, the income that the taxpayer receives will be exempt from GET. The Department further notes that this sourcing rule is consistent with the sourcing of income from services, which is sourced to where the services are used and consumed pursuant to Hawaii Revised Statutes section 237-29.53.

Second, the Department notes that this bill will require form and computer system changes and therefore requests that the bill be amended to apply to tax years beginning after December 31, 2018.

Thank you for the opportunity to provide comments.

TAX FOUNDATION OF HAWAII

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SUBJECT: GENERAL EXCISE, USE, Impose Tax on Intangible Property

BILL NUMBER: HB 2416

INTRODUCED BY: LUKE

EXECUTIVE SUMMARY: Imposes GET and Use Tax on intangible property used in the State, while exempting revenues from using intangible property outside the State. We urge caution on this bill because of potentially far-reaching impact.

SYNOPSIS: Adds a new section to chapter 237, HRS, allowing an exemption for intangible property used out of State. Allows the purchaser to certify the out-of-state use (similar to the current G-61 export certificate).

Adds a new section to chapter 238, HRS, imposing use tax on imported tangible property at 4%.

Makes conforming amendments.

EFFECTIVE DATE: July 1, 2018

STAFF COMMENTS: This bill has far-reaching implications and needs to be thought through carefully. It could apply, for example, if a Hawaii resident bought stocks or bonds, because the transfer of ownership of the stocks or bonds could be seen as importation of the stocks or bonds, which are intangible property. Income from such instruments is explicitly exempt from the GET under HRS section 237-3(b), but that exemption wouldn't be worth much if the value of the instrument is immediately taxed under this bill.

Digested 1/30/2018