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To: The Honorable Donovan M. Dela Cruz, Chair
and Members of the Senate Committee on Ways and Means

Date: Tuesday, February 6, 2018
Time: 10:00 A.M.
Place: Conference Room 211, State Capitol

From: Linda Chu Takayama, Director
Department of Taxation

Re: S.B. 2968, Relating to Taxation

The Department of Taxation (Department) offers the following comments on S.B. 2968 for the Committee's consideration.

S.B. 2968 requires nonresident owners of real property in the State to enter into an agreement with a third party for the collection of rent on behalf of the owner. The bill also requires persons who enter into rental collection agreements with a nonresident owner to deduct and withhold from the rent the amount of general excise tax (GET) payable by the owner, but makes an exception for taxpayer-owners exempt under Hawaii Revised Statutes (HRS) section 237-23. The bill is effective on July 1, 2018.

First, the Department notes that the amendment to HRS section 237-18 would require the person collecting rent on behalf of a property owner to withhold from the rent the tax owed by the owner, but does not obligate that person to remit the tax to the Department. Accordingly, the Department recommends adding language that imposes personal liability on the person withholding the tax.

Second, if the person collecting the rent will be required to report and pay taxes on behalf of the owner, a provision should be added specifying that the GET should be reported and paid on a separate GET account. GET should not be reported and paid on the account of the person collecting the rent.

Third, the Department notes that the bill exempts property owners who are exempt under

HRS section 237-23, from mandatory collection of rent by a third party, but all property owners who are listed in HRS section 237-23 are not necessarily exempt from GET for rental income. If the intent of this bill is for mandatory collection to apply to all nonresident owners, the Department suggests removing this provision.

Based on the foregoing, the Department recommends amending subsection (i) as follows:


Every person authorized by the nonresident owner of real property located within this State to collect rent for that property on behalf of the owner, pursuant to a rental collection agreement under section 237-30.5(e), shall ~~[deduct]~~:


- (1) Deduct and withhold from the rents collected and payable to the owner of the real property the amount of the tax imposed by this chapter and payable by the owner; ~~[provided that this subsection shall not apply with respect to rents collected and payable to an owner of real property who is exempted by section 237-23 from taxation under this chapter.]~~
- (2) Obtain a license under this chapter for purposes of reporting and paying taxes on behalf of the owner of real property; and
- (3) Be personally liable for the taxes withheld under this section if taxes are withheld, but not reported or paid, together with penalties and interest as provided by law.


Finally, the Department requests that the bill is amended to apply to tax years beginning after December 31, 2018 to allow the Department sufficient time to make the necessary form and computer system changes.

Thank you for the opportunity to provide comments.



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February 6, 2018

The Honorable Donovan Dela Cruz, Chair

Senate Committee on Ways and Means
State Capitol, Room 211
Honolulu, Hawaii 96813

RE: Senate Bill 2884 Relating to Taxation

HEARING: Tuesday, February 6, 2018, at 10:00 a.m. in Room 211

Aloha Chair Dela Cruz, Vice Chair Keith-Agaran and Members of the Committee,

I am Ken Hiraki, Director of Government Affairs, here to testify on behalf of the Hawai'i Association of REALTORS® ("HAR"), the voice of real estate in Hawai'i, and its close to 9,500 members. HAR **provides comments on Senate Bill 2968**, which requires a person authorized to collect rent on behalf of a nonresident owner of real property located in the State to withhold the general excise tax due on rents collected. Requires nonresident owners who receive rents attributable to real property located in the State to enter into a rent collection agreement.

The requirement that real estate licensees be responsible for withholding taxes from rent for out of state property owners is contrary to the current requirement in the tax code, which provides that the owner of the property, not the real estate licensee is responsible for paying the General Excise Tax. HAR would further note that not all of our members collect and remit taxes on behalf of their clients, and this is negotiable between the parties.

While HAR understands the importance of ensuring that the State is able to collect the appropriate amount of taxes owed by all property owners. HAR believes that it should be the owners responsibility and not a real estate licensee who property manages for their client.

HAR would also note that this measure is unclear as to the disposition of the taxes, once the tax is withheld.

Mahalo for the opportunity to testify on this measure.





The Senate
The Twenty-Ninth Legislature
Regular Session of 2018

To: Senator Dela Cruz, Chair

Senator Keith-Agaran, Vice-Chair

Date: February 6, 2018

Time: 10:00 a.m.

Place: Conference Room 211

RE: Senate Bill 2999, Relating to Taxation

Chair Dela Cruz and Members of the Committee:

RBOAA must **OPPOSE** the bill.

This Bill **REQUIRES** nonresident owners of real property in the State of Hawaii who receive rental income attributable to that property to enter into a rental collection agreement.

Further, it requires in the collection of the rent that general excise tax will be withheld from the rents.

This Bill is a violation of the Privileges and Immunities Clause that provides “Citizens of each State shall be entitled to all Privileges and Immunities of Citizens in the several States.” **The United States Supreme Court has found that “one of the privileges which the Clause guarantees to citizens of State A is that of doing business in State B on terms of substantial equality with the citizens of that State.”**

The Privileges and Immunities Clause forbids any State from discriminating against citizens of Other States.

The United States Supreme Court held in 1869 that:

It was undoubtedly the object of this clause in question to place the citizens of each State upon the same footing with citizens of other States, so far as the advantages resulting from citizenship in those States are concerned. It relieves

them from the disabilities of alienage in other States, it inhibits **discriminating legislation against them by other States** ...it insures to them in other States the same freedom possessed by the citizens of those States in the acquisition and enjoyment of property, and in the pursuit of happiness, and it secures to them in other States the equal protection of their laws. (emphasis added)

The Equal Protection Clause of the United States Constitution provides that “no State shall ... deny to any person within its jurisdiction the equal protection of the laws.”

The Hawaii State Constitution, Article I, Bill of Rights provides these protections to people:

Due Process and Equal Protection:

No person shall be deprived of life, liberty or property without due process of law, nor be denied the equal protection of the laws, or be denied the enjoyment of the person's civil right or be discriminated against.

Right to Privacy:

The right of the people to privacy is recognized and shall not be infringed without the showing of a compelling State interest. The legislature shall take affirmative steps to implement this right.

Search, Seizures and Invasion of Privacy:

The right of the people to be secure in their persons, houses, papers and effects against unreasonable searches, seizures and invasions of privacy shall not be violated.

Rights of Citizens:

No citizen shall be disenfranchised or deprived of the rights and privileges secured to the citizens.

As noted above, every protection that Hawaii through its Constitution provides to its people, must also provide the same to others of other states pursuant to the United States Constitution Privileges and Immunities Clause and Equal Protection Clause.

We believe this Bill violates the United State Constitutional protections as well as the State of Hawaii Constitution.



The effect of this Bill would result in an impermissible seizure of business of nonresident property owners. It deprive nonresident property owners of the same rights granted to resident property owners and is therefore discriminatory.

Resident property owners are required to apply for a GET registration, a TAT (if renting for less than 180 days). They collect their own rents, pay their own taxes, file their own tax documents. They have control over all financial aspects of their business and maintain their privacy and have a direct confidential relationship with the Department of Taxation.

Nonresident property owners are required to apply for a GET registration, a TAT (if renting for less than 180 days). But they would be required to enter into a rent collection contract, someone else would collect rent, deduct taxes and presumably pay the taxes - although the Bill is silent on this point. They are deprived of controlling the financial aspects of their own business which is essence is a seizure, their privacy is intruded upon by a forced contract with a third party, they are deprived of a direct confidential relationship with the Department of Taxation.

We, therefore, respectfully request that this Bill be deferred.

Thank you for the opportunity to testify on this measure.

Sincerely,

Neal Halstead
President,
Rental by Owner Awareness Association

Rental By Owner Awareness Association (RBOAA) is a Hawaii non-profit corporation founded in 2011, with over 1000 members. Our mission is to provide Hawaii vacation-rental property owners with information to help them comply with the applicable State and County regulations, support the Hawaii economy by offering visitors choice in accommodation, and advocate for the rights of Hawaii vacation property owners. RBOAA members provide transient vacation rentals in full compliance with existing tax and County regulations. RBOAA fully supports enforcement of existing regulations.

TAX FOUNDATION OF HAWAII

126 Queen Street, Suite 304

Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: GENERAL EXCISE, Withhold Tax on Rents Paid to Nonresident Owners

BILL NUMBER: SB 2968

INTRODUCED BY: DELA CRUZ, INOUYE, S. Chang, K. Kahele

EXECUTIVE SUMMARY: Requires a person authorized to collect rent on behalf of the nonresident owner of real property located in the State to withhold the general excise tax due on rents collected. Requires nonresident owners who receive rents attributable to real property located in the State to enter into a rent collection agreement.

SYNOPSIS: Amends section 237-18, HRS, to add a new subsection providing that every person authorized by the nonresident owner of real property located within this State to collect rent for that property on behalf of the owner, pursuant to a rental collection agreement under section 237-30.5(e), shall deduct and withhold from the rents collected and payable to the owner of the real property the amount of the tax imposed by this chapter and payable by the owner; provided that this subsection shall not apply with respect to rents collected and payable to an owner of real property who is exempted by section 237-23 from taxation under this chapter.

Amends section 237-30.5, HRS, to require any nonresident receiving rent from real property in this State to enter into a rental collection agreement contemplated by this measure.

EFFECTIVE DATE: July 1, 2018.

STAFF COMMENTS: This measure attempts to tackle the pervasive problem of nonresident real property owners who either don't know or don't care that Hawaii imposes tax on rental income (most states' sales taxes do not apply to rental income).

Here are some technical comments for consideration:

1. Section 237-18, HRS, although having a broad title, is now commonly understood to contain "income splitting" provisions where the parties described are to pay tax on their respective shares of income from a transaction. This provision probably would be easier to find if it is made a standalone section with an appropriately descriptive title. Alternatively, the language proposed to be added to section 237-18 could be added to section 237-30.5.
2. For rental agreements where the term of the rental is less than 180 consecutive days, the withholding agent should be withholding transient accommodations tax as well.
3. It is questionable why tax-exempt (HRS section 237-23) organizations are exempted from this withholding requirement because the exemption in section 237-23 generally *does not* apply to rents received by a tax-exempt organization.
4. A definition of nonresident is needed. We suggest using the definition of "nonresident person" from HRS section 235-68.

Re: SB 2968

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Digested 2/3/2018

Coalition for Equal Taxation

Chair Dela Cruz and Committee Members:

On behalf of the Coalition for Equal Taxation, we OPPOSE SB2968 and request that the Bill be deferred.

This Bill provides for carving out a separate system of rent collection that is unique to nonresident owners of property in the State of Hawaii. It requires a contract be entered into on the part of a nonresident owner who must have a third party collect rent and withhold taxes.

We ask the Committee to consider this fundamental criteria of law making. Does it conform to the State of Hawaii Constitution? If not, it will be per se invalid and unconstitutional.

Does this Bill conform to the United States Constitution? If not, it will be per se invalid and unconstitutional.

This Bill fails in treating out-of-state persons the same as in-state persons and therefore is discriminatory.

SB2968 could be challenged on the grounds that the measure violates the rights of property owners who are non-Hawaii residents under Article IV, Section 2 ("Privileges and Immunities Clause"), the Equal Protection Clause of the Fourteenth Amendment ("Equal Protection Clause" and Article I, Section 8 ("Commerce Clause") of the Constitution of the United States.

Privileges and Immunities Clause provides that "one of the privileges which the Clause guarantees to citizens of State A is that of doing business in State B on terms of substantial *equality* with the citizens of that State." Further it "insures to them in other States the same freedom possessed by the citizens of those States in the acquisition and enjoyment of property, and in the pursuit of happiness, "**and it secures to them in other States the equal protection of their laws.**" (*emphasis added.*)

Equal Protection Clause provides that "**no State shall ... deny to any person within its jurisdiction the equal protection of the laws.**" (*emphasis added.*)

Commerce Clause provides "Congress expressly "shall have power to regulate commerce ...among the several States ..." It has been judicially established that the Commerce Clause is not only a "positive" grant of power to Congress, but it is also a "negative" constraint upon the States.

Therefore, **the Commerce Clause prohibits a state from passing legislation that improperly burdens or discriminates against interstate commerce.**

The Supreme Court has outlined a two-tiered approach to analyzing state regulations under the Commerce Clause: The first step is analyzing any law subject to judicial scrutiny under the negative Commerce Clause is to determine whether it "*regulates evenhandedly* with only "incidental" effects on interstate commerce, or **discriminates against interstate commerce.**" As we use the term here, "**discrimination" simply means differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter. If a restriction on commerce is discriminatory, it is virtually per se invalid.**" (*emphasis added.*) Barber v. State of Hawai'i, 42 F.3d 1185, 1194 (9th Cir. 1994)

SB2968 meets the definition of "discrimination" as defined by the Court. This Bill legislates differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter, thereby, rendering the measure "virtually per se invalid."

Further, the premise of this Bill is an assumption that nonresident owners are less compliance or perhaps less honest than resident owners of property. It should be pointed out that resident owners of rental property have the same ability to wrongfully withhold payment of taxes as do nonresident owners. Bills written with a presumption of a guilt on the part of a class or category, i.e. nonresidents, is prejudicial and discriminatory.

State of Hawaii Constitution: Article I, Section 6: Right to Privacy. "The right of the people to privacy is recognized and shall not be infringed upon..." "The Legislature shall take affirmative steps to implement the right of the people to privacy."

The Legislature is required to actively protect privacy of individuals. This Bill fails to provide that protection.

State of Hawaii Constitution: Article I, Section 7: Searches, Seizures and Invasion of Privacy. Article I, Section 7: "The right of the people to be secure in their persons, houses, papers, and effects against unreasonable searches, seizures and invasions of privacy shall not be violated."

This Bill subjects nonresident property owners to their business operations being seized by a third party and thus is a violation of Article I, Section 7.

As the United States Constitution makes clear, States may not treat, legislate, create laws, or tax nonresidents any differently than they do their own citizens. To do otherwise, is a violation of the 14th Amendment.

We respectfully urge this Committee to evaluate the substantial Federal and State constitutional challenges that result in discrimination and please defer this Bill.

John Chang
Coalition of Equal Taxation