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

Date: Monday, February 11, 2019

Time: 10:00 A.M.

Place: Conference Room 211, State Capitol

From: Linda Chu Takayama, Director
Department of Taxation

Re: S.B. 1268, Relating to Tax Reporting

The Department of Taxation (Department) strongly supports S.B. 1268, an Administration measure, and offers the following comments for the Committee's consideration.

S.B. 1268 amends Hawaii Revised Statutes (HRS) sections 237-30.5 and 237D-8.5 to revise the way persons who collect rents or gross rental proceeds on behalf of owners of real property or operators of transient accommodations report such collection to the Department.

Under current law, persons collecting rent or gross rental proceeds on behalf of others must report information identifying each owner or operator on whose behalf they collect. However, they are not required to report the total amount of money collected on behalf of each owner or operator. Current law also requires the person to provide the owner or operator a copy of a tax liability notice. Under current law, there is no penalty for noncompliance with the reporting requirements.

S.B. 1268 would require persons who collect rents or gross rental proceeds on behalf of others to report to the Department the total amount of rent or gross rental proceeds collected on behalf of the owner or operator during the previous calendar year. The bill would maintain reporting of the identifying information required under current law as well as the requirement to provide a tax liability notice to the owner or operator. Finally, S.B. 1268 imposes a penalty for noncompliance with the reporting requirements. The penalty is \$500 per violation per month.

The Department believes this bill will improve compliance in two ways. First, the increased reporting requirements will lead to increased voluntary compliance. If taxpayers know that the Department has information detailing how much rent they received, they will be more likely to complete returns and pay their taxes voluntarily. This will lead to both better collections and a reduced administrative burden.

Second, reporting of the total amount of rent and gross rental proceeds collected will provide an independent measure of a taxpayers' receipts. This will simplify and improve the accuracy of any eventual audit of the taxpayer.

Thank you for the opportunity to provide testimony in support of this measure.

TAX FOUNDATION OF HAWAII

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SUBJECT: GENERAL EXCISE, TRANSIENT ACCOMMODATIONS, Reporting Rental Activity

BILL NUMBER: HB 1042; SB 1268 (Identical)

INTRODUCED BY: HB by SAIKI by request; SB by KOUCHI by request

EXECUTIVE SUMMARY: Updates the manner in which persons authorized to collect rent for others provide information to the Department of Taxation and establishes penalties for noncompliance.

SYNOPSIS: Rewrites section 237-30.5 and 237D-8.5, HRS, that now provides for notice to the property managers' clients. Imposes penalties of \$500 a month for noncompliance unless it is shown that the failure was due to reasonable cause and not to neglect.

EFFECTIVE DATE: Upon approval.

STAFF COMMENTS: This is an Administration bill sponsored by the Department of Taxation and designated TAX-02 (19).

Under current law, property managers and similar businesses who collect rent for another are supposed to provide their clients with specific notices and are supposed to provide the Department specific information. However, since current law does not provide penalties for failure to do so, compliance with this provision appears to be spotty at best.

This bill attempts to address this problem.

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February 11, 2019

TO: Senate Committee on Ways and Means
The Honorable Donovan M. Dela Cruz, Chair
The Honorable Gilbert S.C. Keith-Agaran, Vice Chair

FROM: Amanda Pedigo, Vice President, Government and Corporate Affairs
Expedia, Inc.

RE: SB1268 Relating to Tax Reporting - OPPOSE

Dear Chairman Dela Cruz, Vice Chairman Keith-Agaran and distinguished members of the Senate Committee on Ways and Means,

I represent the Expedia Group, a family of global leading travel technology platforms that empower travel and tourism throughout Hawaii. Vacation rental platforms HomeAway and VRBO are proud members of the Expedia Group family.

For nearly three decades, HomeAway platforms have been the leaders in offering unique, family-focused vacation experiences for traveling families and groups. We take immense pride in our long-standing commitment to our local homeowners, their small business partners, the communities they serve and the millions of families that have used vacation rentals to experience Hawaii in a unique and special way.

While Expedia recognizes and supports the State's right to collect all taxes owed, it cannot support SB1268

Although SB1268 may not have intended to, it includes provisions that violate state and federal law and that will not withstand judicial scrutiny. It also includes provisions that are simply bad policy that will harm the state's economy and drive some vacation rental property owners "underground" to avoid onerous regulation.

HomeAway and other hosting platforms have filed successful lawsuits in other jurisdictions against similar laws. To avoid a potential legal challenge, Expedia urges the Legislature to join with the administration and industry to adopt a workable regulation that does not violate state and federal law.

Stored Communications Act – Privacy of Personal Information

Federal law requires HomeAway to keep confidential the personal information of homeowners and travelers who use their websites. Specifically, the Stored Communications Act (SCA), prescribes the kinds of legal process that a government must follow before it can obtain and HomeAway can disclose customer information to the governmental entity.

The SCA “was enacted because the advent of the Internet presented a host of potential privacy breaches” *Quon v. Arch Wireless Operating Co.*, 529 F.3d 892, 900 (9th Cir. 2008), *rev’d on other grounds*, *City of Ontario v. Quon*, 560 U.S. 746 (2010) (citation omitted)). To prevent such breaches, the SCA prescribes the form of legal process the government must use to obtain user information from online providers that meet the definitions of an “electronic communications service” (“ECS”) or “remote computing service” (“RCS”). In simple terms, an ECS provides communication services to users and stores communications temporarily to transmit them, while an RCS stores and processes user information for longer periods. *See* 18 U.S.C. §§ 2510(16), 2711(2) (definitions). HomeAway is both an ECS and RCS provider. *See HomeAway.com, Inc. v. City of Portland*, No. 3:17-CV-00091-MO, 2017 WL 2213154, at *1 (D. Or. May 11, 2017). It is an ECS provider for communications between listing owners and travelers through its secured network, and an RCS because it stores and processes information from users, such as information provided for listing properties.

Under Section 2702(a)(3), an RCS or ECS provider “shall not knowingly divulge a record or other information pertaining to a subscriber to or customer of such service (not including the contents of communications covered by paragraph (1) or (2)) to any governmental entity.” The statute contains exceptions, which, in relevant part, permit disclosure “as otherwise authorized in section 2703.” *Id.* § 2702(c)(1). Section 2703 permits the disclosure of basic information, such as a customer’s name and address, source of payment, and other discrete categories, if the government “uses an administrative subpoena authorized by a Federal or State statute or a Federal or State grand jury or trial subpoena.” *Id.* § 2703(c)(2). For all other information, the government must obtain a search warrant or a court order that requires it to provide notice to the customer and establish “specific and articulable facts showing that there are reasonable grounds to believe that ... the records or other information sought, are relevant and material to an ongoing criminal investigation.” *See* 18 U.S.C. § 2703(d).

Put in plain language, to obtain “basic subscriber information,” which, as defined by the SCA is information like a customer name and contact information, the governmental entity must use a subpoena. It cannot simply pass a law that requires a platform to hand over that information without any legal process. SB1268 seeks personal information far beyond “basic subscriber information”—and without *any* form of legal process.

The SCA therefore prohibits HomeAway from disclosing the information the SB1268 seeks without a subpoena or other process, notwithstanding a local law that requires disclosure. In fact, a federal court stopped enforcement of a similar provision in the Portland City Code, which would have required HomeAway and other providers to disclose to the city’s taxing authority, upon request, “all physical addresses of transient lodging occupancy locations within Portland city limits and the related contact information, including the name and mailing address of the general manager, agent, owner, host or other responsible person for the location.” *HomeAway.com, Inc. v. City of Portland*, 2017 WL 2213154, at *4 (noting the court had during oral argument enjoined enforcement of Portland City Code Section 6.04.040(B)). The Court held that “the provision is likely preempted by the [SCA].” *Id.* at *1. The City of Portland yielded after that ruling and has not tried to enforce its law.

HomeAway’s concerns are not just theoretical: the SCA allows individuals whose information is provided to a governmental entity in violation of the statute’s requirements to sue for damages.

18 U.S.C. § 2707. Intentional violations can be punished by both statutory and punitive damages and attorneys' fee awards.

In short, SB1268 violates the process established by the SCA.

U.S. and Hawai'i Constitutions - Protected Privacy Interests

SB1268 also violates the provisions of the U.S. and Hawai'i Constitutions

The Fourth Amendment extends to electronic communications and protects against government searches. The U.S. Supreme Court has warned against allowing technological advances to “erode the privacy guaranteed by the Fourth Amendment.” *Kyllo v. United States*, 533 U.S. 27, 34 (2001). The Fourth Amendment’s protection of “papers” covers business records. *Hale v. Henkel*, 201 U.S. 43, 76-77 (1906); *see also Marshall v. Barlow's Inc.*, 436 U.S. 307, 311 (1978) (Fourth Amendment protects business property no less than residential property).

As such, hosting platforms like HomeAway have a protected privacy interest in the information sought under SB1268. This is true even though that information pertains to the owners and operators. *City of Los Angeles v. Patel*, 135 S.Ct. 2443 (2015) (hotel owners had reasonable expectation of privacy as to information on guests' names and addresses, and details about guests' vehicles).

This rule was recently affirmed in New York, where a federal court stopped enforcement of a New York City ordinance like SB1268 that would require hosting platforms on a monthly basis to turn over data regarding customers who use their websites to advertise vacation rentals, including customer name, property address, and information about the level of rental activity each month. *Airbnb, Inc. v. City of New York*, (S.D. N.Y. Jan. 3, 2019), 18 Civ. 7712 (PAE) and 18 Civ. 7742 (PAE). The court had “little difficulty” holding that the ordinance “is a search or seizure within the Fourth Amendment.” In so holding, the court discussed an expansive line of authority that “ma[de] clear that the compelled production from home-sharing platforms of user records is an event that implicates the Fourth Amendment.” *See Oklahoma Press Pub. Co. v. Walling*, 327 U.S. 186 (1946) (holding that the Fourth Amendment applied to administrative subpoenas *duces tecum* issued in an investigation into violations of the Fair Labor Standards Act); *United States v. Morton Salt Co.*, 338 U.S. 632 (1950) (recognizing that the protection of the Fourth Amendment “is not confined literally to searches and seizures as such, but extends as well to the orderly taking under compulsion of process”); *See v. City of Seattle*, 387 U.S. 541 (1967) (compulsion of corporate books and records are subject to the Fourth Amendment); *McLane Co., Inc. v. E.E.O.C.*, 137 S.Ct. 1159 (2017) (compulsion of records implicates “the privacy interests protected by the Fourth Amendment”).

The requirements sought to be imposed under SB1268 violate HomeAway's constitutionally protected privacy interests. The protection's central command is that official searches and seizures be reasonable. *Riley v. California*, 134 S.Ct. 2473, 2482 (2014). In the context of civil cases, federal courts require “special needs” to validate suspicion-less searches. *New Jersey v. T.L.O.*, 469 U.S. 325 (1985). The government must show that it is impracticable or unreasonable to require it to demonstrate individualized suspicion to a neutral decision-maker before conducting the search. *Id.*

The effect of SB1268 is to allow sweeping suspicion-less searches without a showing that it is impracticable or unreasonable to demonstrate individualized suspicion to a neutral decision-maker. Such an invasion violates both the U.S. and Hawai`i Constitutions.

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The vacation rental industry plays a vital role in Hawaii's economy. We recognize and support the State's right to collect all taxes owed and would like to work with the state and local governments to modernize the regulations of this important economic sector.

Thank you for the opportunity to share this testimony.

