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**TESTIMONY OF
GARY S. SUGANUMA, DIRECTOR OF TAXATION**

TESTIMONY ON THE FOLLOWING MEASURE:

H.B. No. 1471, Relating to Telework

BEFORE THE:

House Committee on Labor & Government Operations

DATE: Tuesday, February 14, 2023

TIME: 9:30 a.m.

LOCATION: State Capitol, Room 309

Chair Matayoshi, Vice-Chair Garrett, and Members of the Committee:

The Department of Taxation ("Department") offers the following comments regarding H.B. 1471 for your consideration.

H.B. 1471 amends the definition of "nonresidents" in section 235-4, Hawaii Revised Statutes (HRS), by establishing a presumption of nexus for nonresidents who were providing services in the state immediately prior to the March 4, 2020 Governor's proclamation related to the Covid-19 Emergency, and are now performing the same services from a location outside of the State due to a "pandemic-related circumstance." Definitions for "Hawaii coronavirus disease 2019 state of emergency" and "pandemic-related circumstances" are added to section 235-4.2, HRS. Nonresidents for whom the presumption of nexus will apply will have their total income derived from services previously provided within the State and now performed remotely subject to Hawaii's income tax. The bill is effective upon approval and applies to any taxable years beginning after December 31, 2022.

First, the Department recommends that the language in section 2 of the bill be amended to combine (A) and (B) to avoid any ambiguity and for technical and style purposes.

Second, the Department notes that the bill will only apply to a small, specific

group of individuals and that enforcement and verification for this group may be difficult.

Finally, the Department notes that due to the number of bills with tax law changes that have been introduced this year, the Department may not have the resources to implement all measures passed this session in time for tax year 2023. The Department will continue to monitor the status of proposed legislation and will advise whether some changes will require a later effective date.

Thank you for the opportunity to provide comments on this measure.

TAX FOUNDATION OF HAWAII

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SUBJECT: INCOME, Nexus Presumption for Teleworkers

BILL NUMBER: HB 1471, SB 1116

INTRODUCED BY: HB by SAIKI by request; SB by KEITH-AGARAN, KANUHA, MCKELVEY, RHOADS, Dela Cruz, Kidani, San Buenaventura

EXECUTIVE SUMMARY: Clarifies that there is a presumption of a nexus for certain nonresident employees who telework. Amends the income tax law to apply to the total income of certain nonresident employees who telework.

SYNOPSIS: Amends section 235-4(b), HRS, to state that although a nonresident is taxed on Hawaii source income, a nonresident who immediately prior to the COVID-19 pandemic was performing services in Hawaii and now is performing those same services remotely from outside the State due to a pandemic-related circumstance, is taxed on all income from the services performed outside the State.

Amends section 235-4.2, HRS, to add a presumption that a nonresident as described above has nexus with the State.

EFFECTIVE DATE: Taxable years beginning after December 31, 2022.

STAFF COMMENTS: While the tax authorities might be frustrated that some people who used to be physically working in Hawaii now aren't because of the pandemic and they think tax collections have fallen as a result, the solution put forth by this bill may be problematic.

First, the concept of nexus is from federal law, not state law. It is a requirement under the federal Due Process and Commerce Clauses that a person have certain minimum contacts with a State before that State is allowed to exercise taxing jurisdiction over that person. Thus, the presumption of nexus in this bill, if enacted, might have no legal effect.

Second, there may be other constitutional problems that may arise depending on how it is interpreted. Suppose, for example, Taxpayer T lives in Virginia and, before the pandemic, was performing physical services in Virginia, California, and Hawaii. Suppose 40% of T's pay is attributable to work in Virginia, and 30% each to California and Hawaii. COVID-19 hits, and T stops flying to Hawaii and California but does work to benefit customers there remotely. If the bill's enactment tasks the Department of Taxation with going after 30% of T's income, the same as before, the Department may have to fight with Virginia, who will say that T lives there (which is true) and doesn't have to cede any taxing jurisdiction to Hawaii. If the bill tasks the Department with going after 100% of T's income, California may join the fight as well, and Hawaii may be seen as overreaching.

Digested: 2/12/2023