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TESTIMONY OF
GARY S. SUGANUMA, DIRECTOR OF TAXATION

TESTIMONY ON THE FOLLOWING MEASURE:
S.B. No. 313, Relating to a Wealth Asset Tax

BEFORE THE:
Senate Committee on Judiciary

DATE: Thursday, January 30, 2025
TIME: 9:15 a.m.
LOCATION: State Capitol, Room 016

Chair Rhoads, Vice-Chair Gabbard, and Members of the Committee:

The Department of Taxation (DOTAX) offers the following comments regarding S.B. 313 for your consideration.

Section 1 of S.B. 313 creates a new chapter in Hawaii Revised Statutes (HRS) establishing a wealth asset tax equal to one percent of an individual taxpayer's statewide net worth in excess of $20,000,000. The bill is effective upon approval and applies to taxable years beginning after December 31, 2025.

Section 2 of S.B. 313 directs DOTAX to submit proposed legislation suggesting the types of debts to be considered in determining net worth, methods to be used for valuation of assets, time periods for which valuation of assets shall occur, methods for allocation and apportionment, withholding requirements, reporting requirements, limitations periods, and audit and assessment provisions.

DOTAX notes the following key concerns in administering the proposed wealth tax:

First, by their nature wealth taxes make it difficult for taxpayers to determine whether the tax applies to them. Business and real property appraisals are complex, time intensive, and arduous undertakings. A wealth tax forces taxpayers to incur significant costs to simply determine their net wealth and whether the tax applies. Since the wealth tax is to be reported and paid on an annual basis with a taxpayer's income tax, as implied by the proposed § 4 on page 3, the appraisal burden will also be imposed annually – even if the appraisal determines a taxpayer has no liability that year.

Second, a wealth tax presents difficulties for collections, as it is imposed on unrealized gains, or assets that have not been already sold or exchanged for liquid assets. Since taxpayers may not have liquid assets to pay their liability, it would pose a problem if there is not enough time between a taxpayer's appraisal date and payment deadline. Income taxes are more easily collected since income is usually realized in the form of cash,

Third, wealth tax assessments present significant risks for appeals because appraisals can vary depending on the methodology used (sales comparison approach vs. cost approach vs. income approach) and assumptions made. Appeal risks are higher because of the subjective nature of appraisals and DOTAX lacks the skills and experience in conducting individual wealth appraisals. DOTAX will likely need to engage third-party experts if taxpayers appeal a wealth tax assessment.

DOTAX is unable to administer the proposed tax in Section 1 for taxable years beginning after December 31, 2025, without further details. Significant aspects of the wealth tax are to be addressed by DOTAX submitting proposed legislation under Section 2 of the bill no later than forty days prior to the convening of the regular session of 2026. However, any legislation proposed on this timeline will likely not be approved in time for filers to begin complying with the wealth tax by January 1, 2026. Creation of the administrative rules, forms, instructions, and systems for administering the wealth tax could only occur after these issues are addressed through legislation and even then, would take significant time to implement.

Finally, the bill's request for DOTAX to propose legislation on various aspects of the wealth tax may direct resources away from DOTAX's primary goal of administering the tax laws that are already in effect. DOTAX suggests that the issues in Section 2 of the bill, which involve material policy considerations, are more suited for deliberation and publication by the Tax Review Commission, which is scheduled to convene this year for its systematic review of the State's tax structure.

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

SERVCO

Senator Karl Rhodes, Chair
Senator Mike Gabbard, Vice Chair
Committee on Judiciary

Thursday, January 30, 2025
Conference Room 016; 9:15 a.m.

RE: SB 313 Relating to a Wealth Asset Tax – In Opposition

Aloha Chair Rhoads, Vice Chair Gabbard and members of the committee:

I am the Executive Chair of Servco Pacific Inc. but am representing the 112 Hawaii family businesses in the Coalition to Save Hawaii's Family Businesses.

We oppose SB 313 because it would require costly and unduly burdensome measures to comply in the case of family businesses and would be a destructive, unfair and ultimately ineffective tax on family businesses. We all know that Hawaii-based businesses have been disappearing (with no Hawaii-based companies taking their place), and this bill will help accelerate that 40 year trend.

We believe that the cost and time to comply with this proposed wealth tax on family business assets would be unreasonably high. Unlike bank accounts or public stockholdings, there is no easy way to determine the value of an operating family business other than by doing an annual third party valuation. While the cost of a valuation varies with the size and complexity of the business, it is commonly in the mid-five figures. In addition, commercial real estate assets will require separate third party appraisals, which are also costly. More importantly, valuation firms will need to interview a number of the business's executives and managers to discuss financial projections and future risks and opportunities. That information, which would be in the valuation report to be submitted as part of the tax return, would be extremely sensitive as it would include projections of revenues, profit margins and debt levels, and assessment of opportunities and risks. If that information were to be discovered by a competitor, it would be very damaging. And, the Hawaii Department of Taxation will have to review all of that paperwork each year.

In terms of the substantive problems with this bill, any tax that is imposed on the value of illiquid assets creates major challenges to family businesses. Because family businesses are privately owned and their stock is not traded on a public stock exchange, the only practical way for a family shareholder to raise funds is to have the family business extend a loan or pay more in dividends. A wealth tax on a family business shareholder becomes a tax on the family business. Whether funds are borrowed or received in dividends, the wealth tax reduces reinvestment into the business and thereby compromises that business's competitiveness. All

SERVCO PACIFIC INC.
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Honolulu, HI 96819 USA

businesses must reinvest most of their profits to keep up with the competition, whether that it is to create new products, improve their facilities, develop their people or upgrade their technology.

Even worse, a wealth tax over time will force the sale of parts of the family business. Initially, the family business will borrow funds to loan or dividend to its shareholders (which debt in itself is not healthy for the business), but at some point, it will be forced to liquidate assets. All family businesses will be damaged by this, but the clearest case is with family farms and ranches, which are typically "asset rich but cash poor". Nothing is sadder than a family farm or ranch being forced to sell off a few acres a year to pay the tax.

As mentioned above, we need to reinvest the great bulk of our profits to remain competitive. But, as a general matter for Hawaii's family businesses, our toughest competitors are national and global public companies. They already have huge advantages in scale, financial strength, marketing and talent. But, because we know our local customers and how to do business here, and we compete on a level playing field, we have stayed in the game. A wealth tax, however, makes the playing field uneven and unfair because public companies do **not** have to pay it whereas family businesses do. It is only assessed on a public company's shareholders who live in Hawaii, and they have easy ways to liquidate portions of their holdings on a public stock exchange.

Finally, this is not a very effective tax. The State would actually get more tax revenues from family businesses if they allowed them to reinvest more: every dollar that is reinvested yields future streams of general excise tax, income tax, property tax and employee income tax revenues. A wealth tax ends up being short-sighted and ultimately counterproductive. Moreover, as with the case of the state estate tax, imposing this tax will encourage Hawaii residents subject to the tax to move their residency to another state. An academic study by economists, Jon Bakija and Joel Slemrod, found that a state would receive 1.73 times more in excise, income and property taxes if an individual continued to reside in state for five years than with a state estate tax. The same analysis would apply to a wealth tax. We already know of several individuals who have moved out of state because of the state estate tax, and a wealth tax would only encourage more departures.

All of these reasons are why only one state, Massachusetts, has a state wealth tax. Let's keep Hawaii Hawaii, and Hawaii's family businesses are a major part of that. We only ask that we be treated fairly so that we can continue to reinvest in Hawaii and to contribute to our community.

Very truly yours,

Mark H. Fukunaga

LEGISLATIVE TAX BILL SERVICE

TAX FOUNDATION OF HAWAII

735 Bishop Street, Suite 417 Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: MISCELLANEOUS, New Wealth Asset Tax

BILL NUMBER: SB 313, HB 1235

INTRODUCED BY: SB by RHOADS, HB by KAPELA, AMATO, GRANDINETTI, IWAMOTO, LA CHICA

EXECUTIVE SUMMARY: Establishes a wealth asset tax of one per cent of the state net worth of each individual taxpayer who holds $20,000,000 or more in assets in the State.

SYNOPSIS: Adds a new chapter to the HRS to establish a wealth asset tax.

The new tax is on the activity of sustaining excessive accumulations of wealth.

The amount of tax to be paid every year is 1% of the state net worth of each individual taxpayer who holds $20,000,000 or more in assets in the State; provided that the individual taxpayer's net worth shall be based on the individual's assets, not joint assets, and a married individual shall file a separate return; provided further that if the taxpayer pays a wealth asset tax on the same asset in a different state, the amount paid to the other state shall be subtracted from the state tax liability.

A taxpayer's state net worth includes but will not be limited to the aggregate value of assets in the following categories:

(l) Real Property

(2) Stock in any publicly and privately traded C-corporation

(3) Stock in any S-corporation

(4) Interests in any partnership

(5) Interests in any private equity or hedge fund

(6) Interests in any other noncorporate business

(7) Bonds and interest-bearing savings accounts

(8) Cash and deposits

(9) Farm assets

(10) Interest in mutual funds or index funds

(11) Put and call options on securities

(l2) Futures contracts

(l3) Art and collectables

(l4) Financial assets held offshore

(15) Pension funds

(l6) Debts owed to the taxpayer

(l7) Other assets

The tax imposed is to be reported and paid at the same time as income taxes.

Assets belonging to any person who can be claimed as a dependent that are in excess of $50,000 are aggregated with the assets of the taxpayer who can claim the person as a dependent.

The department of taxation is to prescribe forms and rules to implement the chapter.EFFECTIVE DATE: Upon approval, provided that section 2 shall apply to taxable years beginning after December 31, 2025.

STAFF COMMENTS: The national Tax Foundation (no relation to our organization) recently published a comment on wealth tax proposals that were proposed in CA, CT, HI, IL, MD, NY, and WA. Its commentary, at https://taxfoundation.org/state-wealth-tax-proposals/, is republished here for the Committee's information.

Wealth Tax Proposals Are Back as States Take Aim at Investment

January 17, 2023

By Jared Walczak

Wealth taxes are back in a big way.

In a coordinated effort, lawmakers in seven states that collectively house about 60 percent of the nation's wealth—California, Connecticut, Hawaii, Illinois, Maryland, New York, and Washington—are introducing wealth tax legislation on Thursday.

The campaign is part of a broader national focus on new taxes on investment, entrepreneurship, and wealth. For instance, a pending proposal in New York would yield a nearly 30 percent tax on wealthy New York City residents' capital gains income, about 50 percent higher than the 20 percent federal tax on long-term capital gains. Elsewhere, lower estate tax thresholds would impose the tax on the upper middle class and not just the very wealthy—including the small businesses and farms policymakers have long worked to protect from estate taxes to avoid forcing them to break up to pay the tax. And the wealth taxes themselves would vary across the seven states, partly due to differing state constitutional constraints.

Not that constitutions will always stand in the way of legislative proposals. A wealth tax is transparently in conflict with Washington's state constitution, but that has not stymied prior proposals and it isn't standing in the way of a new effort to be unveiled on Thursday. California proposals have tended to include exit taxes—designed to continue to tax those who respond by leaving the state—that implicate a host of federal constitutional provisions, a reality that has provoked little consternation among supporters. And most prior proposals would tax *worldwide* net worth for state residents, with all the constitutional questions that raises.

The constant across all seven states, or wherever such taxes are proposed: wealth taxes are economically destructive, their base is almost impossible to measure accurately, and they create perverse incentives and promote costly avoidance strategies. Very few taxpayers would remit wealth taxes—but many more would pay the price.

Proponents sometimes argue that wealth taxes are small and that the rich can afford them. But because the rates are on net worth—not on income—they cut deeply into investment returns, to the detriment of the broader economy. Average taxpayers may not care if the ultra-wealthy have lower net worths. But they will certainly care if innovation slows and investments decline.

We are not accustomed to thinking about taxes in terms of stocks (accumulated wealth) rather than flows (income streams). To most people, it's not intuitive how a wealth tax rate compares to something we better understand, like income tax rates.

Imagine a $50 million investment, held for 10 years and earning a 10 percent nominal annual rate of return in a 3 percent annual inflation environment. Without a wealth tax, that investment would yield $46.5 million in investment returns, in current dollars, after 10 years. With a 1 percent wealth tax, it would yield $37.3 million. The wealth tax would wipe out nearly 20 percent of the gains. If the gains were realized at the end of 10 years, a 1 percent wealth tax would have reduced gains by as much as the 20 percent federal capital gains tax.

In current dollars (valued at the start, not the end, of the investment period), that 1 percent annual wealth tax becomes a 14.5 percent effective tax on net income ($6.3 million of $43.6 million in pre-tax gains). But because each year there was less principal to invest than there would have been absent the annual tax, another $2.9 million is forgone not as tax revenue but as investment gains that never materialized. The result: a 1 percent wealth tax erodes 19.8 percent of the investment income.

If prior efforts are any indication, some of these proposals (like Washington's) will have a base of fairly liquid, publicly traded investments, for which there is a known market value. But others, potentially including California's, would tax all assets of the wealthy, many of which lack a known market value. This could include tangible assets, like artwork, as well as nonfinancial intangible assets, like trademarks or goodwill, which can be nearly impossible to value. Worst of all, it can include ownership stakes in closely held corporations and partnerships, which often defy evaluation.

A promising tech startup might briefly be valued at hundreds of millions of dollars but fold without ever turning a profit. Another might fly under the radar until suddenly acquired for billions of dollars. Owners of the former might face insurmountable wealth tax burdens on a hypothetical net worth that never generates actual income and ultimately vanishes, while owners of the latter might avoid any wealth tax on a company that presumably had significant value before a price tag was affixed by its acquisition.

Taxing wealth consisting of unrealized gains from publicly traded assets is relatively straightforward, since some portion of the shares could be sold in satisfaction of tax liability. (This would, of course, still have consequences for some wealthy investors who are trying to maintain a controlling interest, and conflicting treatment of capital gains at the federal and state levels would create confused incentives.) But with private business assets, the tax can be much more consequential: some portion of the company or its assets may have to be sold to pay taxes on gains that only exist on paper. The owners are asset rich but cash poor.

Even for the most public of public figures, net worth is not only difficult to assess, but also difficult to project. And wealth taxes are imposed regardless of whether there is any income at all, and regardless of whether net worth is increasing or decreasing.

In current dollars, Elon Musk lost $226 billion between November 2021 and December 2022. Sixty-two percent of his wealth frittered—not to say twittered—away. And he at least had investments to liquidate had he been required to pay wealth tax on the much higher November 2021 valuation. For many entrepreneurs in the earlier stage of their venture, not only might their net worth prove highly volatile (and difficult to assess), but they also may have few ways to generate the cash flow necessary to pay the tax.

At either end of that spectrum, of course, there is the prospect of exit: those subject to a wealth tax could decamp to another state, a move that is far easier at the state than the national level. In fact, the economic consequences—both from outmigration and lower economic activity—are so significant that even at the national level, most countries have abandoned any wealth taxes they once had.

Thirteen OECD countries have imposed wealth taxes since 1965, but the number dwindled to three—in Norway, Spain, and Switzerland—by 2022, with governments increasingly acknowledging the economic harms intrinsic to such taxes. However, Colombia's new left-wing government reinstituted a wealth tax for the start of the current calendar year. That is the only recent example for states to follow, amid a general trend of repudiation and repeal. (France has a tax on high-end real property, but no longer on other sources of wealth.)

From thirteen to four, at the national level, where exit is comparatively difficult. Yet seven states want to try this experiment in the United States?

California has previously considered an 0.4 percent state wealth tax, which proponents estimated would have raised about $7.5 billion a year—equal to 4.2 percent of state revenue at the time, and just under 1.1 percent of combined federal and state tax revenue from California, more than the tax share under three of the four national wealth taxes in OECD countries.

People will move. California knows people will move. Its response: an exit tax, and wealth taxes owed for years after leaving the state. This almost certainly runs afoul of the Commerce Clause of the U.S. Constitution and interferes with the constitutionally protected right of travel.

But that's where the economic illogic of wealth taxes leaves states: contemplating constitutionally dubious taxation of nonresidents to counter the simple reality that wealth taxes undercut investment and drive entrepreneurs and innovators out of state.

* * * * *

Errata: This piece originally stated that New York City's state-city capital gains tax, at just under 30 percent, would be almost twice as high as the federal rate. It would of course be about 50 percent higher.

Digested: 1/27/2025

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Removing barriers to Hawaii's prosperity

LATE

Jan. 30, 2025, 9:15 a.m.
Hawaii State Capitol
Conference Room 415 and Videoconference

To: Senate Committee on Judiciary
Sen. Karl Rhoads, Chair
Sen. Mike Gabbard, Vice-Chair

From: Grassroot Institute of Hawaii
Ted Kefalas, Director of Strategic Campaigns

RE: SB313 — RELATING TO A WEALTH ASSET TAX

Aloha Chair, Vice-Chair and other members of the Committee,

The Grassroot Institute of Hawaii **opposes** SB313, which would establish a wealth asset tax of "1% on the state net worth of each individual taxpayer who holds $20 million or more in assets in the state."

In this proposal, "assets" refers to the "worldwide net worth" of the taxpayer and includes items such as real estate, stock, business interests, business funds and art and collectibles.

The intention of this bill might be noble, but as a practical matter, wealth taxes are difficult to administer and can cause economic damage.

To the first point, the state Department of Taxation would have to figure out how to accurately estimate the entire net worth of wealthy individuals on a year-to-year basis, at a cost yet to be determined. How much money would the department need to hire appraisers and accountants to estimate the tax burden of such individuals?

The bill also seems to assume that those who would be taxed will do nothing in response. In fact, such a tax likely would incentivize those same individuals to adopt creative accounting strategies aimed at lowering their net worths, so they could avoid having to pay the tax.

To the second point — about potential economic damage — a wealth asset tax also could encourage high net worth individuals to move their assets out of Hawaii to states that don't have such a tax, which in turn would reduce business investment in Hawaii and curb job growth.

A study of European wealth taxes in the 1980s and 1990s discovered that such taxes "dampen economic growth." And out of 13 European countries that employed wealth taxes before the turn of the century, only three still had them as of 2020. The other 10 abandoned them because of their high administrative costs, inefficiency and economic harm.[1]

If Hawaii lawmakers want to help working families, they should abandon their reliance on taxes as a public policy tool, which has succeeded only in establishing Hawaii as the state with the highest cost of living.

Instead of attempting to solve the state's economic problems through a tax on the wealthy, lawmakers should focus on lowering Hawaii's cost of living, such as by lowering taxes and fees and reducing regulations that limit opportunities and stifle economic growth.

Thank you for the opportunity to testify.

Ted Kefalas
Director of Strategic Campaigns
Grassroot Institute of Hawaii

[1] Jared Walczak, "Wealth Tax Proposals Are Back as States Take Aim at Investment," Tax Foundation, Jan. 17, 2023; Allison Scharger and Beth Akers, "Issues 2020: What's Wrong with a Wealth Tax," Manhattan Institute, Oct. 8, 2020; and Asa Hansson, "Is the wealth tax harmful to economic growth?" World Tax Journal, 2010.

SB-313
Submitted on: 1/27/2025 10:54:14 AM
Testimony for JDC on 1/30/2025 9:15:00 AM

Submitted By	Organization	Testifier Position	Testify
Victor K. Ramos	Individual	Oppose	Written Testimony Only

Comments:

Simply put, this proposal is unfair to those identified in this bill as "1" percenters.

I OPPOSE this bill.

SB-313
Submitted on: 1/27/2025 3:01:07 PM
Testimony for JDC on 1/30/2025 9:15:00 AM

Submitted By	Organization	Testifier Position	Testify
Scott Smart	Individual	Oppose	Written Testimony Only

Comments:

Testimony on S.B. 313

I STRONGLY OPPOSE this bill. Attempting to create this "wealth" tax will be an administrative nightmare, and to the extend it is successful mainly work to drive people out of the state. How many appraisers does the legislature propose to provide authorization for to determine this "wealth"?

Technical comment:

SECTION 1 proposed new chapter / section -1 has a definition ot *"taxpayer" means a person subject to a tax imposed by this chapter, including individuals, estates, and trusts.*

Yet "by this chapter" refers in new section -2 to a "qualified taxpayer". Nothing in this bill defines "qualified taxpayer" nor does SECTION 2 ask the department of taxation to propose rules for determining "qualified taxpayer".

SB-313
Submitted on: 1/27/2025 4:05:41 PM
Testimony for JDC on 1/30/2025 9:15:00 AM

Submitted By	Organization	Testifier Position	Testify
Michael EKM Olderr	Individual	Support	In Person

Comments:

I support this bill. If the rich and affluent want to claim and own parts of Hawaii, they should pay their fair share. To them, Hawaii is a postcard; a house here is a trophy. They exploit this island as a symbol of status and wealth. If the people who call this island home have to scrap to keep living here, those with 100 times their means should also do so. That way, they might finally realize that Hawaii is more than a postcard or a trophy; it is a home that's been exploited for far too long and deserves better stewards than those too shallow to think so little of it.

SB-313
Submitted on: 1/27/2025 9:09:42 PM
Testimony for JDC on 1/30/2025 9:15:00 AM

Submitted By	Organization	Testifier Position	Testify
Keoni Shizuma	Individual	Support	Written Testimony Only

Comments:

Aloha committee members of the Senate Committee on Judiciary,

I stand in support of this bill.

The extremely wealthy that this bill will impact have benefited disproportionately from economic growth and unfair tax loopholes that favor the wealthy. They should contribute more to the public good and this tax helps with that.

There will be very few that will be affected by this tax and they can afford it.

Mahalo for your time and consideration.