JOSH GREEN M.D.
GOVERNOR

SYLVIA LUKE
LT. GOVERNOR

GARY S. SUGANUMA
DIRECTOR

KRISTEN M.R. SAKAMOTO
DEPUTY DIRECTOR

STATE OF HAWAIʻI
DEPARTMENT OF TAXATION
Ka ʻOihana ʻAuhau
P.O. BOX 259
HONOLULU, HAWAIʻI 96809
PHONE NO: (808) 587-1540
FAX NO: (808) 587-1560

TESTIMONY OF GARY S. SUGANUMA, DIRECTOR OF TAXATION

TESTIMONY ON THE FOLLOWING MEASURE:
H.B. No. 1173, Relating to Tax Liens.

BEFORE THE:
House Committee on Finance

DATE: Wednesday, February 19, 2025
TIME: 2:00 p.m.
LOCATION: State Capitol, Room 308

Chair Yamashita, Vice-Chair Takenouchi, and Members of the Committee:

The Department of Taxation (DOTAX) offers the following comments on H.B. 1173 for your consideration.

H.B. 1173 amends section 231-33(f), Hawaii Revised Statutes (HRS), to require DOTAX to identify the assessment date for any taxes owed on certificates of tax liens.

H.B. 1173 also amends section 231-33(g), HRS, to require DOTAX to issue certificates of discharge for any liabilities that have been satisfied or "become unenforceable."

DOTAX notes that the amendment to section 231-33(g), HRS, requiring the discharge of "unenforceable" liens, will cause ambiguity and confusion. Although the preamble of the bill indicates that the intent is to discharge liens after expiration of the 15-year period, a tax debt is not completely unenforceable after the 15-year limitation period expires.

Act 166, Session Laws of Hawaii (SLH) 2009, created a 15-year statute of limitations on certain collection actions on tax assessments. Specifically, Act 166 prohibits a "levy" or "proceeding in court under chapter 231" to collect tax if the levy or proceeding is initiated after the 15-year period. Act 166 does not, however, prohibit

DOTAX from taking collection actions other than a levy or court proceeding under chapter 231, and thus does not render a tax debt completely unenforceable or uncollectible after the 15-year period expires.

For example, under current law, DOTAX may receive payment on a tax debt after the 15-year period expires if a taxpayer needs to obtain a tax clearance or clear a lien on real property. Liens exist to preserve a creditor's interest and may stay on a property for more than 15 years after the initial assessment as a passive method of collection. This may occur if the outstanding amount does not justify a foreclosure and the property has not been sold. However, once the property is sold or refinanced and the lien needs to be removed, DOTAX retains the authority to require full payment in exchange for removing the lien. This does not violate the existing limitation on collections because it does not constitute a levy or proceeding in court.

Based on the foregoing, it is unclear what circumstances would require DOTAX to issue a certificate of discharge.

DOTAX further notes that if the bill is amended to expressly require DOTAX to issue a certificate of discharge after expiration of the 15-year period, significant time and effort would be required to determine which liens would be affected because of the various tolling provisions. For each tax debt over 15 years old, DOTAX would need to determine whether the 15-year period is tolled because (1) the taxpayer agreed to a suspension; (2) the taxpayer's assets were in control or custody of a court during any period of time; (3) the taxpayer applied for an offer in compromise; or (4) the taxpayer was outside the State for a continuous period of at least six months.

Accordingly, if DOTAX will be required to issue a certificate of discharge based on expiration of the 15-year period, DOTAX requests that the effective date of the bill be amended to January 1, 2027, to provide sufficient time to identify and analyze the affected liens, issue certificates of discharge, and make necessary system changes to ensure ongoing compliance.

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

LEGISLATIVE TAX BILL SERVICE

TAX FOUNDATION OF HAWAII

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

SUBJECT: ADMINISTRATION, NET INCOME, GENERAL EXCISE, USE, TRANSIENT ACCOMMODATIONS, CONVEYANCE, RENTAL MOTOR VEHICLE, INSURANCE PREMIUM, MISCELLANEOUS, Discharge Tax Liens When Unenforceable

BILL NUMBER: HB 1173

INTRODUCED BY: YAMASHITA

EXECUTIVE SUMMARY: Requires the Department of Taxation to: (1) State the assessment date on certificates of tax lien; and (2) Issue certificates of discharge when the tax liability on which a lien is based has become unenforceable by lapse of time.

SYNOPSIS: Amends section 231-33, HRS, to require a certificate of tax lien to state the date on which the liability for the tax or taxes was assessed. Also requires the department to issue a certificate of discharge as to any liability that has been satisfied or that has become unenforceable.

EFFECTIVE DATE: Upon approval.

STAFF COMMENTS: Sections 6 through 14 of Act 166, SLH 2009, enacted what has been described as a 15-year statute of limitations on collection of taxes. The language added to each of the affected taxing chapters reads:

> Where the assessment of the tax imposed by this chapter has been made within the period of limitation applicable thereto, the tax may be collected by levy or by a proceeding in court under chapter 231; provided that the levy is made or the proceeding was begun within fifteen years after the assessment of the tax. For any tax that has been assessed prior to July 1, 2009, the levy or proceeding shall be barred after June 30, 2024.
>
> [Some provisions tolling the 15-year period follow.]

We understand that the Department of Taxation interprets the above language to bar any NEW collection action, and that it is therefore not required to release any preexisting liens and also may deny tax clearances to any taxpayer that has a tax debt regardless of how old that debt is.

The language in Act 166, SLH 2009, appears to have been modeled on Internal Revenue Code section 6502, which states:

> **§ 6502. Collection after assessment.** (a) Length of period.--Where the assessment of any tax imposed by this title has been made within the period of limitation properly applicable thereto, such tax may be collected by levy or by a proceeding in court, but only if the levy is made or the proceeding begun--

(1) within 10 years after the assessment of the tax, or [list of exceptions].

The significance of the language "by levy or by a proceeding in court" in the federal statute can be explained by going back over a century. The first federal statute of limitation on collection of tax was enacted in the Revenue Act of 1918, where section 250(d) provided:

> (d) Except in the case of false or fraudulent returns with intent to evade the tax, the amount of tax due under any return shall be a determined and assessed by the Commissioner within five years after the return was due or was made, and no suit or proceeding for the collection of any tax shall be begun after the expiration of five years after the date when the return was due or was made. In the case of such false or fraudulent returns, the amount of tax due may be determined at any time after the return is filed, and the tax may be collected at any time after it becomes due.

Revenue Act of 1918, sec. 250, 40 Stat. 1082.

At the time, the Service believed that the prohibition was only on judicial proceedings, leaving the agency free to collect by other means, such as levy and distraint. The U.S. Supreme Court did not agree, for it said:

> There are two methods to compel payment. One is suit, a judicial proceeding; the other is distraint, an executive proceeding. The word 'proceeding' is aptly and commonly used to comprehend steps taken in pursuit of either. There is nothing in the language or context that indicates an intention to restrict its meaning, or to use 'suit' and 'proceeding' synonymously.
>
> The purpose of the enactment was to fix a time beyond which steps to enforce collection might not be initiated. The repose intended would not be attained if suits only were barred, leaving the collector free at any time to proceed by distraint. In fact distraint is much more frequently resorted to than is suit for the collection of taxes. The mischiefs to be remedied by setting a time limit against distraint are the same as those eliminated by bar against suit. Under petitioner's construction taxpayers having no property within reach of the collector would be protected against stale demands, while others would be liable to have their property distrained and sold to pay like claims. The result tends strongly to discredit petitioner's contention.
>
> ….
>
> … A reasonable view of the matter is that it was the intention of Congress by the clause here in question to protect taxpayers against any proceeding whatsoever for the collection of tax claims not made and pressed within five years.

Bowers v .New York & Albany Lighterage Co., 273 U.S. 346, 349, 351 (1927). The Court also took notice of a later version of the statute, in the Revenue Act of 1924, that applied the time limitation to "distraints" as well as "suits." *Id*. at 351. The Court affirmed judgments in the

lower courts holding that money collected by distraint beyond the limitation period had to be returned to the taxpayers from which the money was taken.

Since then, the federal courts have held that a limitation on collection by levy/distraint and lawsuits, as stated in IRC § 6502, in HRS § 235-111, and in comparable provisions of Hawaii taxing chapters, constituted a limitation on collection by any means, so that the Government could not keep any money it collected beyond the statutory period.

> An element of unfairness may seem to exist on account of the inability of the collector to make a valid collection of an amount which had been timely assessed, but that would likewise be true in any case where the Commissioner has failed to make proper collection within the statutory period. Congress has provided a statutory period when collection can be made and a collector may not proceed contrary thereto. Here the remedy through which collection could have been effectively made was provided by plaintiff but released by the collector without any fault on the part of plaintiff. Collection was then made after the statute had run. Such a collection is an overpayment within the meaning of section 607 of the Revenue Act of 1928, and since a claim for refund was timely filed it is refundable to plaintiff.

Brewerton v. United States, 80 Ct. Cl. 529, 9 F. Supp. 503, 508 (1935). Subsequent federal cases also have made it clear that the Service is not allowed to keep money to satisfy a taxpayer debt if the underlying collection statute of limitations has expired.

In 2009, the Legislature also expressed support for a statute of limitations on collection. SB 118, SD 1 (2009), which contains language very similar to sections 6 through 14 of Act 166, SLH 2009, was explained in a committee report:

> The purpose of this measure is to limit the time period in which the collection of a tax by levy or court proceeding may commence to ten years after assessment of the tax.
>
> Your Committee finds that taxpayers should have the benefit of ascertaining with certainty at a future time when their tax liability comes to an end. The federal government imposes a ten-year statute of limitations on the collection of delinquent taxes. According to testimony, Hawaii is one of only four states that presently does not have some form of statute of limitations on tax collections.

Senate Stand. Comm. Rep. No. 194 (2009).

Another way to look at the situation is that if the Department receives taxpayer money through whatever means, and keeps it after the 15-year period has come and gone, the Department has collected the money "by levy," because "levy" is "the imposition or collection of an assessment, such as a tax" (https://www.merriam-webster.com/dictionary/levy). Thus, the collection would be barred by current law.

The language in the bill is based on Internal Revenue Code section 6325(a)(1), which states:

(a) RELEASE OF LIEN

Subject to such regulations as the Secretary may prescribe, the Secretary shall issue a certificate of release of any lien imposed with respect to any internal revenue tax not later than 30 days after the day on which—

(1) LIABILITY SATISFIED OR UNENFORCEABLE

The Secretary finds that the liability for the amount assessed, together with all interest in respect thereof, has been fully satisfied or has become legally unenforceable; …

The bill would align the Hawaii tax laws with the sections of the Internal Revenue Code after which the collection statute of limitations is modeled.

Digested: 2/15/2025

HAWAII ASSOCIATION OF PUBLIC ACCOUNTANTS

Organized August 7, 1943
P.O. BOX 61043
HONOLULU, HAWAII 96839

Committee on Finance

Wednesday, February 19, 2025; 2:00 p.m.
Conference Room 308 & Videoconference
State Capitol

Re: SUPPORT, with amendment, of HB1173 – Relating to Tax Liens

Chair Yamashita, Vice Chair Takenouchi, and Committee Members:

The Hawaii Association of Public Accountants (HAPA) is the only statewide public accounting organization with active chapters on Oahu, Maui, Big Island, and Kauai. It has approximately 450 members, consisting primarily of small to mid-sized CPA firm owners and employees who are in the active practice of public accountancy.

My name is Marilyn M. Niwao, M.S.P.H., J.D., CPA, CGMA, and I am a past State President and currently a State Director of the Hawaii Association of Public Accountants. I am a Hawaii licensed CPA and Attorney, and a principal of a well-established Maui CPA firm, Niwao & Roberts, CPAs, a P.C.

I am also the immediate past Vice Chair of the Hawaii Council on Revenues, a former Commissioner of the Hawaii Tax Review Commission, and a Past President of the National Society of Accountants. However, I am testifying here solely in my capacity as a State Director of the Hawaii Association of Public Accountants and co-chair of its legislative committee, while drawing upon my knowledge obtained while serving in the above positions.

HB1173 requires the Department of Taxation to (1) state the assessment date on certificates of tax lien; and (2) issue certificates of discharge when the tax liability on which a lien is based has become unenforceable by lapse of time.

Recommended Amendment to HB1173:

HAPA recommends that subsection (g) of Section 231-33, Hawaii Revised Statutes, as set forth in HB1173 be amended to read as follows to reflect those taxes and sections of the Hawaii Revised Statutes under which the Department of Taxation was made subject to a fifteen year limitation on collection after assessment in Sections 6 (Income Tax), 7 (GET), 8 (TAT), 9 (Use Tax), 10 (Fuel Tax), 11 (Conveyance Tax), 12 (Vehicle Surcharge Tax), and 14 (Insurance Tax) of Act 166, Session Laws of Hawaii 2009:

> (g) The department may issue a certificate of discharge of any part of the property subject to the lien imposed by this section, upon payment

> in partial satisfaction of such lien, of an amount not less than the value as determined by the department of the lien on the part to be so discharged, or if the department determines that the lien on the part to be discharged has no value. The department shall issue a certificate of discharge as to any liability that has been satisfied or that has become unenforceable under sections 235-111, 237-40, 237D-9, 238-7, 243-14, 247-6.5, 251-8, and 431:7-204.6. Any [~~such~~] discharge so issued shall be conclusive evidence of the discharge of the lien as therein provided.

The Hawaii collection limitation was patterned after the IRS ten year limitation set forth in IRC Section 6502(a)(1 which allows the IRS to levy or begin court proceedings "within ten years after the assessment of the tax." The above-referenced Hawaii statutes provide that a levy must be made or court proceedings begun "within fifteen years after the assessment of the tax." This is why it would be useful for the tax lien certificate to include the date on which the liability for the tax or taxes was assessed.

The above-mentioned HRS sections also contain provisions that may suspend or extend the Hawaii fifteen-year limitation on collection after assessment, which should be addressed by HAPA's proposed amendment above.

IRC Section 6325(a) directs the IRS to release a federal tax lien within 30 days of when the liability is fully paid or becomes legally unenforceable. HAPA therefore requests that you support HB1173, as amended, to (1) state the assessment date on certificates of tax lien; and (2) issue certificates of discharge when the tax liability on which a lien is based has become unenforceable.

Thank you for this opportunity to testimony. Please do not hesitate to ask any questions by contacting me at niwao@mauicpa.com or at (808) 242-4600, ext. 224.

Respectfully submitted,

Marilyn M. Niwao

Marilyn M. Niwao, M.S.P.H., J.D., CPA, CGMA
HAPA State Director and Legislative Committee Co-chairperson

Ronald I. Heller
700 Bishop Street, Suite 1500
Honolulu, Hawaii 96813

phone 808 523 6000 fax 808 523 6001
rheller@torkildson.com

Before the House Committee on Finance

Wednesday, February 19, 2025 at 2:00 pm

Testimony of Ronald I. Heller

In Support of HB 1173

RELATING TO TAX LIENS

Chair Yamashita, Vice-Chair Takenouchi, and Members of the Committee:

I **support** HB 1173.

I have been practicing tax law in Hawaii for more than 40 years, and I have seen instances of taxpayers (or their children) being burdened by liens that remain on record with respect to old uncollectible taxes.

This bill would simply bring Hawaii into alignment with the tax collection rules that apply to the IRS at the federal level – once an underlying tax debt is no longer collectible due to the statute of limitations expiring, then any tax lien recorded with respect to that uncollectible debt is discharged. Note this has been the rule at the federal level for decades – this is not a new or radical idea.

I would be happy to respond to any questions you may have.

Respectfully submitted,

Ronald I. Heller

Ronald I. Heller

Richard Paul McClellan III
LAWYER
www.taxsolutionslawyer.com

February 17, 2025

HOUSE COMMITTEE on FINANCE

Rep. Kyle T. Yamashita, Chair
Rep. Jenna Takenouchi, Vice Chair

Re: **HB1173 Tax Liens; Discharge When Unenforceable**

Hearing Date: 2/19/2025, 2:00 P.M.

Dear Chair Yamashita, Vice-Chair Takenouchi, and Committee Members Grandinetti, Holt, Hussey, Keohokapu-Lee Loy, Kitagawa, Kusch, Lamosao, Lee, Miyake, Morikawa, Templo, Alcos, Oda, and Ward:

As a licensed attorney practicing for thirty years in tax controversies, **I strongly support House Bill 1173 for multiple reasons**.

HB1173 will help taxpayers, practitioners, and the tax authorities (DoTax and Internal Revenue Service) understand their obligations and rights. This bill requires the Department of Taxation to include the assessment date on certificates of tax lien. The assessment date helps taxpayers by informing the taxpayer of how long they have to pay off the balance. The assessment date allows the Department of Taxation and the Internal Revenue Service to readily determine priorities in cases of the sale of real property. Knowing the assessment date saves professional fees because it allows practitioners to readily advise their clients without having to request information from the Department.

A. Exhibits attached for reference:

I have attached a sample federal tax lien to my testimony, with identifying information redacted. Please note that the federal tax lien contains the date of assessment and last day for refiling. The tax liens are redacted because, in the era they were issued, identifying information was listed on the face of the lien.

B. Provision Relating to "Date of Assessment":

The "date of assessment" is extremely helpful because it:

1. enables Taxpayers to know how long they have to pay off the balance and understand the Department's position on payments in an approved payment plan;
2. allows the Department of Taxation and the Internal Revenue Service to readily determine priorities in cases of the sale of real property and the priority for distribution of proceeds. See, *Minnesota Department of Revenue v. United States*, 184 F.3d 725, 729 (8th Cir. 1999), citing *United States v. City of New Britain, et.al.*, 347 U.S. 81, at 86 (1954).

3. Allows practitioners to readily advise taxpayers without resorting to a specific request to the Department or time-consuming research.

C. Conforming the Discharge to Federal Practice Is Appropriate.

Conforming to the federal practice and procedures is fair to the taxpayer because the tax lien would include the expiration date on the lien document itself. Including the expiration date on the lien would make administration less burdensome upon the Department of Taxation because the lien would be essentially self-releasing.

I have attached a redacted copy of a federal tax lien for reference.

The Internal Revenue Service typically releases expired tax liens within thirty (30) days of expiration as a matter of policy, but because the federal tax lien has an expiration date on the face of the lien, it can be considered "self-releasing." See, Internal Revenue Manual, 5.12.3.3.2 (7-15-2015).

D. The DoTax Is Appropriately Collecting Back Taxes

The Legislature is reminded that the collection statute of limitations (generally) does not apply in situations where a levy (bank levy, wage levy) is made, or a court action to collect has been filed, prior to expiry. See, HRS § 237-40 (a) (in part, emphasis added):

> Where the assessment of the tax imposed by this chapter has been made within the period of limitation applicable thereto, the tax may be collected *by levy or by a proceeding in court under chapter 231*; provided that the levy is made or the proceeding was begun within fifteen years after the assessment of the tax. For any tax that has been assessed prior to July 1, 2009, the levy or proceeding shall be barred after June 30, 2024

According to the DoTax FYE 06/30/2024 Annual Report, page 49, the Department of Taxation issued 34,795 levies in the preceding year, slightly down from 38,712 the prior FYE. Since approximately 2015, the Attorney General, Civil Recoveries Division, has filed hundreds of court cases to reduce tax liens to judgment and collect upon the judgments.

The number of levies should be considered in light of the total civilian workforce, estimated at approximately 670,000.
https://dbedt.hawaii.gov/economic/qser/labor-force/

The Legislature is urged to pass this thoughtful measure.

/s/ Richard McClellan

(808) 523-0449
Thomas Square Centre, 846 S. Hotel Street, Suite # 308
Honolulu, HI 96813

1008

Form 668 (Y)(c)
(Rev. October 2000)

Department of the Treasury - Internal Revenue Service

Notice of Federal Tax Lien

Area:
SMALL BUSINESS/SELF EMPLOYED AREA #12
Lien Unit Phone: (206) 220-5596

Serial Number
redacted1

For Optional Use by Recording Office

As provided by section 6321, 6322, and 6323 of the Internal Revenue Code, we are giving a notice that taxes (including interest and penalties) have been assessed against the following-named taxpayer. We have made a demand for payment of this liability, but it remains unpaid. Therefore, there is a lien in favor of the United States on all property and rights to property belonging to this taxpayer for the amount of these taxes, and additional penalties, interest, and costs that may accrue.

Name of Taxpayer JI redacted

Residence
HONOLULU, HI 96822-2871

IMPORTANT RELEASE INFORMATION: For each assessment listed below, unless notice of the lien is refiled by the date given in column (e), this notice shall, on the day following such date, operate as a certificate of release as defined in IRC 6325(a).

Kind of Tax (a)	Tax Period Ending (b)	Identifying Number (c)	Date of Assessment (d)	Last Day for Refiling (e)	Unpaid Balance of Assessment (f)
1040	12/31/1998	547 REDACTED	05/22/2000	06/21/2010	5720.64
1040	12/31/1999	547-	10/15/2001	11/14/2011	6363.13
1040	12/31/2000	547	10/15/2001	11/14/2011	1493.34

Place of Filing
BUREAU OF CONVEYANCES
REGISTRAR
HONOLULU, HI 96803

Total $ 13577.11

This notice was prepared and signed at SEATTLE, WA, on this,

the 24th day of November, 2003.

INTERNAL REVENUE SERVICE
915 2ND AVE M/S W246
SEATTLE WA 98174

Signature
for C. YEE

Title
REVENUE OFFICER
(808) 539-1550

32-02-3649

(NOTE: Certificate of officer authorized by law to take acknowledgment is not essential to the validity of Notice of Federal Tax lien Rev. Rul. 71-466, 1971 - 2 C.B. 409)

Part 1 - Kept By Recording Office

Form **668(Y)(c)** (Rev. 10-00)
CAT. NO 60025X