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To: The Honorable Donna Mercado Kim, Chair
and Members of the Senate Committee on Government Operations

Date: Thursday, January 8, 2018
Time: 3:15 P.M.
Place: Conference Room 224, State Capitol

From: Linda Chu Takayama, Director
Department of Taxation

Re: S.B. 2257, Relating to Taxation

The Department of Taxation (Department) has serious concerns regarding S.B. 2257 and offers the following comments for the Committee's consideration.

S.B. 2257 requires that any revenue estimate provided by the Department to the Legislature, executive office, or administrative office include a description of the methodology and assumptions made in deriving the revenue estimate. The bill also subjects revenue estimates and their methodology to public disclosure notwithstanding certain laws prohibiting disclosure of confidential tax return or tax return information. The bill is effective upon approval.

First, the Department notes that it provides revenue estimates to the Governor, Council on Revenues, and other state agencies, such as the Department of Budget and Finance and the Department of Accounting and General Services, in performance of their respective functions. The Department is concerned that subjecting the methodology and assumptions of its revenue estimates to public scrutiny will result in the frustration of legitimate government functions.

Second, in preparing revenue estimates, the Department is performing a function that is very similar to the federal Joint Committee on Taxation (JCT). The JCT is nonpartisan committee of the U.S. Congress which is involved in all stages of the legislative process, including bill drafting and preparing official revenue estimates for all proposed tax legislation. The Department is generally tasked with preparing revenue estimates because the Legislature does not have a committee like the JCT to prepare official revenue estimates for it.

The JCT does not provide the specific methodology for each proposed tax measure it provides an estimate for. Instead, the JCT describes its revenue estimating process and general

considerations in some detail.¹ An overview of revenue estimating process, as provided by the JCT, is as follows:

- The JCT staff provides estimates relative to baseline receipts projected for future years under present law, not relative to receipts in years prior to the enactment of the proposal.
- The JCT staff incorporates many types of behavioral responses in revenue estimates.
- The JCT staff generally assumes a fixed gross national product when preparing conventional revenue estimates.

The Department is willing and able to provide a similar report which outlines the revenue estimating process that it follows.

Third, the Department firmly believes that revenue estimates prepared for proposed tax legislation should be free of any political pressure. During the consideration of a bill, the legislative focus will often shift from the substance of a tax measure to the revenue estimate for it. This is appropriate given the importance of a balanced budget. However, if the methodologies and assumptions behind revenue estimates are disclosed, the focus may shift not to the cost of the measure but instead to the methodology and assumptions made to determine that cost. The Department is concerned that this focus will compromise the independence of its revenue estimates. To preserve the independence of revenue estimates, the Department does not disclose its methodology or assumptions to anyone outside of the Department, including other executive branch agencies.

Finally, revenue estimates are frequently derived from confidential taxpayer data. The Department is seriously concerned about the erosion of taxpayer confidentiality this bill represents. It is important to remember that our State's tax system is based on voluntary compliance with the tax laws. Voluntary compliance requires taxpayers to truthfully report their income and pay the tax owed, without any worry that the information reported will be disclosed to the public. Lack of confidence in the voluntary compliance system will result in reduced tax revenues for the State.

Thank you for the opportunity to provide comments.

¹ The Joint Committee on Taxation. "The Joint Committee on Taxation Revenue Estimating Process." January 23, 2017.



Senate Committee on Government Operations
Chair Donna Mercado Kim, Vice Chair Russell Ruderman

02/08/2018 3:15 PM Room 224
SB2257– Relating to Taxation

TESTIMONY / SUPPORT
Corie Tanida, Executive Director, Common Cause Hawaii

Dear Chair Kim, Vice Chair Ruderman, and members of the committee:

Common Cause Hawaii supports SB2257 which would require DOTAX to provide revenue estimates along with a description of the methodology and assumptions used when arriving at the estimate. It requires the estimates and descriptions to be open to public disclosure, inspection and copying.

The issue of taxes and revenue impact affects everyone. As such, the public should have access not only to revenue estimates provided by DOTAX but also the methodology and assumptions used to arrive at the estimate. By increasing transparency and access, this bill would allow the public to better understand and weigh in on bills that impact state revenue.

Thank you for the opportunity to offer testimony **supporting SB2257**.



Email: communications@ulupono.com

SENATE COMMITTEE ON GOVERNMENT OPERATIONS
Thursday, February 8, 2018 — 3:15 p.m. — Room 224

Ulupono Initiative Strongly Supports SB 2257, Relating to Taxation

Dear Chair Kim, Vice Chair Ruderman, and Members of the Committee:

My name is Murray Clay, and I am Managing Partner of Ulupono Initiative, a Hawai'i-based impact investment firm that strives to improve the quality of life for the people of Hawai'i by working toward solutions that create more locally produced food; increase affordable, clean, renewable energy; and better management of waste and fresh water. Ulupono believes that self-sufficiency is essential to our future prosperity and will help shape a future where economic progress and mission-focused impact can work hand in hand.

Ulupono strongly supports SB 2257, which requires that revenue estimates provided by the Department of Taxation (DOTAX) to the Legislature be accompanied by a description of the methodology used and assumptions made in providing the estimate, because it helps to understand the department's conclusions and whether DOTAX is using the most updated information. It also supports our value of transparency in policymaking.

Decisions made by the Legislature have a lasting effect on the people of Hawai'i. As a result, it is in the best interest for policymakers to have more open, transparent information, especially from experts in the field. Furthermore, it is critical that DOTAX shares how it came to such conclusions since the Legislature relies heavily on this analysis and many legislators cite it as the most accurate and impartial source.

Because advocates and experts typically do not see the conclusions of the DOTAX analysis until a hearing begins, they are forced to wonder how DOTAX arrived at its figures. For example, DOTAX's analysis on an energy storage tax credit a few years ago projected far more tax credits being claimed than could be supported by either the needs of the grid or sound economic analysis. In short, the estimated "cost" to the State was over exaggerated. Meanwhile, legislators will often side with DOTAX over advocates since it has the perception of neutrality even if DOTAX is often the least familiar stakeholder on the subject matter in question. Especially during the hectic legislative session, it is also extremely difficult to schedule meetings with DOTAX to understand the methodology. While we are not claiming that DOTAX does this purposefully, there is no doubt that there is a great incentive to avoid explaining its methodology in great detail. DOTAX would be able to avoid

Investing in a Sustainable Hawai'i

meeting with stakeholders long enough before a bill must meet its next legislative deadline.

Financial analysis requires data/estimates of the assumptions that are filtered thru a financial model/framework/program to come up with the final numerical results. Therefore, if DOTAX provides an analysis of a bill's financial impact in its testimony, then logically it should also have its assumptions readily available. In our experience, however, it chooses not to disclose its assumptions and methods in its testimony.

While the Department of Taxation is likely to have additional initial scrutiny from stakeholders if it releases its methodology, over the long run, this should force more interaction between DOTAX and knowledgeable subject matter experts. As DOTAX engages with expert individuals and organizations, it will learn more about the sectors it analyzes and create more realistic and accurate projections in the long run, which will benefit lawmakers' decision-making.

Our concern is that the cost of poorly thought-out State policies could be significantly higher than the cost of any additional DOTAX staff needed to comply with this bill.

As environmental issues become ever more complex and challenging, we appreciate this committee's efforts to look at policies that improve the quality of life for the people of Hawai'i through open and transparent decision-making.

Thank you for this opportunity to testify.

Respectfully,

Murray Clay
Managing Partner

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Senate Committee on Government Operations
Honorable Donna Mercado Kim, Chair
Honorable Russel E. Ruderman, Vice Chair

RE: Testimony in Support of S.B. 2257, Relating to Taxation
Hearing: February 8, 2018 at 3:15 p.m.

Dear Chair and Members of the Committee:

My name is Brian Black. I am the Executive Director of the Civil Beat Law Center for the Public Interest, a nonprofit organization whose primary mission concerns solutions that promote governmental transparency. Thank you for the opportunity to submit testimony **strongly supporting S.B. 2257**.

S.B. 2257 requires public access to revenue estimates and assumptions that are used by the Legislature and State government to decide major issues of public policy. The public records law recognizes: "Government agencies exist to aid the people in the formation and conduct of public policy. Opening up the government processes to public scrutiny and participation is the only viable and reasonable method of protecting the public's interest." S.B. 2257 codifies this State policy in this one critical instance as it applies to revenue estimates.

Revenue estimates often are motivating factors in significant policy decisions. The public cannot have faith in the quality of the State's decisions if it cannot evaluate the quality of the underlying assumptions that drive that decision. Requiring access to revenue estimates allows public scrutiny of the State's assumptions toward the collective goal of developing better public policy and greater public confidence in government decisions.

Thank you again for the opportunity to testify in **support** of S.B. 2257.

TAX FOUNDATION OF HAWAII

126 Queen Street, Suite 304

Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: MISCELLANEOUS, Disclosure of Department of Taxation Revenue Estimates

BILL NUMBER: SB 2257; HB 1817 (Identical)

INTRODUCED BY: SB by KEITH-AGARAN, DELA CRUZ, K. RHOADS, English, Gabbard, Kim; HB by BROWER, CREAGAN, EVANS, JOHANSON, KOBAYASHI, KONG, LOPRESTI, MIZUNO, MORIKAWA, NISHIMOTO, OHNO, QUINLAN, TODD, Nakamura, San Buenaventura, Takayama, Takumi

EXECUTIVE SUMMARY: Requires every revenue estimate provided to the legislature or to an executive or administrative office to have a description of the methodology and assumptions, and requires that it be available to the public. It's a welcome step toward government transparency, and some tweaks may be needed to make sure it works as intended.

SYNOPSIS: Adds a new section to HRS chapter 231 to require that every revenue estimate provided by the department to the legislature or to any executive or administrative office shall be accompanied by a description of the methodology used and assumptions made in providing the estimate. The revenue estimate and description shall be open to public disclosure, inspection, and copying, notwithstanding sections 235-116, 237-34, and 237D-13, or any other law restricting disclosure of tax return or tax return information to the contrary.

EFFECTIVE DATE: Upon approval.

STAFF COMMENTS: At present, the availability of estimated revenue impact information on bills wending their way through the legislature is spotty at best. Even when the Department of Taxation testifies on tax bills, some testifiers share revenue impact information with the legislature; others don't; others share information with the legislative committees and leave the public in the dark; and still others share information with the committees and the public only in response to questions asked at a hearing. Having the information would be a great step toward openness and transparency in important legislative decisions.

To make the measure robust, we suggest that the bill needs to clarify *when* during the process the statement will be available to the public. If this is not done, overzealous people within the government can, and if past practice is followed will, argue that this information is part of a governmental deliberative process and, as such, needs to be kept from the public's prying eyes. The result, usually, is that the information will be withheld from disclosure until it is no longer useful or relevant. For an example of how this game of cat-and-mouse takes place, we offer the following article, which the Foundation published on Oct. 2, 2017. Although the article involves a slightly different issue, the information there is still relevant.

Fritz v. Department of Taxation, and Why You Should Care

Over the past several months, there has been a court fight brewing that could have changed how the Department of Taxation lobbies for legislation.

That's right. Not only special interest groups and activists lobby for legislation. The Department does too. Every year, it introduces and strongly supports "Administration Bills." Many of these propose to make the Department's job easier, but at the expense of taxpayer rights. So it's important for taxpayers to keep tabs on how the Department is pushing these bills.

One example of the above kind of bill was HB 2396 / SB 2925 in last year's legislative session. If a taxpayer files an amended federal income tax return or is adjusted by the IRS, current law allows an extra year for the Department to assess additional tax or for the taxpayer to claim a refund. The bill provided that only the Department, and not the taxpayer, could take advantage of this "bonus time," which is usually needed because tax audits take a while to conclude. The Foundation was concerned that this legislation created a "one-way street," or procedural trap, that could allow the State to retain money to which it was not entitled under law.

Peter Fritz, an attorney who used to work for the Department, tried to get the Department to disclose the letters, texts, and emails sent to legislators in 2009. "Can't do," the Department said. "Work product paid for by taxpayers normally needs to be made public, but policy deliberations can be withheld, and these communications are in that category." Fritz didn't agree, and asked the State Office of Information Practices (OIP) to rule on the matter. OIP ruled in Fritz's favor in 2011, ordering the Department to cough up the documents. The Department complied. But by the time it did so, it was years after the legislative session ended.

In the 2016 legislative session, Fritz tried again. The Department refused to provide documents relating to Administration Bills that it was then sponsoring, again relying upon the "deliberative process privilege" that the OIP had ruled in 2011 to be inapplicable. "Gotta do a case by case determination," the Department said. Fritz filed suit. In January 2017, well after the ending of the 2016 session, the Department "voluntarily disclosed" the documents, although explicitly saying that it "reserved any and all rights to withhold any other documents from disclosure on any and all grounds."

Those documents could have made a difference during session. When SB 2925, described above, was heard by the Senate Ways and Means Committee, then-Chair Jill Tokuda and Majority Leader J. Kalani English were particularly interested in whether the bill was a solution in search of a problem. When they pointedly asked the Department about it at the hearing, the Department representatives professed ignorance. The records later turned over, however, clearly showed that the Department was reacting to a case involving *only one* taxpayer. The legislation, by the way, ultimately died.

In the lawsuit, Fritz asked the court to take positive steps so that the Department can't again play cat-and-mouse. The State, of course, maintained that once they turned over the documents, the suit can no longer exist because courts are there to decide actual controversies, not purely academic issues. The circuit court judge agreed with the State, and the lawsuit will soon be dismissed.

When the Department of Taxation states a position in a communication to the Legislature, the public is entitled to know what that position is. This is especially important with a complicated

Re: SB 2257

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subject like taxation, where the public relies heavily on guidance and interpretations put out by the Department. (Other legislators do too.) And it is critical to have a fully informed debate when the Department tries to coax legislators to change the law in a way that would make its job easier at the expense of taxpayer rights and protections.

Digested 2/5/2018

SB-2257

Submitted on: 2/5/2018 12:20:20 PM

Testimony for GVO on 2/8/2018 3:15:00 PM

Submitted By	Organization	Testifier Position	Present at Hearing
Ray Kamikawa		Support	Yes

Comments:

I support and urge passage of the bill.

As the sole source of revenue estimates for the State's legislative proposals, the Department of Taxation's methodology and assumptions behind such estimates should be disclosed. This will provide transparency to the process, giving everyone an opportunity to question the analysis.

There are varying degrees of accuracy in revenue estimates. Those based on information from DOTAX's tax return entries, such as changes in tax rates, would offer the most accuracy. Some rely on secondary sources, such as DBEDT's data book. And others are just guesses. It is unfair to the Legislature and public for DOTAX to offer estimates without informing them of the bases of those estimates, which can help everyone form an opinion as to their reliability. If they are just guesses, DOTAX should state that revenue estimates are "indeterminate."

Thank you for the opportunity to testify.

PETER L. FRITZ

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THE SENATE
THE TWENTY-NINTH LEGISLATURE
REGULAR SESSION OF 2018

COMMITTEE ON GOVERNMENT OPERATIONS

Testimony on S.B. 2257
Hearing: February 8, 2018

Relating To Taxation

Chair Kim, Vice Chair Ruderman and members of the Committee. My name is Peter Fritz. I am a former Rules Specialist and a tax attorney. I am testifying today **in support** of S.B. 2257.

This bill would require that Department of Taxation revenue estimates provided to the legislature or executive or administrative office be public information. Information on the revenue impact of proposed federal legislation is available to the public for federal bills and it should be the same for Hawaii proposed bills.

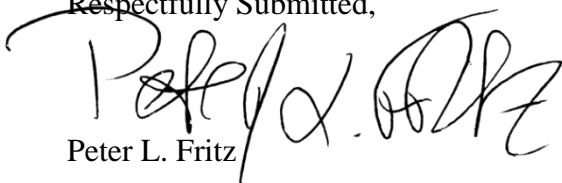
Revenue estimates are important for evaluating bills. Revenue estimates can indicate why certain legislation was introduced and can influence whether a bill will be passed or held. This information should be available to the public.

An example of how such information is important is SB 2925, a bill introduced in 2016. This administration bill would have allowed the Department of Taxation to assess additional state tax based on an IRS determination, while at the same time prohibiting taxpayers from claiming refunds based on IRS determinations that they were entitled to a refund. The existing policy in effect at the time of this bill was that if the IRS made an adjustment to a person's federal income tax, the state would follow that adjustment, upward or downward. This bill would have changed that to a one-way process where your Hawaii tax can go up based on what the IRS finds, but it cannot go down based on what the IRS finds. It is a very rare situation that the IRS will make a determination that a taxpayer overpaid their taxes and it usually will be because a taxpayer made a mistake on their return. I subsequently learned that there had been one situation where the IRS determined that the taxpayer was entitled to a refund. Had the revenue estimate and the explanation behind the estimate been available, the unfairness of this bill would have become obvious from the beginning and legislative time could have been saved.

The federal government believes that it is important for the public to have information about its bills and Hawaii taxpayers should be provided with similar information.

Thank you for the opportunity to testify.

Respectfully Submitted,



Peter L. Fritz