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

Date: Wednesday, February 20, 2019  
Time: 10:05 A.M.  
Place: Conference Room 211, State Capitol

From: Linda Chu Takayama, Director  
Department of Taxation

Re: S.B. 495, S.D. 1, Relating to Taxation

The Department of Taxation (Department) offers the following comments on S.B. 495, S.D. 1, for the Committee's consideration.

S.B. 495, S.D. 1, creates an economic nexus standard for Hawaii income tax. The bill states that a person that lacks physical presence in Hawaii is presumed to be engaged in business in the State if the person engages in 200 or more transactions with persons in the State or has \$100,000 or more in gross income from sources in the State in the current or previous calendar year. The bill is effective upon approval and applies to taxable years beginning after December 31, 2018.

First, the Department notes that this bill will clarify the circumstances under which a person will be subject to Hawaii income tax and that the proposed standard is similar to the standard created for purposes of the general excise tax by Act 41, Session Laws of Hawaii (SLH) 2018.

Finally, the Department notes that it will be able to administer the changes in this bill with the current effective date.

Thank you for the opportunity to provide comments.

# TAX FOUNDATION OF HAWAII

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SUBJECT: INCOME, Nexus Presumptions

BILL NUMBER: SB 495, SD-1

INTRODUCED BY: Senate Committee on Judiciary

EXECUTIVE SUMMARY: States that a seller with more than \$100,000 in in-state sales or 200 transactions into the state shall be deemed to be doing business in the state for purposes of the income tax law. Creates a nexus presumption for income tax like the presumption for general excise tax adopted last year. Clarification is needed on the \$100,000 test because it might not be interpreted as intended, and serious consideration should be given to placing this standard in chapter 231 to make it applicable to more tax types.

SYNOPSIS: Adds a new section to chapter 235, HRS, providing that a person is presumed to be systematically and regularly engaging in business in the State, whether or not the person has a physical presence in the State, if in the current or preceding calendar year: (1) the person engages in two hundred or more business transactions with persons within the State; or (2) the sum of the value of the person's gross income attributable to sources in this State equals or exceeds \$100,000 or for a person that does business within and without the State the numerator of the person's sales factor for the State equals or exceeds \$100,000.

EFFECTIVE DATE: Taxable years beginning after December 31, 2018.

STAFF COMMENTS: Apparently, this bill was intended to be the counterpart for income tax to the nexus standard for general excise tax enacted last year as Act 41, SLH 2018. The nexus presumption under Act 41 is triggered if a potential taxpayer completes 200 transactions, or sales exceeding \$100,000. We recommend using the same language as Act 41 to be consistent with that law and with *South Dakota v. Wayfair, Inc.*, 585 U.S. \_\_\_ (2018), the Supreme Court case on which Act 41 relies.

In this bill, the second prong of the standard refers to the sales factor. However, there may be unintended consequences because the sales factor, at least for sales of tangible personal property, is computed using “throwback rules” that source sales to another state if nexus is not established in this state. That reference may result in taxpayers taking the position that sales of goods into Hawaii don’t count because of the throwback rules. At a minimum, the second half of prong (2) should be removed: “The sum of the value of the person's gross income attributable to sources in this State equals or exceeds \$100,000 [~~or for a person that does business within and without the State the numerator of the person's sales factor for the State equals or exceeds \$100,000~~].”

It is now unclear whether the nexus standard in Act 41 is supposed to apply to only the GET or other tax types. Apparently, that uncertainty prompted this bill. This bill, however, appears to

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apply only to net income tax. What about franchise tax, public service company tax, transient accommodations tax, and so forth? Because nexus is a concept that applies to all taxes, the Committee should consider moving the language of Act 41 to chapter 231, and have it apply to all taxes.

Digested 2/17/2019



**HAWAII GOVERNMENT EMPLOYEES ASSOCIATION**  
AFSCME Local 152, AFL-CIO

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The Thirtieth Legislature, State of Hawaii  
The Senate  
Committee on Ways and Means

Testimony by  
Hawaii Government Employees Association

February 20, 2019

S.B. 495, S.D. 1 – RELATING TO TAXATION

The Hawaii Government Employees Association, AFSCME, Local 152, AFL-CIO supports the purpose and intent of S.B. 495, S.D. 1 which creates a nexus standard for taxing out-of-state businesses on their business income in Hawaii.

In the past two decades, our economy has quickly evolved from purchases made exclusively at brick-and-mortar physical storefronts to now include increasing amounts of internet purchases via online merchants and third-party vendors. As the popularity of e-commerce continues to exponentially grow, fairness dictates that internet-based transactions should be treated in the same manner as other retail transactions. Retail transactions that are taxable by brick and mortar retailers should also be taxable when sold through the internet.

Hawaii has already lost millions of dollars in uncollected internet-based sales, and the losses will likely increase as internet commerce continues to grow. Creating a nexus standard to tax those who regularly and systematically engage in business in Hawaii is necessary and appropriate.

Thank you for the opportunity to testify in support of S.B. 495, S.D. 1.

Respectfully submitted,

*for* Randy Perreira  
Executive Director