

# TAX FOUNDATION OF HAWAII

126 Queen Street, Suite 304

Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: TRANSIENT ACCOMMODATIONS, Add Personal Liability

BILL NUMBER: HB 1043, SD1

INTRODUCED BY: Senate Committee on Judiciary

EXECUTIVE SUMMARY: Amends chapter 237D, Hawaii Revised Statutes, to repeal the misdemeanor for failing to register under chapter 237D and replacing it with a fine structure and to make various technical amendments.

SYNOPSIS: Amends section 237D-4, HRS, to remove the misdemeanor criminal penalty for engaging in the business of furnishing transient accommodations or as a plan manager without being registered. Rather, the noncompliant person shall be subject to the citation process and monetary fines provided in this section.

Amends section 237D-16, HRS, to make section 237-41.5, HRS, relating to personal liability for unpaid tax, applicable to TAT.

Makes various technical and conforming amendments.

EFFECTIVE DATE: 1/1/2022.

STAFF COMMENTS: This is an administration measure sponsored by the Department of Taxation and identified as TAX-03 (21).

Most of the bill makes simple technical changes to the TAT law. It also gets rid of a misdemeanor penalty and substitutes civil fines instead.

But the blockbuster buried in the bill is that it establishes personal liability for unpaid TAT by incorporating one of the provisions from the General Excise Tax Protection Act of 2010, namely HRS section 237-41.5.

Section 237-41.5 provides that if the taxpayer is an entity, and it has unpaid taxes, then the Department can go after the personal assets of any responsible person within the entity, as long as that person “willfully fails to pay or cause to be paid” the tax. That would include any decision to pay any creditor of the company before the tax liability.

Historically, trust fund liability arises when the taxpayer receives and holds someone else’s money that is supposed to be paid to the government, and then doesn’t pay it. This happens, for example, in wage withholding taxes. This also occurs in sales tax states where the tax is the liability of the purchaser and the seller has the obligation to collect and remit the purchaser’s tax. If this money is collected and not turned over to the government, it’s akin to stealing and the government does seem to be justified in using unusual means such as responsible party liability in order to collect it. With Hawaii GET and TAT, however, the tax is another expense of the

business. The business is liable for the tax and needs to pay it. It does not come into possession of someone else's money because, there is no withholding of GET and TAT (at least not in the transient accommodations context) and unlike in the sales tax states, "passing on" of tax liability is purely a matter of contract. Department of Taxation, General Excise Tax Memo. No. 4. Thus the "trust fund" theory on which personal liability is based does not appear to apply to the TAT.

The TAT has been in existence since 1986. Act 340, SLH 1986. The General Excise Tax Protection Act was passed in 2010. Act 155, SLH 2010. Here we are 34 years after the TAT's inception and a decade after the GET provision took effect. Why is the Department pushing for trust fund provisions only now?

If the Committee is inclined to pass the bill and include the above provisions, we suggest making the imposition of personal liability explicit so it can be easily found by those reading the law, such as by restoring section 237D-16, HRS, to its unamended form and then adding:

**237D-\_\_ Certain amounts held in trust; liability of key individuals.** There is hereby imposed personal liability of key individuals of any entity liable for the tax imposed by this chapter in the same manner as provided for the general excise tax in section 237-41.5.

A provision such as this would eliminate "gotcha" situations and would be fairer to the taxpaying public.

Digested 3/27/2021



March 31, 2021

Senator Honorable Donovan M. Dela Cruz, Chair  
Senator Gilbert S.C. Keith-Agaran, Vice Chair  
Members of the Senate Committee On Ways & Means

Re: **HB 1043, HD 3, SD 1 (SSCR 1193)**

**Relating to the Transient Accommodations Tax**

Hearing Date: 4/6/2021, 9:30 a.m.

Dear Chair Dela Cruz & Honorable Committee Members:

I am offering **Comments** regarding my concerns about this bill. Specifically, about the provisions in Section 11 relating to personal liability for unpaid corporate TA taxes. The bill as drafted imports selected language from HRS 237 (the General Excise tax chapter).

This bill as drafted and amended, does not *expressly* provide persons subject to personal liability the right to judicial review, fails to ensure persons assessed have basic information concerning the assessments, and, in the scenario where multiple persons are assessed, does not ensure that basic information about co-obligators and payments is available.

I have included proposed language to address some of the concerns raised in my comments.

1. Persons Being Assessed Liability Should be Entitled To Meaningful Judicial Review

This bill could impose liability for Transient Accommodations (“TA”) tax on a former officer of a bankrupt hotel. It is unlikely that the former officer of a bankrupt hotel would be able to pay an annual TA assessment and make a refund claim. The liability could be hundreds of thousands of dollars and in many cases practically impossible and tremendously unfair due to the size of the debt.

Persons being assessed liability should be entitled to access to our civil justice system. The concept that an officer or responsible employee should have to pay a corporate debt to obtain access to our court system has previously been rejected in other “responsible person” settings.

To prevent any confusion about the legal rights of persons potentially being assigned liability for unpaid or underpaid TA tax, the Legislature should **specifically mention their rights to appeal an assessment**. The specific word “assessment” for personal liability does not appear in Chapter 237’s (237-41.5) provisions relating to personal assessment for unpaid GE taxes.

To address these concerns, I respectfully request that SECTION 11 (current page 15) be amended to incorporate HRS 237-42 “Appeals”:

**[\$237D-16] Administration and enforcement; rules.** (a) The director of taxation shall administer and enforce this chapter. In respect of:

(1) The examinations of books and records and of taxpayers and other persons,

(2) Procedure and powers upon failure or refusal by a taxpayer to make a return or proper return, and

(3) The general administration of this chapter, the director of taxation shall have all rights and powers conferred by chapter 237 with respect to taxes thereby or thereunder imposed; and, without restriction upon these rights and powers, sections 237-8 and 237-36 to 237-42 are made applicable to and with respect to the taxes, taxpayers, tax officers, and other persons, and the matters and things affected or covered by this chapter, insofar as not inconsistent with this chapter, in the same manner, as nearly as may be, as in similar cases covered by chapter 237.

***Added language in bold italics.*** See, §237-42 Appeals. Instead of stopping at 237-41.5, the language of 237-42 should be incorporated:

**§237-42 Appeals.** Any person aggrieved by any assessment of the tax for any month or any year may appeal from the assessment in the manner and within the time and in all other respects as provided in the case of income tax appeals by section 235-114.

Inclusion of this language providing an express right to appeal would clarify that persons assessed personal liability for TA taxes have the legal right to an initial appeal to the Tax Court or to the Board of Review without being compelled to pre-pay and file a refund suit.

## 2. Limited Right to Basic Information

A person being assessed as a responsible person should be entitled to review the tax returns and assessments upon which the personal assessment is premised. Former officers or employees may not have access to the entity’s tax return or an assessment that could be the result of audit changes or late-filed returns.

Current law allows assessments to be prepared on mere estimates (237D-9) and the estimates are presumed correct (237D-9).

In addition, when more than one entity or person is assessed, all liable legal and natural persons should be entitled to some information concerning the status of collection proceedings and payments by other liable persons.

I suggest that Section 11 have an additional subsection (b) added that states:

"(b) Upon written request, the Department shall provide any person upon whom personal liability is sought to be imposed or has been imposed copies of the legal entity's tax return(s), or assessment(s), as the case may be, for any periods that are the subject of the potential or actual assessment of personal liability arising under this section. Furthermore, in any instance where more than one person is subject to liability for the same liability, any liable person may request in writing, and the Department shall disclose: the name of any other person determined to be liable and whether the Department has attempted to collect the liability from such other person, the general nature of such collection activities, and the amount collected."

This language is in part borrowed from the Internal Revenue Code at 26 U.S.C. 6103(e)(9).

The burden of compliance for the Department of Taxation is minimal.

The suggested language also resolves potential concerns that the Department of Taxation is not properly crediting payments.

The new language also permits responsible persons sufficient information to determine whether to bring indemnity-type claims against other co-obligors.

Sincerely,

/s/ Richard McClellan