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The Twenty-Fourth Legislature, State of Hawaii
Hawaii State Senate
Committee on Ways and Means

Testimony by
Hawaii Government Employees Association
March 28, 2008

H.B. 2961, H.D. 2, S.D. 1 – RELATING
TO TAXATION

The Hawaii Government Employees Association, AFSCME, Local 152, AFL-CIO supports the purpose and intent of H.B. 2961, H.D. 1, which is to make specific changes to Hawaii's tax law that will allow the state to participate in the Streamlined Sales and Use Tax Agreement that will permit the taxation of Internet-based transactions. There are several reasons for taxing Internet-based transactions.

Retail trade has been transformed by the Internet. As the popularity of "e-commerce" grows, fairness dictates that Internet-based transactions should be treated in the same manner as other retail transactions. Retail transactions that are taxable by "bricks and mortar" retailers should also be taxable when sold through the Internet.

Hawaii has already lost millions of dollars in Internet-based sales, and the losses will likely increase as the importance of the Internet continues to grow. Therefore, we support H.B. 2961, H.D. 2, S.D. 1 that makes necessary changes to the tax code to comply with the Streamlined Sales and Use Tax Agreement. The ongoing loss of millions in tax revenue from e-commerce is a problem that will get worse over time unless we take appropriate action. The revenues gained through the Streamlined Sales and Use Tax Agreement may fund public education and other important public policy priorities. Thank you for the opportunity to testify in support of this important measure.

Respectfully submitted,

Nora A. Nomura
Deputy Executive Director



Senator Rosalyn Baker, Chair
Senator Shan Tsutsui, Vice Chair
Committee on Ways & Means
State Capitol, Honolulu, Hawaii 96813

HEARING Friday, March 28, 2008
 9:30 am
 Conference Room 211

RE: HB2961, HD2, SD1, Relating to Taxation

Chair Baker, Vice Chair Tsutsui, and Members of the Committee:

Retail Merchants of Hawaii (RMH) is a not-for-profit trade organization representing about 200 members and over 2,000 storefronts, and is committed to support the retail industry and business in general in Hawaii.

RMH supports HB2961, HD2, SD1, which adopts amendments to Hawaii's tax laws to implement Streamlined Sales and Use Tax Agreement.

Through our affiliation with the National Retail Federation, the world's largest retail trade association, and a major participant in the Streamlined Sales Tax Project, RMH has watched the development and progress of this program over the past seven years and has supported Hawaii's initiatives to participate in the multi-state discussions. As commerce over the Internet increased, traditional brick and mortar retailers, which are required by law to collect taxes for government, have experienced an erosion of their sales base to remote sellers, which, under most circumstances, are not subject to tax mandates. The Streamlined Sales Tax Project will level the playing field.

Additionally, we are encouraged that an initiative in congress holds even greater promise to ameliorate this unfair situation.

The members of the Retail Merchants of Hawaii respectfully request that you pass HB2961, HD2, SD1. Thank you for your consideration and for the opportunity to comment on this measure.

A handwritten signature in cursive script, appearing to read 'Carol Prejzler'.

President



HB2961 SD1 Relating to Streamlined Sales Tax

DATE: Friday, March 28th, 2008
9:30am
Conference Room 211

TO: Senate Committee on Ways and Means
Senator Roslyn Baker, Chair

FROM: Lisa H. Gibson
President
Hawaii Science & Technology Council

RE: Testimony In Support of the Intent of HB2961 SD1

Aloha Chair, Vice Chair, and Members of the Committee:

The Hawaii Science & Technology Council supports HB2961 SD1, the Streamlined Sales Tax Bill, which would adopt changes to Hawaii's tax law that will allow Hawaii to participate in the Streamlined Sales and Use Tax Agreement. HiSciTech supports legislation such as this because:

1. It merely assists in the collection of taxes already due to State of Hawaii;
2. It will enhance state tax revenue in a time of economic turmoil.
3. It will level the playing field for local businesses with out of state vendors. .

The Hawaii Science & Technology Council is a private tax-exempt 501(c)6 industry association with a 28-member board. The council serves Hawaii companies engaged in ocean sciences, agricultural biotechnology, astronomy, defense aerospace, biotech/life sciences, information & communication technology, energy, environmental technologies, and creative media.

Thank you for the opportunity to testify on this important bill.

Lisa H. Gibson
President

TAXBILLSERVICE

126 Queen Street, Suite 304

TAX FOUNDATION OF HAWAII

Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: MISCELLANEOUS, Streamlined sales and use tax; earmark for DOE and UH

BILL NUMBER: HB 2961, SD-1

INTRODUCED BY: Senate Committee on Economic Development and Taxation

BRIEF SUMMARY: Adds a new chapter to the law to set out sections of HRS chapter 237 which establish transactions subject to the 0.5% general excise tax rate.

Adds a new chapter to the law to set out sections of HRS chapter 238 which establish transactions subject to the 0.5% use tax rate.

Adds a new chapter to the law to set out sections of HRS chapter 237 which establish transactions subject to the 0.15% general excise tax rate. The measure delineates provisions governing “insurance producers.”

Adds several new sections to HRS chapter 237 to establish sourcing rules to determine when a product or service is taxed, including telecommunication services. The measure delineates provisions defining “direct mail” and how the sourcing of direct mail transactions will be ascertained.

Adds several sections to HRS chapter 255D to establish provisions relating to the determination of the proper general excise or use tax rates between different tax jurisdictions, rounding on tax computations, amnesty for registered sellers who pay, collect, or remit general excise or use taxes in accordance with the terms of the streamlined sale and use tax agreement, tax rate changes by a county, certified service provider, confidentiality of records, liability for uncollected tax and rate changes, and customer refund procedures.

Amends HRS sections 237-8.6 and 238.2.6 to prohibit a county to conduct an independent audit of sellers registered under the streamlined sales and use tax agreement.

Amends HRS section 237-24.3 to redefine the term “prosthetic device.”

Amends HRS section 237-31 to provide that ____% of all tax revenues realized under the newly restructured chapters (formerly HRS chapter 237) shall be deposited into the state treasury to the credit of the department of education and the university on an equal basis provided that such moneys shall augment and not replace existing operating or capital improvement budgets. Beginning on July 1, _____, all tax revenues realized under the newly restructured chapters (formerly HRS chapter 237) shall be deposited into the state treasury.

Appropriates an unspecified amount of general funds for fiscal 2009 for technical assistance and briefings to enable the auditor to carry out the purposes of this act including the preparation of proposed legislation by contracting with a legal professional with a background and practice in taxation. The

legislative reference bureau shall assist the auditor or contractor in drafting any legislation. The appropriation shall take effect on July 1, 2008.

Requires the president of the senate and the speaker of the house to appoint two legislative members each, and one public member each to a committee to hold meetings to carry out this act. The director of taxation shall be an ex-officio member.

It shall be unlawful for any person or employee of the state to make known information imparted by any tax return or permit any tax return to be seen or examined by any person. Also provides that it shall be lawful to allow a private contractor to inspect any tax return of any taxpayer, or to furnish the private contractor with any information concerning any item on a return only for the purposes of conforming the state's general excise and use taxes to be operative for the Streamlined Sales Tax Project's Model Agreement and Act.

EFFECTIVE DATE: January 1, 2010

STAFF COMMENTS: The Streamlined Sales Tax Project's Model Agreement and Act is a project undertaken with other states that is intended to simplify sales and use tax administration as it relates to multiple sales and use tax rates, definitions, and taxing jurisdictions.

Goals of the project include the establishment of a single sales tax rate, uniform definitions of sales and use tax terms, requiring states to administer any sales and use taxes, and a central electronic registration system to allow a seller to register to collect and remit sales and use taxes for all states.

At the national level, there appears to be a number of difficulties in the negotiations and unanimous agreement is far from reality. Before jumping on the band wagon, lawmakers should exercise care as it should be remembered that Hawaii does not have a sales tax as found in other states. To the contrary, the general excise tax, while viewed as a sales tax, is a far cry from the retail sales tax structure found on the mainland.

The 2005 legislature had approved a measure to direct the department of taxation to identify issues that need to be resolved to effectuate the orderly enactment and operation of a streamlined sales and use tax based on the Streamlined Sales Tax Project Model Agreement and Act. The act also repealed the streamlined sales and use tax advisory committee council which was to consult with the department of taxation on the implementation of the streamlined sales and use tax agreement in Hawaii. When this measure was sent to the governor, the governor vetoed it due to the repeal of the advisory council, unrealistic deadlines in the measure, and concerns of allowing a third party to access confidential tax return information. A special session of the legislature overrode the governor's veto and the measure passed as Act 3 of the Special Session of 2005.

Basically the measure attempts to turn Hawaii's gross receipts tax imposed for the privilege of doing business in Hawaii into a retail sales tax structure with respect to where the tax is imposed. Much of the bill is devoted to separating the wholesale imposition of the tax from the retail and then reworking where the tax is applied otherwise known as "sourcing." The general excise tax, as we know it today, would be radically changed to accommodate the format adopted by the Streamline Sales Tax Project (SSTP).

What is not evident in the measure is that by participating in the consortium known as the SSTP, Hawaii

businesses will be required to collect the sales taxes of other states when purchases are made by residents of that state. The cost of collecting, accounting, and remitting those taxes will add even more overhead costs to operating a business in Hawaii. So why is there such enthusiasm on the part of the legislature to participate in the SSTP? Lawmakers have been promised hundreds of millions of dollars that could be had if the state would just participate in the project. The suggestion came to the 2001-2003 Tax Review Commission on the recommendation of their consultant who was already an advocate of the project.

Of course, no thought was given to how this would affect Hawaii businesses and what additional costs there would be. Given the fact that Hawaii businesses will now have to operate in a different mode insofar as the general excise/SSTP sales tax, will lawmakers compensate businesses for undertaking the collection of other state's retail sales taxes? Indeed, the law being proposed in this measure is a hybrid of the current general excise tax law and a retail sales tax. It retains the two-tiered wholesale/retail system and keeps the tax imposed on services as well as on business-to-business transactions. So the measure attempts to have the best of both worlds - to force other states to collect our general excise tax while retaining the pyramiding features of the general excise tax. This is a major change in the state's largest source of general fund revenues. Care should be taken in making this transition as it could alter not only the past interpretation of the general excise tax, but it may also have a major impact on the revenue producing capacity of the tax.

One of the key issues still under discussion amongst the members who have already signed on is "where" does the sale occur. For a number of the larger states like California, Illinois, and Texas which have much at stake since they are states that manufacture goods shipped to other states, the sourcing rules they adopted use "origin" based rules, that is the tax that is imposed at the place from which the goods are shipped and not where the purchaser takes possession. The proposed bill here is ambiguous at best as in some cases being origin based as long as the purchaser takes possession of the goods at the place of the business but provides, on the other hand, for the taxation at the address to which the goods are delivered. It is this destination rule that causes the most problems for businesses as they must now deal with a plethora of rates depending on the number of states from which they receive orders for their goods. A recent development at a meeting in Dallas amended the SSTP agreement to allow a state to elect whether it would impose a destination-based collection or one based on the origin of the transaction. This was to stop the hemorrhaging of loss of members to the Agreement. While some states may elect destination, there is no doubt that the larger states will elect origin sourcing as they are probably net exporters of goods. That being the case, Hawaii residents will probably end up paying the Illinois or California sales tax on their purchases from out-of-state vendors and in the long run, the purported windfall will turn into a disaster for Hawaii. Under current law, the use tax would otherwise have been due on those sales and while it has been difficult to enforce and collect on individual sales, more of an effort should be placed on the collection of the use tax where Hawaii already has jurisdiction.

Again, a main area of concern is whether the states can afford the streamlined system itself. Given the promises that have been made and not delivered upon such as the software that is supposed to facilitate the collection and remittance of the various states' sales taxes, to the promise to pay the cost of funding the administrative structure of the governing board, it appears that all of these are promises with no intent to make it happen. As such, it is premature for Hawaii to jump on the throttling locomotive engine that appears to be headed for a brick wall. This proposal needs more discussion in the interim and further clarification as well as a discussion with taxpayers who must carry out the duty of the actual collection. Curiously, this is what the 2005-2007 Tax Review Commission recommended, that until the member states of the SSTP Agreement come to a definitive conclusion, it is premature for Hawaii to jump on

board. With this latest development, it appears that Hawaii will be a net loser as its residents will end up paying other state's sales taxes.

While the proposed measure attempts to conform Hawaii's general excise and use tax laws to the streamlined sales and use tax agreement, due to its complexity and technical aspects, it is questionable whether members of the legislature are qualified to determine whether this measure will be sufficient to comply with the Streamlined Sales and Use Tax Agreement.

In 2006 a bill that would adopt the streamline sales tax agreement was introduced and nearly passed the legislature but for a small glitch in the closing moments of the session. This, despite the fact that the State Auditor had a consultant assess the revenue potential of participating in the project. Instead of the hundreds of millions of dollars the promoters of the project had promised, the consultant estimated that Hawaii would benefit at the very least by about \$10 million and at the most \$50 million.

At the same time, when the department of taxation was asked what it estimated it would cost the department to implement the project for Hawaii, the price tag was set at \$15 million. Thus, it came as no surprise that when the Tax Review Commission looked at the issue, the decision was a no brainer, Hawaii would stand to gain about \$10 million in revenue, but it would cost the state \$15 million to implement. And that doesn't include the cost to businesses in Hawaii that would be required to collect the sales taxes of other states.

So the Commission's advice to the legislature and administration was to wait. In its recommendation it was noted that "the largest states (by economic size) have failed to sign on to the project, jeopardizing the chances of becoming an effective vehicle for collecting the Use Tax. Until the Project shows greater promise of producing results, it is premature for Hawaii to incur the expense to join it."

This measure also proposes to initially earmark a portion of the revenues that are basically general excise tax revenues into the state treasury and credit those revenues equally between the department education and the University of Hawaii. This would be in addition to any other funds they receive through the normal appropriation process. While the measure also proposes that all such revenues would be earmarked to the department of education and the University of Hawaii at an unspecified date, this would result in a substantial loss of general fund revenues to fund necessary state programs, including capital improvement requests statewide. An earmarking of 100% of general excise tax revenues with 50% earmarked to the department of education and 50% to University of Hawaii would also obviate the need for a legislative session as there would not be sufficient funds for the remaining state operations. This is nothing more than pandering to supporters of the department of education and the University for their support of this measure.

The long and short of this measure is that it is nothing more than a tax increase that will probably end up benefitting other states if the majority of states adopt "origin" based sourcing and continuing a tradition of passing the cost to administer and complying with the proposal on to businesses in Hawaii, adding yet another nail in the coffin for businesses in Hawaii. It is certainly a reflection of the lack of understanding of Hawaii's unique general excise tax and how generous it is in producing revenues for the state and is an effort driven by greed.

LINDA LINGLE
GOVERNOR

JAMES R. AIONA, JR.
LT. GOVERNOR



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SENATE COMMITTEE ON WAYS & MEANS

TESTIMONY REGARDING HB 2961 HD 2 SD 1 RELATING TO TAXATION

TESTIFIER: KURT KAWAFUCHI, DIRECTOR OF TAXATION (OR DESIGNEE)

DATE: MARCH 28, 2008

TIME: 9:30AM

ROOM: 211

The intent of this bill is to conform Hawaii law to the requirements of the Streamlined Sales and Use Tax Agreement ("SSUTA"). The Streamlined Sales and Use Tax Agreement is a method developed by the states and businesses primarily to have internet and catalogue sellers voluntarily collect the sales and use tax from consumers on behalf of the States for those sellers who did not have nexus with the state. Currently, people who buy from catalogues and the internet are supposed to pay use tax on their purchases, however in practice, few do.¹ This bill would provide a *voluntary* mechanism for internet and catalog sellers to collect this tax from the consumers and pass it on to the Department, thereby resulting in a net revenue gain to the State.

The Department of Taxation takes **no position on the content** of this measure; however respectfully **requests that the original HD 1 and other technical corrections requested by the Department in HB 3192/SB 3114 be inserted in its place.**

I. ORIGINAL CONTENTS—THE IMPORTANCE OF STUDYING TAX INCENTIVES

The Legislature has enacted path-breaking tax credits to promote growth in technology and innovation, with the goal of encouraging knowledge-based, higher-wage industries in Hawaii. The Legislature has also recognized, however, that it is important to evaluate the effectiveness of its efforts in this area as well as other areas of tax incentive policy. The Department of Taxation respectfully requests the authority and resources to conduct an economic study on the effects of Hawaii income tax credits.

¹ However, businesses generally comply with the use tax more than individuals.

II. SUGGESTED AMENDMENTS FOR EFFICIENT TAX ADMINISTRATION

The Department respectfully requests that the Committee consider inserting the following technical considerations into this measure for streamlined tax administration. These amendments can be found in HB 3192/SB 3114:

ERRONEOUS REFUND CLAIMS—Congress recently amended the Internal Revenue Code to allow for a twenty percent penalty on any excessive refund claims. This new erroneous refund claim penalty is found at 26 USC § 6676. This penalty was included in recent congressional legislation as a revenue raiser for the federal government. With certain of the tax incentives provided in Title 14, HRS, providing the Department of Taxation with the ability to assess a penalty for refund or credit claims where a taxpayer's claim lacks a reasonable basis will assist with the administration of Hawaii's taxes by providing a deterrent mechanism, which presently does not exist. As was the intent on the federal level, this legislation would also be a potential revenue raiser for the general fund.

During this provision's prior consideration in the Senate, the industry had problems with this penalty's lack of definitions. The Department does not object to the Committee inserting a specific definition of "reasonable basis" to include, among other things inadvertence, mistake, or innocence. Also, the Department does not object to thresholds where this penalty takes effect; nor does the Department object to applying this penalty only where tax professionals are involved. The Department is willing to work with the Committee on draft language for this provision.

Because this legislative session has many fiscal constraints given the current economic conditions, this amendment will provide revenue gains for the budget.

PUBLIC BOARD OF REVIEW INFORMATION—Current law is ambiguous as to whether certain information discussed at a Taxation Board of Review hearing is public and able to be disseminated.

Chapter 232, HRS, is clear that a Board of Review hearing is a public meeting. However, other conflicting confidentiality laws preclude the Department from discussing the taxpayer's identity or the specific legal arguments presented to the Board of Review. A dilemma arises if a person who was not present at the hearing requests information regarding the hearing, the Department cannot disclose appeal briefs or taxpayer identity. However, if the same person were at the hearing, the person would know the taxpayer's identity and other material information. This bill clarifies what information is public when discussed at a Board of Review hearing.

SOCIAL SECURITY NUMBERS ON APPEAL DOCUMENTS—With the onset of identity theft, administration of tax appeals should likewise conform to protection of such sensitive data.

Currently, tax appeals require taxpayers to submit a copy of the tax return(s) in dispute during the appeal. Tax returns routinely contain sensitive data, including social security numbers of individuals. This bill authorizes individuals and the Department to redact all but the last four digits

of the social security number on any tax returns filed with the Tax Appeal Court.

"KIDDIE TAX" AMENDMENTS—In its conformity provisions, Hawaii does not expressly conform to the "Kiddie Tax" assessed by the Internal Revenue Code.

However, Hawaii has adopted its own "Kiddie Tax" at section 235-7.5, HRS. In 2006, Congress made various amendments to the "Kiddie Tax" contained in the Internal Revenue Code. This bill makes similar conforming amendments to the changes made by Congress to ensure consistency in the application and assessment of these similar taxes.

Because this legislative session has many fiscal constraints given the current economic conditions, this amendment will provide revenue gains for the budget.

TAX ADMINISTRATION SPECIAL FUND—Act 206, Session Laws of Hawaii 2007, amended the Tax Administration Special Fund to allow use of the funds for the administration of credits under section 235-110.9, HRS.

The Department of Taxation understood the intent of this amendment was to allow use of the funds for administration of other high tech credits, including the refundable credit for research activities under section 235-110.91, HRS. This bill clarifies that the tax administration special fund may be used for administering both high technology tax credits.

CANNED COMPUTER SOFTWARE ELIGIBILITY FOR THE CAPITAL GOODS EXCISE TAX CREDIT—Hawaii's capital goods excise tax credit allows a credit equal to the general excise tax paid on depreciable tangible personal property.

The credit defines depreciable tangible personal property as of the Internal Revenue Code of 1954, as amended in 1984. Canned computer software was considered depreciable tangible personal property in the Internal Revenue Code of 1986. This bill amends the definition of depreciable tangible personal property to allow for canned computer software to qualify for the capital goods excise tax credit. The bill also deletes from the definition of cost "the actual invoice price," so that cost will be defined as basis, which is simpler to administer. The bill also eliminates the phase-in language since the credit has been completely phased-in since 1989.

This amendment will clarify erroneous positions taken by taxpayers and tax practitioners that argue computer software currently qualifies under this credit.

SOCIAL SECURITY NUMBER USE IN TAX ADMINISTRATION—Chapter 487J, HRS, was enacted in 2006 to limit the use of social security numbers by businesses and government.

The Department's tax administration processes and procedures rely heavily on the use of the social security number to ensure identification of a taxpayer. This bill makes clarifying amendments to chapter 487J, HRS, that allow the Department of Taxation to utilize social security numbers in the administration of Hawaii taxes.

III. THE STREAMLINED SALES & USE TAX PROJECT

A. Concerns over this legislation in a slowing economy.

Initially, the Department points out that it is a well-settled principle of economics that when an economy is slowing, increasing taxes is strongly discouraged because people are already struggling to make ends meet financially. During economic slowing, economics suggests that money should remain with the people and in the economy in order to boost economic performance. The Department cautions further consideration of this legislation during a slowing economy based upon these economic concepts.

B. Benefits of Streamlined Sales Tax.

The Streamlined Sales & Use Tax Project may provide benefits to Hawaii, including:

1. **Increased Revenue to the General Fund.** It is undetermined at this time exactly how much additional revenue Hawaii may stand to gain from this bill. The Department concedes that a revenue gain is likely, however the Department is concerned that past projections have significantly overestimated this potential gain.
2. **Level the Playing Field.** Adopting this legislation will effectively bring equity to local retailers that lose business to internet or mail-order commerce. By purchasing goods on the internet, for example, local purchasers can realize a minor tax benefit by purchasing out-of-state. Each sale out-of-state is a lost sale in Hawaii, thus impacting local businesses.

C. Concerns about Streamlined Sales Tax implementation in Hawaii.

1. **Adds Complexity.** Because Hawaii has a general excise tax imposed on the seller rather than a sales tax, which is imposed on the buyer, the provisions of the SSUTA do not fit neatly into Hawaii's general excise tax regime. Therefore, the SSUTA provisions need to be modified to take Hawaii's different tax structure into account.

In addition, to comply with the SSUTA's requirement that the State and each local taxing jurisdiction have only one rate, except in certain circumstances not applicable in Hawaii, the different tax rates applicable under Hawaii general excise tax law need to be removed from the general excise tax chapter and shifted into another taxing chapter. The creation of three new chapters also adds complexity to Hawaii's tax law and may prove to be another source of confusion to taxpayers.

In addition, whether the approach taken in the bill would be considered a "replacement tax" is an issue. It is also unclear at this time whether replacement taxes are permitted under the SSUTA.

2. **Provides Amnesty.** The SSUTA requires the State to provide amnesty to out-of-state sellers that may or may not have nexus with the State. The State will be giving up its

right to pursue these sellers for general excise tax on their operations in the State.

3. **Vendor Compensation.** The SSUTA requires the State to compensate out-of-state vendors who voluntarily participate in the SSUTA for collecting the Hawaii tax. However, in-state businesses that are obligated to pay the Hawaii tax are not compensated for collecting and paying the tax.
4. **Voluntary.** Currently, participation by sellers pursuant to the SSUTA is voluntary. While hundreds of companies have agreed to participate, Amazon.com and eBay have indicated that they will not participate at this time. Therefore, it is unclear how much potential revenue will be generated for Hawaii by participating in SSUTA.
5. **"Home Rule" Concerns.** Participation in SSUTA requires the State to annually certify to the national governing board that the state's laws are in compliance with SSUTA. Therefore, **any tax law changes in the future must meet the requirements of SSUTA** in order for the State to continue to comply with SSUTA. Therefore, **the State is limiting its ability to adopt legislation in favor of decisions made by a national governing board regarding a state's tax law.**

In addition, now that the City and County of Honolulu has enacted the county surcharge, the City and County of Honolulu must be bound to follow the SSUTA with respect to the surcharge.

6. **Appropriations.** The Department will need an appropriation to implement the SSUTA compliance, which, among other things, requires the development of a database of zip codes and tax rates. The Department is currently working on developing an accurate and comprehensive cost estimate for implementing this legislation. The complexity associated with updating the Department's current tax collection systems and the required labor and incidental costs require further analysis.
7. **Further Study.** The Department believes that further study is warranted on this issue. The general excise tax is a major revenue source for the State and any substantial revisions, such as those contained in this bill, should only be enacted after a thorough and thoughtful analysis can be done. In addition, time would also enable the Department to learn from other states' experiences with the SSUTA. Other states did not actually begin implementing SSUTA until late 2005. On April 1, 2008, eighteen states² will have become full members of SSUTA and begun implementing SSUTA. (Three new state recently became full member states: Arkansas, Wyoming, and Nevada; but these states were already participating as Associate Member states. In fact, since the agreement became effective in 2005, only Washington, Vermont and Rhode Island have been added to the list of original associate and full members.) If the State waits, it could learn from the problems the other states' experience. Some states remain cautiously guarded about

²The full member states are Arkansas, Indiana, Iowa, Kansas, Kentucky, Michigan, Minnesota, Nebraska, New Jersey, North Carolina, North Dakota, Oklahoma, Rhode Island, South Dakota, Vermont, West Virginia, Wyoming. Nevada becomes a full member state on April 1, 2008. Washington will become a full member on July 1, 2008.

implementing the SSUTA. For example, New York issued a report that cautioned joining the project because it was unclear whether the project would yield net benefits to taxpayers and local businesses. Again, further study of these paramount issues is advised.

C. General comments.

Delayed Effective Date—The delayed effective date of the bill is appreciated, but the delay may not be long enough to allow these changes to be fully integrated into the computer systems of the Department. A longer delayed effective date would give time for practitioners and businesses to adjust to these changes. When the corporate statutes were substantially revised, the effective date was delayed one year to allow professional associations, businesses, and practitioners sufficient time to analyze the changes in the law, prepare conferences, or other industry analysis. Given the challenges the Department would face integrating such large, wholesale changes into its operations, longer than two years may be more realistic of a time frame. The delayed effective date would also provide time to obtain approval from the National SSTP Governing Board to assure that Hawaii's amendments conform to the SSUTA. This is very important since Hawaii's general excise tax is not a sales tax.

Frequent Changes to the SSUTA Will Require Legislative Action. The legislature needs to be aware that the SSUTA is not a static document. It has undergone substantial and frequent changes since it was adopted on November 12, 2002. It has been amended 11 times.³ It has been amended 7 times since the SSUTA became effective on October 3, 2005. Each change requires member States to amend its law in order to remain in conformity with the SSUTA. The debate at the Governing Board meetings currently includes allowing intra-state origin based taxes, the extension of associate member status beyond the original deadline, and very relevant to this bill, the issue of using "replacement taxes" by States to circumvent the provisions of the SSUTA, such as New Jersey's fur tax.

D. Revenue diversion.

The Department cannot support GET revenue diversions. The Department is always cautious about policy that redirects general excise tax revenue away from the general fund and into specific special funds. The Department routinely opposes funding mechanisms such as this because the general excise tax represents over one-half of the State's overall operating revenue stream. The Department strongly prefers that a direct appropriation be the means for funding the programs of the Department of Education and the University of Hawaii so that the amount may be budgeted and prioritized just as any other program.

³ November 19, 2003, November 16, 2004, April 16, 2005, October 1, 2005, January 13, 2006, April 18, 2006, August 30, 2006, December 14, 2006, June 23, 2007, September 20, 2007, and December 12, 2007

IV. REVENUE IMPACT

The bill would increase revenues by about \$10 million annually.

The expansion of the GET exemption for blind, deaf, and disabled taxpayers would cost about \$500,000 annually.

In a study produced for the State's Auditor in April 2006, Dr. William Fox estimated that joining the SSUTA would provide Hawaii with about \$10 million in additional GET revenues annually. He reaffirmed his estimate in 2007.

The start-up costs for SSUTA conformance could be substantial.