



CERTIFIED PUBLIC ACCOUNTANTS

Tax News Flash

In This Acuity Update:

- **Legislative Update: Final Decking**

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We are now at the stage in our legislative session where bills need to be in final form. When a bill has been amended by both chambers of the Legislature, a conference committee of members of both chambers is appointed to resolve those differences. The Conference Committee can report out a conference draft, which then is voted on by both chambers and if approved the bill goes to the Governor. Or, the conferees could agree that the originating chamber would take back its disagreement. If that happens, the bill can go to the Governor as well. If neither of the above happens, the bill dies.

Once the Governor gets bills, he can sign them, veto them, or let them become law without signature. This process usually happens in June and July.

The status of the below bills is as of May 2, 2011. Titles in red show significant tax legislation that has died. Titles in light blue show that most or all of the bill is still alive and will probably be sent to Gov. Abercrombie.

General Excise Tax as a Trust Fund: Repeal Fails, But It Doesn't Get Worse

Act 155, SLH 2010, denies any taxpayer the benefit of any lower rate, credit, deduction, or income split, unless the taxpayer files a return within one year after the return is due. It would also impose personal liability against a responsible person in a business that fails to pay the general excise tax, just as the IRS does for businesses that withhold tax from employees and fail to pay that tax over to the government. See HRS §§237-9.3 and 237-41.5. This bill passed over opposition by business groups, nonprofits, and others.

This year, [SB 778](#) was introduced to repeal Act 155. The House, however, took the bill in a far different direction, with language that made it even more severe. The [Acuity Update of April 11, 2011](#) contains details.

The good news is that the bill has an effective date in 2030, absolutely needed conference committee intervention...and didn't get it.

SB 778 STATUS: DEAD

Employer Funded Pensions Safe for Now

[HB 1092](#) and [SB 570](#) used to have provisions taxing pensions of individuals whose federal adjusted gross income is above certain levels (\$100K single, \$150K head of household, \$200K

married filing jointly). [HB 1092](#) is now dead, and the Conference Draft of [SB 570](#) removed the provisions taxing pensions. So the taxation of pensions appears to be dead for this session.

HB 1092 STATUS: DEAD

SB 570 STATUS: CD 1 PENDING FINAL APPROVAL BY FULL HOUSE AND SENATE

State Tax Addback Lives; Itemized Deductions Also Capped

[SB 570](#) requires state taxes deductible for Federal purposes to be added back for individuals whose federal adjusted gross income is above certain levels (\$100K single, \$150K head of household, \$200K married filing jointly). Although it may not be much consolation, add-back is required by most states.

[SB 570](#) also imposes a ceiling on the amount of itemized deductions that will be allowed (\$25K single, \$32.5K head of household, \$50K married filing jointly) from 2011 through 2015.

SB 570 STATUS: CD 1 PENDING FINAL APPROVAL BY FULL HOUSE AND SENATE

Pesky GET Exemptions to Get Swatted

Among the several bills that would temporarily kill several exemptions now in the general excise tax, use tax, and the public service company tax, one winner has emerged: [SB 754](#) kills the following exemptions from July 1, 2011, to June 30, 2013. In the following full list, we list the disallowed exemptions in order of their HRS section number; in **bold** are the ones likely to have more widespread application.

- **The deduction by a contractor for amounts paid to a subcontractor (HRS §237-13(3)(B)).**
- The deduction by Federal cost-plus contractors for reimbursed materials, plant, and equipment (HRS §237-13(3)(C)).
- Gross receipts of mobile telecommunications service providers selling to other providers (HRS §237-13(6)(D)).
- **The partial deduction a sublessor gets for lease rent paid for the space subleased (§237-16.5).**
- Gross receipts of a tax-exempt organization for conventions, conferences, trade show exhibits, or display spaces (HRS §237-16.8). The bill takes some pains to emphasize that the tax treatment of other income earned by a tax-exempt organization is not affected.
- Gross receipts of sugar cane producers (HRS §237-24(14)).
- Gross receipts for loading, transportation, and unloading of agricultural commodities shipped interisland (HRS §237-24.3(1)).

- Gross receipts for selling liquor, tobacco products, and food to common carriers engaged in interstate or foreign commerce (HRS §237-24.3(2)).
- Gross receipts from loading or unloading of cargo from watercraft or aircraft (HRS §237-24.3(4)(A)) – BUT stevedoring and related services, as defined in HRS §382-1, furnished to a company by its wholly owned subsidiary continue to be exempt.
- Gross receipts from tugboat and towage services (HRS §237-24.3(4)(B)).
- Gross receipts from transportation of pilots or governmental officials to ships, barges, or vessels offshore; rigging gear; checking freight and similar services; standby charges; and use of moorings and running mooring lines (HRS §237-24.3(4)(C)).
- Gross receipts of labor organizations from real property leases (HRS §237-24.3(10)).
- Rent for aircraft or aircraft engines used for interstate air transportation (HRS §237-24.3(12)).
- Gross receipts of stock, bond, and commodity exchanges and exchange members (HRS §237-24.5).
- High technology research and development grants (HRS §237-24.7(10)).
- Gross receipts from servicing and maintenance of aircraft or construction of an aircraft service and maintenance facility (HRS §237-24.9).
- **Sales of tangible personal property to the Federal Government (HRS §237-25).**
- Gross receipts of petroleum product refiners from other refiners (HRS §237-27).
- Gross receipts related to air pollution control facilities (HRS §237-27.5) – UNLESS the facility has a certificate of exemption valid on July 1, 2011.
- Gross proceeds of shipbuilding and ship repair (HRS §237-28.1).
- Receipts of telecommunications common carriers from call center operators for interstate or foreign telecommunications services (HRS §237-29.8).
- **Gross proceeds of qualified activities conducted in enterprise zones (unless already qualified by DBEDT as of July 1, 2011), including gross proceeds of contractors who construct within such zones (HRS §209E-11).**
- Import of aircraft for leasing or use in air transportation (HRS §238-1(6)).
- Import of oceangoing vehicles for use in interisland transportation (HRS §238-1(7)).
- Import of materials, parts, or tools for use in aircraft service or maintenance (HRS §238-1(8)).

- Import of liquor or tobacco products to be sold to a person or common carrier for consumption out of state (HRS §238-3(g)).
- Use of certain vessels constructed prior to July 1, 1969 (HRS §238-3(h)).
- Use of an air pollution control facility (HRS §238-3(k)).

The full 4% retail rate (but not the county surcharge) applies to the previously exempt amounts.

The bill would take effect on July 1, 2011, and expire on June 30, 2013.

There is a provision grandfathering all exemptions for income earned under a binding written contract in force on July 1, 2011, but only if that contract does not permit the passing on of increased rates of taxes. (This provision is similar to the grandfather clause that applied to the county surcharge when it went into force on January 1, 2007. See HRS §237-8.6(c).)

HB 799 STATUS: DEAD

SB 754 STATUS: CD 1 PENDING FINAL APPROVAL BY FULL HOUSE AND SENATE

HB 793 STATUS: DEAD

And Let's Wipe Out Those Pesky Bugs, Too

HB 865 would increase the service fee for the inspection, quarantine, and eradication of invasive species from 50 cents to 75 cents for every 1,000 pounds of freight brought into the state.

HB 865 STATUS: HOUSE AGREED TO SD 2; BILL ENROLLED TO GOVERNOR

Transient Tax Hike Falters; "Flat Rate" Tax on Comps and Packages Instead

Earlier bills proposed to amend the transient accommodations tax on time share occupants (the "TOT") by hoisting the rate 2 percentage points to mirror the transient accommodations tax increase on hotels enacted last year, and by tripling the TOT tax base.

The Conference Draft of **SB 1186** torpedoed both of these ideas. Instead, the bill imposes a \$10 per night flat rate TAT on "every transient accommodation that is furnished on a complimentary or gratuitous basis, or otherwise at no charge, including transient accommodations furnished as part of a package." This language could be problematic. Could a room be let out at a nominal amount (\$1 a night, perhaps) on which the TAT would be less than ten cents, as opposed to ten dollars? When a hotel operator furnishes transient accommodations as part of a tour package that involved other things, such as a meal and room package, what is the tax now? Under prior law, the operator paid tax on the amount allocated to the accommodations. Under this bill, does a flat rate of \$10 now apply?

SB 1186 STATUS: CD 1 PENDING FINAL APPROVAL BY FULL HOUSE AND SENATE

Rental Vehicle Tax Drops; Facility, Registration, and Weight Tax Hikes Alive

This year, the Department of Transportation submitted bills to hike various fees and taxes.

- **SB 1324** (TRN-8) would have made the \$3 per day tax on rental motor vehicles permanent. This bill died. The tax will drop back down to \$2 per day on September 1, 2011.

- [SB 1327](#) (TRN-13) allows DOT to increase the passenger facility charges – without a public hearing. This bill is alive.
- [SB 1328](#) (TRN-14) would increase the state motor vehicle registration fees by \$20. This bill is also alive and well, and would take effect on July 1, 2011.
- [SB 1329](#) (TRN-15) would increase the state motor vehicle tax by 1 cent per pound (typically, cars weigh between 3,000 and 7,000 pounds). This bill would also take effect on July 1, 2011 if approved.

SB 1324 STATUS: DEAD

SB 1327 STATUS: SENATE AGREED TO HD 1; BILL ENROLLED TO GOVERNOR

SB 1328 STATUS: CD 1 PENDING FINAL APPROVAL BY FULL HOUSE AND SENATE

SB 1329 STATUS: CD 1 PENDING FINAL APPROVAL BY FULL HOUSE AND SENATE

Adoption of Federal Tax Changes – or Lack Thereof

Every year, the Department of Taxation submits, and the Legislature considers, a bill that would adopt some or all of the Federal changes that took place in the past year. This year's bill (known as TAX-01) is no different. It proposes that Hawaii decouple from some of these federal changes. The bill still alive ([HB 1089](#)) proposes nonconformance in these areas:

- Limitation on itemized deductions, sometimes known as the “itemized deduction phaseout” under IRC §68 (Federal removed the phaseout beginning in 2010, State keeps it, but at 2009 threshold levels).
- Itemized deduction for general sales taxes (Federal allows a taxpayer to deduct sales taxes instead of income taxes, State allows a deduction for income taxes only...and might not even allow that)
- Section 179 expensing (State only allows \$25,000, with a phaseout beginning at \$200,000 worth of section 179 property)

HB 1089 STATUS: CD 1 PENDING FINAL APPROVAL BY FULL HOUSE AND SENATE

Penalty Stacking Relief Fails; Returns Still Due on the 20th

Act 166, Session Laws of Hawaii 2009, imposed new tax penalties similar to penalties imposed under federal law. However, while federal law prohibits the stacking of penalties, Act 166 did not. Indeed, we have seen a case where an auditor assessed *70% penalties* (25% failure to file + 25% negligence + 20% substantial underpayment) against a small business owner. [SB 1356](#) was supposed to remove the stacking. However, there will be no change this year; the bill has died.

In addition, [SB 1356](#) was to re-institute the old rule about returns being due on the last day of the month following the taxable period for general excise, transient accommodations, use, fuel, tobacco, liquor, and insurance premium taxes. [HB 1300](#), which requires the Department to establish a system to allow taxpayers to file all tax returns, applications, reports, and similar documents electronically at no cost to the taxpayer, also reestablishes the end of the month as the deadline for filing and payment of various taxes. Both bills are now dead, so the due dates for these returns will stay as they were.

[SB 1356 STATUS: DEAD](#)

[HB 1300 STATUS: DEAD](#)

Sun Credit Continues to Shine; New Satellite Tax Lost in Space; QHTB Stock Gains Remain Exempt

[SB 756](#) takes the renewable energy technologies credit, which now grants benefits to those who install solar or wind property, and would sunset the credit on January 1, 2015. In addition, it would delay any payouts for refundable tax credits claimed in 2012 to July 1, 2013. In the meantime DBEDT would be tasked with completion of an assessment on the effectiveness and ongoing need for the credit.

[SB 756](#) also imposes a tax on direct broadcast satellite providers in addition to the general excise tax. Some testifiers supporting this bill were pushing it as a way to level the playing field with land-line TV providers that are subject to additional fees and regulatory requirements.

Finally, the bill would have repealed the income tax exclusion in HRS section 235-9.5 for income derived from qualified high technology business (QHTB) stocks or stock options.

Renewable energy technology advocates, direct broadcast satellite providers, and QHTB stock or option holders can breathe a little easier now; this bill is dead.

[SB 756 STATUS: DEAD](#)

Cold Water Thrown on Solar and Wind Enterprise Zones

Under the most recent version of [HB 306](#), any renewable energy facility located in an enterprise zone ([current maps available here](#)) would be eligible for a rebate of income and SUI taxes attributable to operations in the zone. It also could have been eligible for an exemption from general excise taxes unless, of course, some of the other legislation we are reviewing here gets enacted. This bill also failed to make it out of conference.

[HB 306 STATUS: DEAD](#)

R&D Extension Fails; New Markets Credit Craters; Relief for Potable Water Companies Dries Up

[HB 1642](#) and [SB 753](#) would have extended the refundable Tax Credit for Research Activities (HRS §235-110.91) another five years to December 31, 2015. The bills are both dead, and so is the TCRA; it sunset on December 31, 2010.

[SB 831](#) would have established a state credit paralleling the federal New Markets tax credit (IRC §45D). It was to be 20% of the federal credit, but only projects in Hawaii would be eligible. This bill also died.

Additional language in [SB 831](#) would have exempted federal IRC §501(c)(12) companies ([What are these?](#)) supplying potable water from the reach of state income and general excise taxes.

[HB 1642 STATUS: DEAD](#)

[SB 753 STATUS: DEAD](#)

[SB 831 STATUS: DEAD](#)

Beefed-Up Movie/TV Credit for Infrastructure on Cutting Room Floor

[SB 318](#) would have added a credit for a qualified infrastructure project to the existing production credit (HRS §235-17). The goal was to have a production or post production facility built in the State, as there is none now.

The bill also would have established a Digital Media Production Infrastructure Tax Credit for investment expenditures made by a taxpayer for qualified digital media infrastructure projects within a Digital Media Enterprise Subzone, which was contemplated as an area around UH-West Oahu.

The bill failed to move out of Conference Committee.

[SB 318 STATUS: DEAD](#)

GET Pyramiding Relief for Related Entities Mummified by Committee

Almost 20 years ago, the Hawaii Supreme Court told us that the general excise tax applies whenever one company does something for another one, even if the two companies happen to be related. The Legislature reacted a few years later by exempting a limited amount of intercompany charges: charges for administrative, legal, and accounting services and interest charges (HRS §237-23.5(a)) and reimbursements for “common paymaster” charges where, say, one employee works for corporations A and B but one corporation cuts the employee’s paycheck and the other one reimburses part of that cost (§237-23.5(b)). Charges for information technology services between related entities were added to the exemption by the landmark technology incentive law, Act 221 of 2001. Nevertheless, the exemption has its limits. The related company exemption does not apply to so-called line services such as marketing and repairs, and the common paymaster exemption technically applies only to corporations because of restrictions in the federal regulation (Treas. Reg. §31.3121(s)-1(b)) the law incorporates by reference.

Both [HB 848](#) and [SB 1107](#) would have addressed these limitations. [HB 848](#) would have exempted amounts paid to a related or indirectly related management entity, taking into account attribution under section 267, IRC, for managing the business of the affiliates. [SB 1107](#) would have exempted “amounts received by a related entity, as defined under section 237-23.5, taking into account the attribution rules under section 267, IRC,” for employee salary and benefit charges that are reimbursed by the related entity. Both bills died in conference.

[HB 848 STATUS: DEAD](#)

[SB 1107 STATUS: DEAD](#)

Dot-com Nexus: Reboot Fails

When sellers of goods and services that are not in Hawaii attempt to sell in Hawaii, the U.S. Supreme Court has said that our state is without power to tax those sellers unless they have

“nexus” with our state. [SB 1355](#) is an attempt to define what that nexus is. In the bill, nexus includes physical presence, meaning having persons or property within the state, or an independent contractor working solely for the putative taxpayer to solicit business within the state. The bill also presumes nexus to exist when the putative taxpayer pays a local seller to directly or indirectly refer potential customers, including by a link on the local seller’s internet website. The current version of the bill requires sellers who don’t pay general excise tax on sales to Hawaii residents to supply the names and addresses of those residents and the dollar amount of all such sales to the Department, and if they do so they would be relieved of any duty to pay tax. This bill didn’t make it out of conference, so click-thru nexus is dead for now.

SB 1355 STATUS: DEAD

The Streamlined Sales Tax (Dis)Agreement

Hawaii, like many other states, has been missing out on collecting GET or Use Tax on goods sold to residents by out-of-state sellers that are outside of the reach of the State’s taxing jurisdiction. Although the tax does indeed apply to purchasers of such goods, it is not cost effective for the State to chase multitudes of small purchasers. Thus, there is interest in the increased collection from remote sellers that is supposed to come with joining the Streamlined Sales Tax Project (SSTP), a national initiative by many similarly situated states. In 2003, the State of Hawaii became a participant in the SSTP. A further act in 2005 advanced the State’s efforts to comply with the terms and conditions of the conforming legislation reflected in the SSTP model agreement and act. However, there is currently a large issue: The SSTP requires a maximum of one tax rate per state, but the GET and Use Tax now have two major rates, namely the wholesale and retail rates. Legislation to split off the wholesale from the retail rates was passed in 2009 but was vetoed by the Governor, who cited concerns with ceding control to the SSTP governing body, providing amnesty, payment of a collection fee to an out-of-state vendor, and an ambiguous effective date. The SSTP rate split-off legislation is now in [HB 1183](#), on which conferees were unable to reach agreement.

HB 1183 STATUS: DEAD

Information on these and other bills moving through the Legislature may be obtained from the Legislature’s web site, www.capitol.hawaii.gov. Or click on the links in this message.

If you have questions about any of these news items,
your client service team at Acuity can bring you the resources that you may need.
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