



CERTIFIED PUBLIC ACCOUNTANTS

Tax News Flash

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Expanded 1099 Requirements About to Die

In a prior [Acuity Tax News Flash \(January 6, 2011\)](#), we reported on expanded requirements to report payments for goods or to corporations, and to report expenses of residential rental real estate. The residential rental requirements were effective January 1, 2011, and the rest would become effective January 1, 2012.

On April 5, the United States Senate by a vote of 87-12 approved H.R. 4, the "Comprehensive 1099 Taxpayer Protection and Repayment of Exchange Subsidy Overpayments Act of 2011." The measure, which retroactively repeals those expanded Form 1099 information reporting rules, was passed by the House on March 3 by a vote of 314-112. H.R. 4 next goes to the White House, and President Obama is expected to sign it.

H.R. 4 offsets the anticipated revenue cost. The Affordable Care Act provides for a premium assistance credit to help lower-income individuals acquire affordable health insurance coverage. Under the bill, more individuals would have to repay all or part of the credit if their income falls between 100% and 400% of the federal poverty line, based on their most recently filed tax returns.

Hawaii E-Payment Requirements Broadened

Under HRS §231-9.9, the Department of Taxation has the authority to require any taxpayer owing more than \$100,000 a year of any particular tax type to pay that tax by electronic funds transfer (EFT). In [Announcement 2011-4](#), the Department announced that it will be expanding the list of tax types for which EFT payment is required. Effective October 1, 2011, EFT payments will also be required for:

- Fuel Tax;
- Cigarette Tax and Tobacco Tax;
- Liquor Tax;
- Franchise Tax; and
- Public Service Company (PSC) tax.

The Department will be mailing notices to affected taxpayers.

Legislative Update: Second Crossover

We previously reported on a number of bills that were being considered by our legislature. Those bills were poised to cross over into the non-originating chamber. At this point in the legislative session, the non-originating chamber has considered, and in almost all cases has amended, those bills. In a number of cases, the amendment consisted of gutting the substance of a bill and inserting the language of another.

Most of these bills will be disagreed to by the originating house, and a conference committee of members of both chambers will be 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. All of this must happen by the end of April if a bill is to pass.

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 April 10, 2011.

General Excise Tax as a Trust Fund, Gone Wrong

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, has taken the bill in a far different direction, with language that makes it even more severe:

- Notwithstanding any other law, NO general excise benefit (exemption, deduction, or lower rate) is allowed unless a person “[o]wes taxes in an amount less than fifty per cent of total general excise tax liability owed for the taxable year.” We don’t know what this means, but if taken literally no one who owes taxes can qualify for any exemption, deduction, or lower rate.
- Personal liability is imposed for “[a]ny amount of gross excise tax liability not paid.” That means if your company gets audited, they assess tax, you don’t agree, and you take them to court without paying the disputed liability (which is perfectly legal), then they can collect the amount from your personal assets. Even if you win in court later, your personal credit may be severely damaged by the enforced collection.

The good news is that the bill now has an effective date in 2030 so it will need conference committee intervention.

SB 778 STATUS: HD 1 PENDING CROSSOVER VOTE BY FULL HOUSE

The Abercrombie State of the State Ideas – Where Have They Gone?

Our last legislative update started with a bill sponsored by the Abercrombie Administration (also known as TAX-10) containing a number of revenue raisers the Governor mentioned in his State of the State address. One version of the bill is still alive, and features of it have found their way into other vehicles.

- Employer funded pensions that are now exempt will become taxable.

[HB 1092](#) only excludes the first \$100,000 of pensions. [SB 570](#) taxes all pensions of individuals whose federal adjusted gross income is above certain levels (\$100K single, \$150K head of household, \$200K married filing jointly).

- The amount of state tax will become nondeductible, which means it will be added back to state taxable income.

[HB 1092](#) requires addback for individuals whose federal adjusted gross income is above certain levels (\$75K single, \$112.5K head of household, \$150K married filing jointly). [SB 570](#) kicks in at different levels (\$100K single, \$150K head of household, \$200K married filing jointly).

[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.

- The state income tax exclusion for copyright royalties and similar income will go away, meaning it will be taxable the same as it is for federal purposes.

This provision appears to be dead—for now.

- The transient accommodations tax on time share occupants (the “TOT”) will be hoisted 2 percentage points to mirror the transient accommodations tax increase on hotels enacted last year.
- The TOT tax base will be tripled.

The TOT hike is alive and well in [SB 1186](#), but the tax base modification seems to have fallen to the cutting room floor. In its place is a provision that imposes a \$10 per night minimum TAT on complimentary accommodations, including accommodations furnished as part of a tour package or points program, or as a reward for purchasing other goods or services.

[HB 1092 STATUS: SD 2 PENDING CROSSOVER VOTE BY FULL SENATE](#)

[SB 570 STATUS: HD 1 PENDING CROSSOVER VOTE BY FULL HOUSE](#)

[SB 1186 STATUS: HD 1 PENDING CROSSOVER VOTE BY FULL HOUSE](#)

Transportation Gets Pricier

This year, the Department of Transportation submitted bills to hike various fees and taxes. [SB 1324](#) (TRN-8) would make the \$3 per day tax on rental motor vehicles permanent. [SB 1327](#) (TRN-13) allows DOT to increase the passenger facility charges – without a public hearing. [SB 1328](#) (TRN-14) would increase the state motor vehicle registration fees by \$20. [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). All of these bills are alive and well.

[SB 1324 STATUS: HD 2 PENDING CROSSOVER VOTE BY FULL HOUSE](#)

[SB 1327 STATUS: HD 1 PENDING CROSSOVER VOTE BY FULL HOUSE](#)

[SB 1328 STATUS: HD 2 PENDING CROSSOVER VOTE BY FULL HOUSE](#)

[SB 1329 STATUS: HD 2 PENDING CROSSOVER VOTE BY FULL HOUSE](#)

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 section 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 because of other bills)
- Section 179 expensing (State only allows \$25,000, with a phaseout beginning at \$200,000 worth of section 179 property)

HB 1089 STATUS: SD 1 PENDING CROSSOVER VOTE BY FULL SENATE

Don't Kick People When They're Already Down! And Give Us 10 More Days of Slack...

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. Ouch! [SB 1356](#) is supposed to remove the stacking, as it prohibits multiple penalties under sections 231-36, 231-36.4, 231-36.6, and 231-36.8. However, *it would have no effect* on the scenario described above, because those facts involve penalties under sections 231-36.6, 231-39(b)(1), and 231-39(b)(2)(A). Thus, this appears to be a case where the concept is fine but the devil is in the details!

In addition, [SB 1356](#) responds to taxpayer complaints about the due date of periodic tax returns being moved up to the 20th of the month. It re-institutes 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.

SB 1356 STATUS: HD 1 PENDING CROSSOVER VOTE BY FULL HOUSE

HB 1300 STATUS: SD 2 PENDING CROSSOVER VOTE BY FULL SENATE

Sunset of Sun Credit; Tax Lost in Space

[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 repeals the income tax exclusion in HRS section 235-9.5 for income derived from qualified high technology business (QHTB) stocks or stock options.

SB 756 STATUS: HD 1 PENDING CROSSOVER VOTE BY FULL HOUSE

Hot and Cold Enterprise Zones

[HB 306](#) was originally proposed as a measure to make technical, clarifying amendments to the Hawaii inheritance and transfer tax (including the generation-skipping tax).

But, as the title of the bill is “Relating to Taxation,” anything relating to taxation is fair game. Thus, the Senate Ways and Means Committee inserted the text of [SB 1164](#), which had proposed to add renewable energy production primarily for sale to a public utility, and a seawater district cooling system, to the list of activities eligible for Enterprise Zone benefits. [SB 1164](#) had crossed over into the House and had made it past a joint hearing of two subject-matter committees, but House Finance failed to move it.

Under the new language 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 might be eligible for an exemption from general excise taxes unless, of course, some of the other legislation we are reviewing here gets enacted.

[HB 306 STATUS: SD 2 PENDING CROSSOVER VOTE BY FULL SENATE](#)

R&D Extension; New Markets

[HB 1642](#) and [SB 753](#) would extend the refundable Tax Credit for Research Activities (HRS §235-110.91) another five years to December 31, 2015. Both versions require the claimant to complete an extensive online survey. The Senate Bill removes the current requirement that the Department of Taxation certify the credit (currently Form N-319A).

[SB 831](#) would establish a state credit paralleling the federal New Markets tax credit (IRC §45D). It would be 20% of the federal credit, but only projects in Hawaii would be eligible. The credit would be nonrefundable but could be allocated between partners in a partnership without regard to IRC §704(b)(2), just like how the Qualified High Technology Business investment credit used to be. This credit would also be usable against the bank franchise and insurance premium taxes. For individuals, the passive credit limitations would apply.

Additional language in [SB 831](#) would exempt 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: SD 1 PENDING CROSSOVER VOTE BY FULL SENATE](#)

[SB 753 STATUS: HD 2 PENDING CROSSOVER VOTE BY FULL HOUSE](#)

[SB 831 STATUS: HD 1 PENDING CROSSOVER VOTE BY FULL HOUSE](#)

Beefing Up the Movie/TV Credit in Pursuit of Infrastructure

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

In addition, it establishes 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 is then defined as a geographic area located within an unspecified radius of a University of Hawaii campus that is within an existing enterprise zone; provided that from July 1, 2011, to June 30, 2013, establishment of a Digital Media Enterprise Subzone is limited to an area within an unspecified radius of UH-West Oahu.

[SB 318 STATUS: HD 2 PENDING CROSSOVER VOTE BY FULL HOUSE](#)

More GET Pyramiding Relief for Related Entities?

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](#) address these limitations not by amending section 237-23.5, but by adding another paragraph to section 237-24.7. [HB 848](#) exempts 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](#) exempts “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 have their own flaws – the House bill doesn’t really define what related or indirectly related entities are, and the Senate bill’s definition is confusing because the definition of related entities in existing law refers to IRC sections 1504 and 1563, which have their own attribution rules that are different from IRC section 267.

[HB 848 STATUS: SD 1 DISAGREED BY HOUSE](#)

[SB 1107 STATUS: HD 2 PENDING CROSSOVER VOTE BY FULL HOUSE](#)

We Have So Many Pesky GET Exemptions...

The House’s plan to kill a large list of GET exemptions was contained in [HB 799](#) and sent over to the Senate. The Senate’s Committee on Economic Development and Technology killed that bill, but it didn’t stay dead long. The House gutted [SB 754](#) (an unrelated bill) and put a version of [HB 799](#) inside it. In the meantime, the Senate Ways and Means Committee wanted to put on the table a bill to raise the GET rate, and published a proposed redraft of [HB 793](#) that contained provisions killing GET exemptions and raising the rate, but adding provisions that would address the regressivity of the tax. After an intense hearing in the Capitol Auditorium and Chair David Ige recommended deferring the bill to fix it some more, Sen. Donovan Dela Cruz moved for an immediate vote on adopting the draft with ONLY the exemption-killing provisions. This passed over the Chair’s objection.

So we now have two bills that would temporarily kill several exemptions now in the general excise tax, use tax, and the public service company tax. Under both bills, the full 4% retail rate (but not the county surcharge) applies to the previously exempt amounts. [SB 754](#) kills the following exemptions, among others, from July 1, 2011, to June 30, 2013. [HB 793](#) kills exemptions from July 1, 2012, to June 30, 2015.

- The deduction by a contractor for amounts paid to a subcontractor (HRS §237-13(3))
- The partial deduction a sublessor gets for lease rent paid for the space subleased (§237-16.5)
- Sales of tangible personal property to the Federal Government (HRS §237-25) [[SB 754](#) only]

- Several exemptions under the general excise and use taxes relating to transportation, such as stevedoring, tugboat, and towage services (§237-24.3(4)), rent for aircraft engines or importation of those engines or parts (§§237-24.3(12), 238-1), and commercial aircraft operation (§237-24.9)
- The exemption for gross proceeds of shipbuilding and ship repair (§237-28.1)
- The exemption for gross proceeds of qualified activities conducted in enterprise zones (unless already qualified by DBEDT as of Jan. 1, 2012), including gross proceeds of contractors who construct within such zones

Although [HB 799](#) had contained a provision grandfathering all exemptions for income earned under a binding written contract in force on July 1, 2011, neither of these bills appears to contain a generally applicable grandfather clause.

HB 799 STATUS: DEAD

SB 754 STATUS: HD 1 PENDING CROSSOVER VOTE BY FULL HOUSE

HB 793 STATUS: SD 1 PENDING CROSSOVER VOTE BY FULL SENATE

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: SD 2 PENDING CROSSOVER VOTE BY FULL SENATE

Dot-com Nexus: Click Through and Be Taxable (Redux from 2009)

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.

A couple of years ago, a similar bill, HB 1405 (2009), was sent to Governor Lingle. Many of the click-through companies, such as Amazon.com and Overstock.com, made it very clear that their Hawaii affiliates would immediately be terminated unless the bill was vetoed. The Governor [did veto the bill](#), and the veto was not overridden. This year’s version of the bill does not seem to strengthen the State’s position by giving presumptive taxpayers a “reporting option.” If under the U.S. Constitution the State of Hawaii is precluded from using its police power to impose a tax upon a presumptive taxpayer, how could it be able to use that same police power to force it to tattle on local customers?

SB 1355 STATUS: HD 2 PENDING CROSSOVER VOTE BY FULL HOUSE

The Streamlined Sales Tax 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](#).

HB 1183 STATUS: SD 1 PENDING CROSSOVER VOTE BY FULL SENATE

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.

Please do not hesitate to contact your client service team for more information or Tom Yamachika at thomas.yamachika@acuityllp.com



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