

Hawaii Tax Developments



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Presented By Accuity LLP

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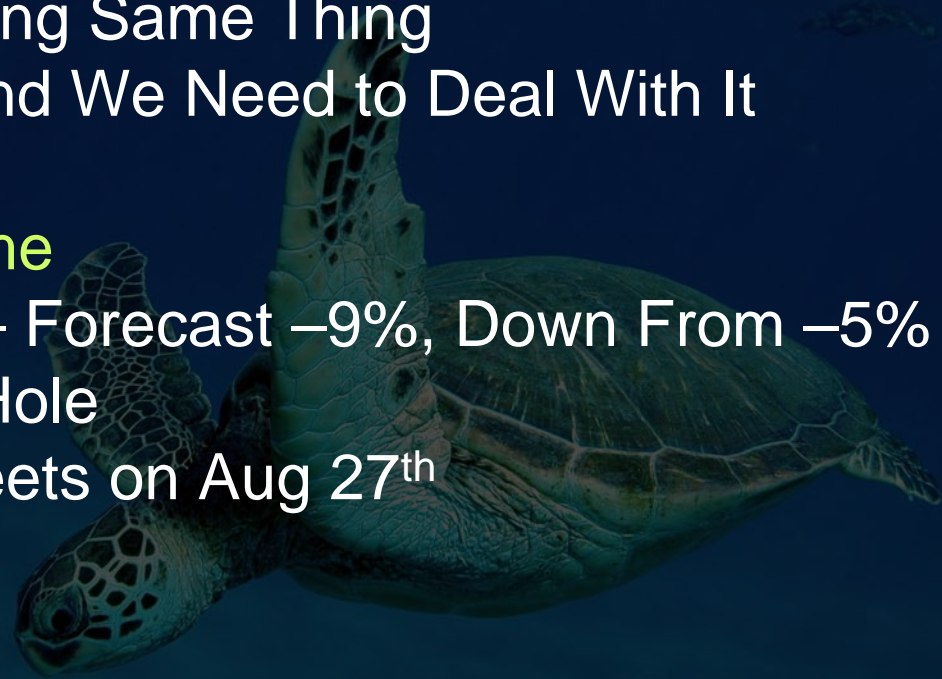
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- **Higher Taxes**

- “Temporary” ?!?!
- Most States Doing Same Thing
- It’s Law Now, and We Need to Deal With It

- **More Action to Come**

- COR May 28th – Forecast –9%, Down From –5%
 - \$185 Million Hole
 - COR Next Meets on Aug 27th



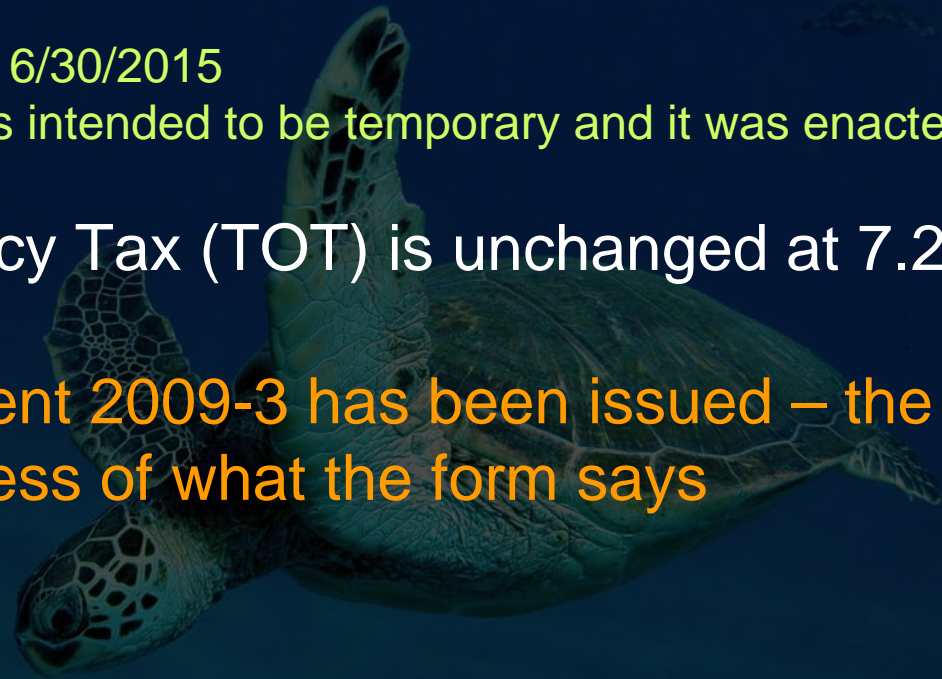
- New Rates effective 1/1/2009 – **We Are Now #1!**
 - \$300K-\$350K (MFJ) at 9%
 - \$350K-\$400K at 10%
 - \$400K+ at 11%
- Single – new rates start at \$150K
- HOH – new rates start at \$225K
- **Capital gains rate is unchanged at 7.25%**
- Standard deduction raised and personal exemption goes up (\$1040 to \$1144) – BUT effective 1/1/2011
- Entire bill is repealed 12/31/2015

• Important Takeaways!

- Estimates not based on 100% PY must be redone
- No penalty for payments due before 8/6/2009 if the ONLY reason for underpayment was the tax increase (Announcement 2009-4)
- 3Q and 4Q estimates (due Sept. and Jan.) must consider the new rates (also affected by personal exemption phaseout in Sp. Sess. Act 14)
- We do not expect the programming on DOTAX computers to change so if you get penalty notices be prepared to argue
- This does not affect the 90% Rule on extensions
 - Extension will be revoked if 90% of tax due is not paid in by 4/20/2010

- **New Rates effective 7/1/2009**
 - **Top rate on single-family or condo unit ineligible for H/O exemption**
 - Was 35 basis points
 - Now 125 basis points for Actual and Full Consideration > \$10M
 - **Top rate on all other property (owner occupant + commercial)**
 - Was 30 basis points
 - Now 100 basis points for AFC > \$10M
- **“Cliff” application – if you hit a higher bracket the highest rate is applied to the WHOLE amount**
 - Investor property selling for \$3,999,999
 - Tax is ~\$24,000
 - Investor property selling for \$4,000,000
 - Tax is \$34,000

- Effective 7/1/2009: 8.25%
- Effective 7/1/2010: 9.25%
- Theoretically this ends on 6/30/2015
 - But the TAT itself was intended to be temporary and it was enacted in 1986.
- Transient Occupancy Tax (TOT) is unchanged at 7.25%
- Note: Announcement 2009-3 has been issued – the new rates apply regardless of what the form says



- Cigarettes under current law:
 - 10¢ per stick now
 - 11¢ on 9/30/2009
 - 12¢ on 9/30/2010
 - 13¢ on 9/30/2011
- Under new law:
 - 13¢ per stick on 7/1/2009
 - 14¢ per stick on 7/1/2010
 - 15¢ per stick on 7/1/2011
- “Little cigars” are now taxed as cigarettes.
- Other tobacco products:
 - Currently taxed at 40% of wholesale price
 - Increases to 70% of wholesale price eff. 9/30/2009
 - Cigars taxed at 50% of wholesale price eff. 9/30/2009
- Transition issues!
 - The repeal of the OLD rate is effective immediately
 - The NEW rate has an effective date
 - Does this mean that there is a period for which there is no tax?



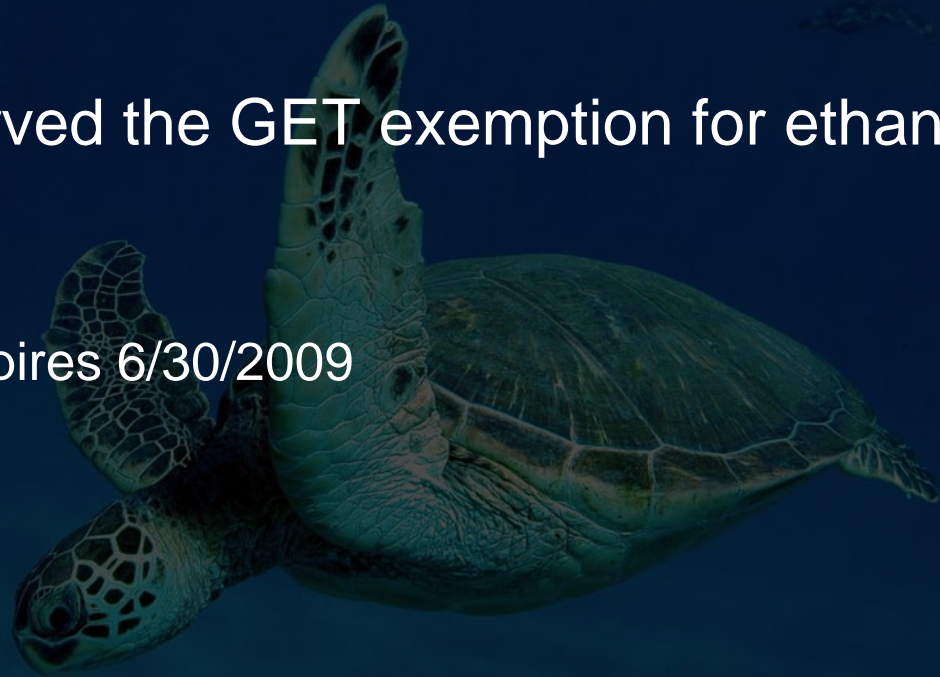
- Transition Issues Resolved (Announcement 2009-5):
- “Little Cigars”
 - 40% of wholesale price up to 5/7/2009
 - NO TAX 5/8/2009 to 9/30/2009
 - 11¢ on 10/1/2009
- Cigars
 - 40% of wholesale price up to 5/7/2009
 - NO TAX 5/8/2009 to 9/29/2009
 - 50% of wholesale price on 9/30/2009
- Other tobacco products (other than cigarettes):
 - 40% of wholesale price up to 5/7/2009
 - NO TAX 5/8/2009 to 9/29/2009
 - 70% of wholesale price on 9/30/2009



- If you owe them, you pay 8% (no change)
- If they owe you, they pay 4% (used to be 8%)
- Effective for refund claims made on or after 1/1/2009
- **Make sure the correct taxpayer is filing returns!**
 - Doctor creates Professional Corporation
 - Doctor forgets to tell insurers that the Corp. has been formed
 - Doctor reports income for GET purposes under Corp.
 - DOTAX gets 1099-MISC with Doctor's SSN (instead of corporation's FEIN)
 - DOTAX issues assessment against Doctor for unpaid GET, with massive penalties
 - It may have been a "wash" before, but isn't now!

- If you are incorporated or domiciled in Hawaii
- If you are exposed to another State's premium tax and that tax is more than what the State charges its own companies (incorporated or domiciled in that State)
- Hawaii will give you a credit for the difference
- **Act concerns the time limit for claiming this credit**
 - Formerly three years
 - Effective 7/1/2009, the credit must be claimed within 12 months after the end of the taxable year...similar to most other Hawaii credits
 - CY 2007 or CY 2006 need to be looked at now, and any claims need to be in the door by 6/30/2009

- Environmental Response Tax hiked to \$1.05 per barrel of oil (was \$0.05)
- Former draft preserved the GET exemption for ethanol blended fuel.
 - That went away...
 - GET exemption expires 6/30/2009
- Effective 7/1/2009



- QHTB Investment Credit for investments 5/1/2009+
 - Mandatory 1:1 (no special allocations, no 2:1)
 - Mandatory 35-25-20-10-10 (no front loading)
 - Cannot offset more than 80% of liability
 - No carryover
 - Department said 5/1/2009+ investment credits are used first
 - Applies to Income, Franchise, and Premium Taxes
- Wired Credit for expenditures 5/1/2009+
 - No Credit
- Capital Goods Excise Tax Credit for property P/I/S 2009
 - No Credit for property P/I/S 5/1/2009+
 - Dept. said property P/I/S 1/1/2009-4/30/2009 is still eligible

- Preparer penalties (similar to IRC §6694)
- Penalties for promoting abusive tax shelter (~IRC §6700)
- Penalties for erroneous claims for refunds or credits (~IRC §6676)
- Additional penalty of 20% for substantial understatement
- Six year statute of limitations on assessment when there is a substantial omission
- No need to have court pre-determine falsity or fraud for unlimited statute of limitations on assessment of tax; but burden of proof on State
- Department of Taxation authorized to undertake temporary rulemaking; rules to be effective for 18 months
- Failure to withhold is a criminal offense (class C felony)
- **New 15 year collection statute of limitations for most tax types; previously unlimited**

- DOTAX to implement an Appeals-type program
- DOTAX must adopt rules providing examples and safe harbors to explain new penalty provisions
- Tax advice shall be disclosed to the public (~IRC §6110) – seems to override existing statute (HRS §231-19.5)
- DOTAX must provide a taxpayer with a closing audit letter at the conclusion of a tax audit

Note: white provisions (previous page) were asked for by Department of Taxation. Green provisions (both pages) were added by the Legislature.

- No surprises
- Although a previous draft attacked the exemption for pensions > \$50K, pensions are spared this time
- Will not pick up:
 - Bonus depreciation
 - Enhanced §179
 - Federal disaster relief
- **IRC §6501(e) (six year statute of limitations for substantial omission) is made effective**
- Bill effective 7/1/2009, but we pick up federal changes when they are effective, under HRS §235-2.5(a)(3).
- For more details see Announcement 2009-10

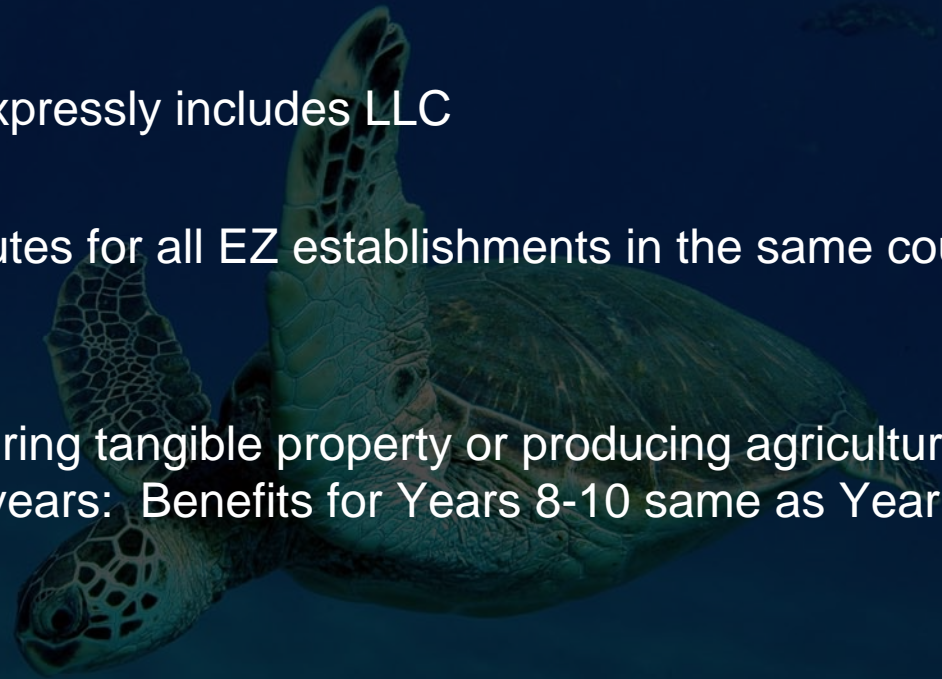
- Establishes a special enforcement section in DOTAX. Primary targets will be **cash-based businesses**, defined as meeting **one or more** of:
 - Substantially underreported or misrepresented the proper amount of tax liability – more than 25%.
 - Must be licensed, registered, or permitted under the tax laws, and isn't.
 - Past pattern of noncompliance of obligations under the tax laws.
 - Does not have a fixed and permanent principal place of business.
 - Has not obtained any required tax clearance.
 - Failed to maintain adequate books and records, or records required to be maintained by law or rule.
 - Does not accept checks or electronic payment devices for business transactions.
 - Offers price differentials when the business transaction substantially involves payment of cash.
 - DOTAX can add to this list.
 - Exceptions are provided for bona fide business needs.

- Fines are provided for any or all of the following, where the **fine is enhanced for a cash-based business**:
 - Failure to produce a tax license upon demand. (\$500/\$1,000 for a cash-based business)
 - Failure to keep books and records, or to produce them upon demand. (\$1,000/\$2,000)
 - Failure to record transaction by receipt. (\$1,000/\$2,000)
 - Failure to record transaction by register. (\$1,000/\$2,000)
 - Offering a lower price if the transaction is paid for in cash. (\$2,000/\$3,000)
 - Possession of currency for tax avoidance purposes. (\$2,000/\$3,000)
 - Exceptions are provided for bona fide business needs.

- Reporting Requirement for **Contractors on Federal Construction Projects**
 - Persons who do not possess a GET License at the time of the award of a federal construction contract must report to DOTAX:
 - The **estimated gross receipts** from the contract, and
 - Any **other information** required by DOTAX.
 - Note that **withholding tax** is required on employees who are brought in to do the job. (HAR §18-235-61-04(b)(1))
 - **60 day “grace period”** is given for employers other than construction contractors.
 - Contractors must withhold from the **first day** when the project is in Hawaii.
 - For more information see Announcement 2009-8

- Date for payment of periodic General Excise Tax pushed back to **20th** day of the month (was last day)
 - **Transition relief** (Announcement 2009-11):
 - For reporting periods ending on or before **12/31/2009**, no penalty if the G-45 is filed by the old deadline (end of following month)
 - Penalties will be imposed beginning 2/22/2010 (2/20 is a Saturday)
- Department also may require any **mandatory e-filer** for federal purposes to e-file for State purposes
 - Will be applied to employers making Federal payroll tax deposits on the **3-day rule** (Ann. 2009-11) (“semi-weekly schedule depositor”)
 - Such employers must make State payroll tax deposits on the same 3-day rule, and via EFT, effective **1/1/2010**

- Eligible business now includes development, sale, production of, or R&D related to, genetically engineered medical, agricultural, or maritime biotechnology products.
- Qualified business now expressly includes LLC
- Qualification tests: Attributes for all EZ establishments in the same county are considered together.
- EZ benefits for manufacturing tangible property or producing agricultural products are extended 3 years: Benefits for Years 8-10 same as Year 7
- Effective 7/1/2009



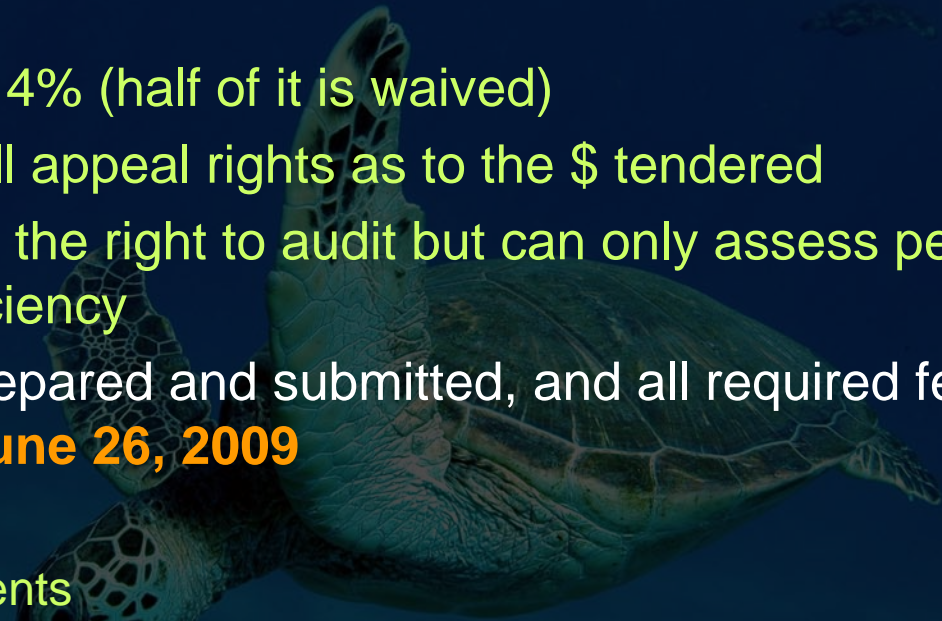
- A taxpayer can elect to reduce the credit by 30% and the reduced amount becomes refundable. **(SOLAR ONLY, includes solar thermal and photovoltaic)**
- For certain **individual** taxpayers the credit amount is refundable without the reduction: **(SOLAR OR WIND)**
 - AGI \$20,000 or less (\$40,000 for MFJ)
 - All income is excludable pension
- The credit is reduced or eliminated if the taxpayer is installing the system to comply with HRS §196-6.5, which requires a solar water heater in order to get a building permit.
- Effective for taxable years beginning on or after 1/1/2009
- Also see: Announcement 2009-9

- HB 1405 “Amazon.com Nexus” **VETOED**
 - Out-of-state sellers presumed taxable if soliciting business with Web link from in-state business partner, \$10,000 in referred business
 - Presumptive nexus if a business solicits 20 in-state residents or has Hawaii source income \$100,000+
- SB 1678 Streamlined Sales Tax Project **VETOED**
 - Not effective until federal law is passed overturning *Quill Corp. v. North Dakota*
- Act 70 (SB 427) TRICARE
 - Clarifies that the support contractor is:
 - Taxable on its fee
 - Not taxable on reimbursements to health care providers
 - Effective 7/1/2009, repealed on 12/31/2013

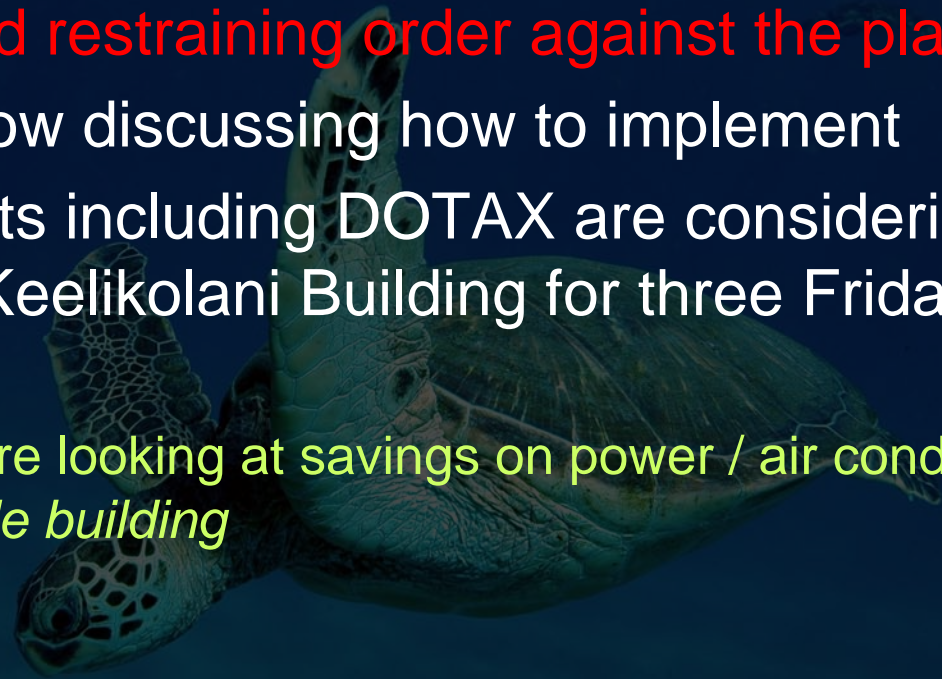
- Act 84 (HB 35) General Income Tax Credit – \$1 for 2009
- Act 165 (HB 1495) Repeals Deduction for Wagering Losses
 - Those 1099's from Vegas are now going to stick, eff. 1/1/2009
- Special Session Act 14 (HB 1544) Phase-Out of Personal Exemption
 - Phase-out starts at 75% of the federal level in place on 7/1/2008
- Act 198 (HB 371) Fuel Tax
 - Boosts tax on naphtha fuel for a power generating facility from 1¢ per gallon to 2 ¢ per gallon effective 7/1/2009
- Act 183 (HB 1809) Electronic Waste
 - New fee of \$2500/yr on retailers of TV's, effective upon approval

- **Act 184 (SB 470) Liquor Establishments**
 - Allows liquor establishments to renew liquor licenses without tax clearance if they enter into a payment plan with DOTAX

- **Act 181 (HB 1550) Tax Sheltered Annuities**
 - If tax sheltered annuity funds representing employee pretax contributions are rolled over into the state Employees' Retirement System, the rollover will be taxable for state purposes
 - Closes a loophole
 - Distributions from ERS are income tax exempt
 - But other retirement plan payments are exempt only if they came from employer contributions

- Not an amnesty program
 - Similar to voluntary disclosure
 - No penalties
 - Interest charged at 4% (half of it is waived)
 - Taxpayer waives all appeal rights as to the \$ tendered
 - Department retains the right to audit but can only assess penalties on any further deficiency
 - Tax returns must be prepared and submitted, and all required fees and interest tendered, by **June 26, 2009**
 - No extensions
 - No installment payments
 - Revenue must be in the door
 - If you miss something, the benefits of the program are denied and they keep the money
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- All state employees will be furloughed 3 days a month under Gov's plan
 - Court has issued restraining order against the plan
- Departments are now discussing how to implement
- Multiple departments including DOTAX are considering shutting down the Keelikolani Building for three Fridays every month
 - The departments are looking at savings on power / air conditioning by closing the *whole building*



- Contact your client service team member
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- Wendell Lee, Partner in Charge, Tax (531-3400)
- Kent Tsukamoto, Managing Partner (531-3400)

