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To: The Honorable Richard H.K. Onishi, Chair;
The Honorable Daniel Holt, Vice Chair;
and Members of the House Committee on Tourism & International Affairs

From: Rona M. Suzuki, Director
Department of Taxation

Re: **S.B. 2922, S.D. 2, Relating to Transient Accommodations Tax**
Date: Thursday, March 12, 2020
Time: 9:00 A.M.
Place: Conference Room 312, State Capitol

The Department of Taxation (Department) **strongly supports** S.B. 2922, S.D. 2, an Administration measure. S.B. 2922, S.D. 2, makes various amendments to the transient accommodations tax (TAT), contained in chapter 237D, Hawaii Revised Statutes (HRS). This measure has a defective effective date of July 1, 2050.

Specifically, S.B. 2922, S.D. 2, makes the following amendments:

1. Repeals the misdemeanor for failing to obtain a TAT registration identification number and replaces the misdemeanor with a monetary fine.

   The criminal penalty for failure to register for a TAT license is not consistent with the monetary fines for similar violations under the general excise tax (GET) law. S.B. 2922, S.D. 2, repeals this penalty and replaces it with fines under the fine structure already existing in chapter 237D, HRS, for other violations for consistency.

2. Applies personal liability for certain controlling officers under section 237-41.5, HRS, to TAT;.

   Section 237D-16, HRS, applies the administrative provisions of GET to TAT, but needs to be updated to include the personal liability provision enacted by the Legislature in 2010. S.B. 2922, S.D. 2, amends section 237D-16, HRS, to explicitly include the GET personal liability provision.

3. Replaces the specific term "operator or plan manager" with "person" or "taxpayer" to ensure that there are no technical defenses or loopholes to any TAT provisions.

   These amendments are necessary because of the imposition of TAT on transient accommodations brokers, travel agents, and tour packagers enacted by Act 211, Session Laws of Hawaii 2018. Prior to this new imposition, TAT was only imposed on operators and timeshare plan managers.

4. Broadens the definition of "operator" to clarify that it includes any person who engages in any activity that results in the collection of receipts that are defined as gross rental proceeds under the TAT law.

   The Department has received numerous inquiries from taxpayers who believe that they are not subject to tax because they are not the "operator" in a transaction. The Hawaii Supreme Court in *Travelocity.com, L.P. v. Director of Taxation*, 135 Hawaii 88 (2015), said that there can only be one operator in a transaction. S.B. 2922, S.D. 2, makes clear that gross rental proceeds received by anyone is subject to TAT; and

5. Repeals references to filing of returns and remittance of payments to specific taxation districts.

   The Department no longer requires taxpayer to file and pay in their home district. Other than taxpayers who are required to filed and/or pay electronically, taxpayers may file and pay taxes at any of the Department's district offices regardless of where they reside or operate their business.

The Department respectfully requests that a non-defective effective date be inserted. Thank you for the opportunity to testify in support of this measure.

LEGISLATIVE TAX BILL SERVICE

TAX FOUNDATION OF HAWAII

126 Queen Street, Suite 304 Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: TRANSIENT ACCOMODATIONS, Replace Criminal Penalty with Fine and Add Personal Liability

BILL NUMBER: SB 2922, SD-2

INTRODUCED BY: Senate Committees on Ways & Means and Judiciary

EXECUTIVE SUMMARY: Amends the transient accommodations tax law to repeal the misdemeanor penalty for failing to register and replacing it with a civil fine structure and to make "various technical amendments" including the addition of personal liability.

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

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

Makes various technical and conforming amendments.

EFFECTIVE DATE: 7/1/2050.

STAFF COMMENTS: This is the Administration measure TAX-03 (20) sponsored by the department of taxation.

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

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

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

Business taxes are normally imposed on business entities, at both the federal and state levels. If taxes aren't paid, the tax agencies collect from the business assets, but generally don't shake down the individuals associated with the businesses.

One significant exception to the rule is what we call "trust fund taxes." That's where one person collects another person's money that is due to the government. The classic example is payroll withholding taxes. An employer has agreed to pay an employee a certain amount of money, but

the law says part of it must be withheld and turned over to the government. The part turned over is the employee's money, but the employee never gets to touch it. Now, if it so happens that the employer needs to pay some other bills and uses employee money to do that, the government essentially views that act as theft, and will go after individuals who misappropriated that money to make the government whole. (Note that under current law, the employee, who has done nothing wrong, is still credited with the tax withheld even though the government hasn't received its money.)

Trust fund tax theory also applies to conventional sales taxes (different from our General Excise Tax). States where sales tax is imposed on the customer, but the seller is required to collect and remit the tax, present the same fact pattern. If the seller uses someone else's money to pay its own bills, those states have no problem going after responsible officials of the seller for the unpaid tax.

In Hawaii, we adopted this principle and imposed "trust fund liability" with respect to the General Excise Tax (GET). But under the GET law, there is no trust fund. The tax is imposed on the seller. So, it's not possible for the seller to pay other creditors with someone else's money. Indeed, if Tomco, Inc. sells something for $100 and charges its customer $4 tax for a total price of $104, the whole $104 is considered Tomco's money and Tomco is assessed tax on all of it as a gross receipt. If Tomco fails to remit the $4 to the government, responsible officials of Tomco are personally liable. Also, whether Tomco passed on the $4 to the consumer has no legal significance. Personal liability applies even if no tax is passed on, per HRS section 237-41.5(a)(2).

It is this principle that the Department now wants to apply to the TAT as a "technical change." When asked why, the Department representatives said it was "for consistency [with the GET]" and "to be just another arrow in our quiver."

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

Digested 3/10/2020