

JOSH GREEN, M.D.
GOVERNOR

SYLVIA LUKE
LT. GOVERNOR



GARY S. SUGANUMA
DIRECTOR OF TAXATION

DEPT. COMPLAINT 171
KRISTEN M.R. SAKAMOTO
DEPUTY DIRECTOR

STATE OF HAWAII
DEPARTMENT OF TAXATION

Ka 'Oihana 'Auhau

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December 22, 2023

The Honorable Ronald D. Kouchi
President and Members of the Senate
Thirty-Second State Legislature
State Capitol, Room 409
Honolulu, HI 96813

The Honorable Scott K. Saiki
Speaker and Members of the
House of Representatives
Thirty-Second State Legislature
State Capitol, Room 431
Honolulu, HI 96813

Dear President Kouchi, Speaker Saiki, and Members of the Legislature:

For your information and consideration, the Department of Taxation (Department) hereby transmits a copy of the Report on the Department's Special Enforcement Section for Fiscal Year 2023, as required by Section 231-81(c), Hawai'i Revised Statutes (HRS).

In accordance with section 93-16, HRS, the Department also informs you that the report may be viewed electronically at: https://tax.hawaii.gov/stats/a5_1annual/a5_1tax_annuals/

If you have any questions or concerns, please feel free to contact me at (808) 587-1540.

Sincerely,

A handwritten signature in blue ink, appearing to read "Gary S. Suganuma", written over a printed name and title.

Gary S. Suganuma
Director of Taxation

Enclosure

DEPARTMENT OF TAXATION
ANNUAL REPORT REQUIRED BY ACT 134, SLH 2009, SECTION 9
For the period from July 1, 2022 through June 30, 2023

Act 134, Session Laws of Hawaii 2009, also known as the "Cash Economy Enforcement Act" (hereinafter sometimes referred to as the "Act"), requires, at section 9 of the Act, that the Department of Taxation ("Department") report the following information to the Legislature:

- I) The state resources committed to implementing the Cash Economy Enforcement Act; and
- II) The additional tax revenues raised as a result of the Act.

The Special Enforcement Section (SES) was established to enforce the Act. Its goal is to ensure that all sectors of Hawaii's economy, especially those that conduct a significant portion of business transactions in cash ("cash economy"), pay their fair share of taxes. In FY 2016, SES was given additional responsibilities for ensuring that short-term vacation rental operators comply with the State's transient accommodations tax (TAT) laws, and in FY 2022, the authority of SES to examine any sector of Hawaii's economy for non-compliance was clarified and codified.

BACKGROUND

The Cash Economy Enforcement Act provided the Department with unique resources to increase taxpayer compliance in the area of the "cash economy" by educating taxpayers about their tax obligations and by conducting civil tax investigations. The Act executes its mandate through SES, which is a specialized unit within the Department's Compliance Division comprised primarily of civil investigators and assistant investigators.

The Department was authorized by section 2 of the Act, codified as section 231-83(b), Hawaii Revised Statutes (HRS), to utilize new hires, as well as existing labor resources to staff the SES operations. Furthermore, section 2 of the Act authorized the Department to identify the proceeds of SES operations to substantially fund the unit. The SES is allowed to identify taxes collected from any taxpayer, assessment, investigation, or collection as a matter of the SES, which may then be deposited into the Tax Administration Special Fund, codified as section 231-85, HRS. Within the Tax Administration Special Fund's expenditure authority, the Department was initially allowed to retain the first \$500,000 to fund the Section's operations, with the remaining fiscal year collections being deposited into the General Fund.

Section 8 of the Act authorized establishing six new full-time equivalent (FTE) positions that may be filled by investigators, investigator assistants, licensed attorneys, or other support staff, in addition to using current personnel. In subsequent years, the Legislature incrementally authorized the Department to retain additional funds and establish additional positions, currently up to \$2,000,000 and 13 FTE positions, to support SES's operations and help with enforcement of TAT laws, codified as section 235-20.5, HRS.

ACTIVITIES AND ACCOMPLISHMENTS

Highlights of SES's FY 2023 activities and accomplishments include:

- Reviewed complaints and referrals provided by the public and other departments and utilized investigative and analytical methods to identify business operators showing indications of noncompliance with general excise tax (GET) and/or TAT laws and evaluated for possible investigation.
- Systematized process for surveying, documenting, and citing host/operators responsible for transient accommodation ads that fail to display tax registration numbers in violation of section 237D-4, HRS (also referred to as “Act 204”).
- Utilizing various investigative techniques, conducted tax investigations of varying complexities to identify income sources and determine the amount of income subject to taxation.
- Requested and secured voluntarily filed GET and/or TAT returns and tax payments. When returns could not be voluntarily secured from the taxpayer, referred the matter and evidence of income subject to tax to Office Audit for assessment.
- Furthered projects on vacation rental/transient accommodation businesses utilizing publicly available and confidential database sources to develop leads on taxpayers who appear to be out of compliance with GET and TAT laws. These projects include information obtained from surveys of vacation rental platforms for Act 204 violations, as well as resources made available by the TAX System Modernization Program (TSM).
- Continued and expanded investigations of on-line retail and service companies in order to ensure they pay their fair share of taxes.
- Increased cooperation with other government agencies to develop leads and enforce Hawaii’s tax laws.

I. STATE RESOURCES COMMITTED TO IMPLEMENTING THE CASH ECONOMY ENFORCEMENT ACT AND OTHER ACTIVITIES

In FY 2022, SES incurred the following expenditures to support its compliance activities:

<u>Category</u>	<u>FY 2022</u>
Personnel Costs	<u>\$846,090</u>
Other Expenses	<u>180,712</u>
Total Expenditures	<u>\$1,026,802</u>
No. of Staff	10

II. ADDITIONAL REVENUES RAISED BY THE CASH ECONOMY ENFORCEMENT ACT

FY 2023 was about sustaining momentum in the face of challenges. Foremost among the challenges were overcoming a severe staffing shortage, having to hire and train new investigators, and physically relocating our offices all at the same time. Despite these challenges, SES was able to sustain the momentum established in previous years by continuing to grow revenue collections from \$40,768,932 in FY 2022, to **\$44,245,670** for FY 2023. This represents an 8.5% increase in total revenue over the previous fiscal year.

With regard to TAT revenue, SES’s efforts this past fiscal year resulted in \$10,164,931 collected, an increase of \$2,427,763 over the previous year (31.4% increase). When \$8,574,912 of GET collections related to transient accommodations are added in, total revenue attributable to SES’s efforts with regard to transient accommodations amounts to \$18,739,843.

FY 2023 was also significant in that after more than two years of suspended field visits due to the threat of Covid, educational site visits by SES to events and businesses communities, including those on the neighbor islands, were once again reinstated. As a result, in FY 2023, SES conducted site visits to 52 locales during which 1,123 individual businesses were visited.

Details of SES's performance compared with the previous fiscal year are as follows:

	<u>FY 2023</u>	<u>FY 2022</u>
Number of Events Visited Throughout the State	52	0*
Businesses Educated on Compliance of Tax Laws	1,123	0*
Complaints Received and Reviewed	61	142
Number of Investigations Completed	104	192
General Tax Impact Revenue Collected	\$34,080,740	\$33,031,764
No. of Taxpayers Remitting General Tax Payments	630	1,200
Average General Tax Impact Revenue Collected per T/P	\$54,096	\$27,527
TAT Impact Revenue Collected	\$10,164,931	\$7,737,168
No. of Taxpayers Remitting TAT Payments	261	648
Average TAT Impact Revenue Collected per T/P	\$38,946	\$11,940
Total Impact Revenue Collected from Taxpayers	\$44,245,671	\$40,768,932

*In FY2022, the numbers shown for Businesses Educated on Compliance of Tax Laws, and the Number of Site Visits Throughout the State, reflect the continued suspension of SES site visits to businesses and vendor events due to the Covid-19 pandemic.