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September 19, 2017

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Rules Office
Hawaii Department of Taxation
830 Punchbowl Street, Room 221
Honolulu, HI 96813

Re: **Comments on Proposed Rules Relating to County Surcharge**

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Ladies and Gentlemen:

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The Notice of Public Hearing relating to these proposed rules states that the Department's intent is to simplify the county surcharge rules by deleting the requirement that the taxpayer have nexus with the county imposing the surcharge. The proposed rules as presented go far beyond that topic and raise several issues and concerns, discussed below.

A. **Nexus with the County Imposing the Surcharge.**

In state tax parlance, "nexus" usually refers to the requirement under the Commerce Clause of the U.S. Constitution that a person or entity have a presence in the jurisdiction that is trying to tax it. *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992). Here, it must be kept in mind that the county surcharge *is not* a state tax. Although the Hawaii Legislature has delegated the power to enact a surcharge on the GET and has prescribed standards and parameters for doing so, the surcharge is imposed by county ordinance. See HRS § 248-2.6; Rev. Ord. of Honolulu §§ 6-60.1 to 6-60.3. Thus, some demonstrable connection between the surcharging county and the prospective taxpayer may be necessary to satisfy constitutional requirements. Just as it would be unusual and unfair for Kauai County to impose its vehicular weight tax against a Nissan Sentra that is garaged in Pukalani and never strays from Maui County, it would seem odd for Honolulu to impose its county surcharge against a Lanai City bakery that occasionally accepts phone orders and ships a few loaves of sweet bread to Kaneohe.

B. **Deletion of Sourcing Rule Relating to Commissions.**

The proposed rules delete the entire section relating to sourcing of commissions, namely HAR § 18-237-8.6-04, and leave nothing in its place. This move has the potential to plunge the law in this area into chaos, with some taxpayers likely to interpret the deletion of the rule as a non-event and others likely to think that the services rules are now to apply to commissions. If the Department's intent is not to change the existing law, there should be no reason to delete the existing rule. If the Department does wish to change the law, we feel that the subject is significant enough so that the Department's intent needs to be made known in the notice of public hearing to comply with HRS § 91-3(a)(1).

EXECUTIVE ADVISORY
BOARD OF DIRECTORS

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C. Adoption of "Benefit to the District" Test.

In several of the existing rules, the Department allowed for the use of "any reasonable allocation method that clearly, fairly, and properly reflects the gross income to the appropriate taxation district; provided that the allocation method is documented." The proposed rules replace every occurrence of that standard with a standard like this:

(b) If services are used or consumed in more than one taxation district, gross income shall be allocated using any reasonable method; provided that the method is consistently used by the taxpayer and supported by verifiable data that reasonably quantifies the proportionate benefit received by each taxation district.

Proposed § 18-237-8.6-03(b). We respectfully suggest that the new standard is a major change, is not an improvement over the old one, and has the potential to cause widespread confusion. Private parties have no idea how to measure the benefit received by a taxation district from a private business transaction (which transaction was never intended to benefit a taxation district in the first place). If the Department's aim is to require the "reasonable allocation method" to have an economic basis, then it could instead fashion a standard similar to that in the reimbursement rules, for example the standard in HAR § 18-237-20-06(e).

In any event, the change to the standard is significant. We do not believe that the existing Notice of Public Hearing apprises the public of the depth of the proposed change, and for that reason the validity of the rule may be called into question under HRS § 91-3(a)(1).

Thank you for the opportunity to submit comments.

Very truly yours,



Thomas Yamachika
President

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