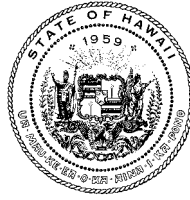


BENJAMIN J. CAYETANO
GOVERNOR

MAZIE HIRONO
LT. GOVERNOR



RAY K. KAMIKAWA
DIRECTOR OF TAXATION

SUSAN K. INOUE
DEPUTY DIRECTOR

STATE OF HAWAII
DEPARTMENT OF TAXATION
P.O. BOX 259
HONOLULU, HAWAII 96809

October 30, 1998

TAX INFORMATION RELEASE NO. 98-8

RE: Application of Act 247, Session Laws of Hawaii 1998 (Act 247), Relating to the General Excise Tax Exemption for Tangible Personal Property Imported into the State for Resale at Wholesale.

Under Act 247,¹ chapter 237 of the Hawaii Revised Statutes (HRS), relating to the general excise tax, has been amended to provide a general excise tax exemption for the sale of tangible personal property that is imported into the State from a foreign or domestic source to a licensed taxpayer for subsequent resale at wholesale as defined in section 237-4, HRS. This exemption applies only to the initial sale of imported tangible personal property to a licensed taxpayer for subsequent resale at wholesale, and does not apply to subsequent wholesale sales, if any. Act 247 is effective July 1, 1998, and applies to gross receipts received after June 30, 1998.

A. In General.

To claim the exemption, the seller must take from the purchaser of imported tangible personal property Form G-17, a Resale Certificate (see attached) certifying that the purchaser shall resell the imported tangible personal property at wholesale as defined under section 237-4, HRS. If the sale is in fact not a sale for resale at wholesale, the purchaser who furnished the certificate shall be obligated to pay to the seller, upon demand, the amount of the additional tax which is imposed upon the seller. In addition, the absence of a certificate raises the presumption that the sale is not a sale for resale at wholesale, unless the purchaser's business is exclusively sales for resale at wholesale. The Department will allow the seller and purchaser to modify the Resale Certificate as necessary in accordance with their particular business operations, i.e., to accommodate purchasers who resell goods both at retail and wholesale.

Prior to Act 247, the gross proceeds from the sale of imported tangible personal property by a wholesaler to a distributor for resale at wholesale was subject to the 1/2% general excise tax rate. Act 247 reduces the pyramiding of the general excise tax for smaller businesses by exempting the wholesaler from the 1/2% general excise tax on the sale of goods to a distributor for resale at wholesale. Accordingly, in the majority of cases the 1/2% general excise tax is

¹ Senate Bill No. 2065, S.D. 1, relating to the general excise tax, was passed by the 1998 Legislature and approved by the Governor on July 20, 1998.

imposed only once on the subsequent sale from the distributor to the retailer. Act 247 allows smaller businesses to compete more effectively with larger businesses which generally can take advantage of economies of scale and structure their distribution system to avoid a transaction from a wholesaler to a distributor, such that the larger businesses are taxed at 1/2% only once on the sale from the distributor to the retailer. Act 247 not only reduces the cost of doing business in Hawaii, but also ultimately reduces costs for Hawaii's consumers.

B. Application of Act 247 to Drop Shipments.

Act 247 may also apply to drop shipments. A "drop shipment," which is sometimes known as direct delivery, means the delivery and acceptance of tangible personal property by a retailer or customer in Hawaii from a manufacturer or wholesaler who is someone other than the seller with whom the retailer or customer placed the order.

The application of Act 247 to drop shipments is best illustrated by examples. The following is an example of a typical drop shipment arrangement that would be impacted by Act 247: D, an out-of-state distributor receives an order for goods over the telephone from a Hawaii retailer. D places the order for goods with an out-of-state manufacturer, M. M ships the goods directly to the Hawaii retailer. The Hawaii retailer sells the goods to a Hawaii consumer. There are four possible tax outcomes depending upon whether M and D have nexus with Hawaii.

1. If M and D do not have nexus:
 - (a) The retailer is considered to have imported the goods for resale at retail and is subject to .5% use tax on the purchase price of the goods (Act 247 does not apply because it is limited to imports for resale at wholesale); and
 - (b) The retailer is also subject to the 4% general excise tax on the gross income from the retail sale of goods to the consumer.
2. If M does not have nexus and D has nexus:
 - (a) Sale of goods from M to D is not taxable because M does not have nexus;
 - (b) D is not subject to the use tax because D is importing goods for resale at wholesale;
 - (c) D is subject to .5% general excise tax on the gross income from the wholesale sale of goods to the retailer; and
 - (d) Retailer is subject to 4% general excise tax on the gross income from the retail sale of goods to the consumer.

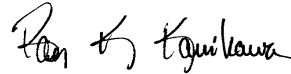
3. If M and D both have nexus:
 - (a) Sale of goods from M to D falls within the Act 247 general excise tax exemption;
 - (b) D is subject to .5% general excise tax on the gross income from the wholesale sale of goods to the retailer;
 - (c) Retailer is subject to 4% general excise tax on the gross income from the retail sale of goods to the consumer; and
 - (d) M is not subject to the use tax because M has imported goods for resale at wholesale.

4. If M has nexus and D does not have nexus:
 - (a) Sale of goods from M to D does not qualify for the Act 247 general excise tax exemption because M is selling goods to D, an unlicensed taxpayer;
 - (b) Sale of goods from M to D does not qualify as a wholesale sale because D is an unlicensed taxpayer, thus, the sale from M to D is treated as a retail sale and the gross income from the retail sale is subject to 4% general excise tax;
 - (c) M is subject to use tax at .5% on the purchase price of the goods because M is considered to have imported the goods for resale at retail (sale of goods from M to D treated as a retail sale because D is unlicensed)
 - (d) D is not subject to the general excise tax on the gross income from the sale of goods to the retailer because D does not have nexus;
 - (e) Retailer is subject to 4% general excise tax on the gross income from the retail sale of goods to the consumer.

Tax Information Release (TIR) No. 95-5 and Hawaii Administrative Rules (HAR) §18-237-13-02.01 provide guidance as to the application of the general excise and use taxes to a three-party drop shipment involving an out-of-state seller, out-of-state wholesaler, and Hawaii customer. Act 247 does not apply to a three-party drop shipment situation because a three-party drop shipment does not involve a sale of goods to a licensed taxpayer for subsequent resale at wholesale. Taxpayers should reference this TIR for guidance as to the application of Act 247 to a four-party drop shipment involving a sale of goods to a licensed taxpayer for subsequent resale at wholesale. The Department intends to amend HAR §18-237-13-02.01 to include a discussion of the application of Act 247.

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If you have any questions regarding this Tax Information Release, please call Administrative Rules Specialist Iris Kitamura at 808-587-1570. Forms and other tax information may be downloaded from the Department's website at <http://www.state.hi.us/tax/tax.html>. On Oahu, forms may be ordered by calling the Department's Forms Request Line at 808-587-7572. Persons who are not calling from Oahu may call 1-800-222-7572 to receive forms by mail or 808-678-0522 from a fax machine to receive forms by fax.



RAY K. KAMIKAWA
Director of Taxation

Attachment