

DEPARTMENT OF TAXATION

ANNUAL REPORT REQUIRED BY ACT 134, SLH 2009, SECTION 9 For the period July 1, 2009 through June 30, 2010

January 24, 2011

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:

- 1) **The State resources committed to implementing the Cash Economy Enforcement Act; and**
- 2) **The additional revenues raised as a result of the Act.**

BACKGROUND

The Cash Economy Enforcement Act provided the Department with unique resources to increase taxpayer compliance in the area of the cash economy, as well as high-risk and complex civil tax investigations in general. The primary focus of the Cash Economy Enforcement Act is the creation of the Special Enforcement Section, which is a specialized unit within the Department's Compliance Division. The Special Enforcement Section is comprised primarily of civil investigators. Specifically, the Department was authorized at 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 Special Enforcement Section operations. Furthermore, Section 2 of the Act authorized the Department to identify the proceeds of Special Enforcement Section operations to assist in the funding of the unit. The Special Enforcement Section is allowed to identify taxes from any taxpayer, assessment, investigation, or collection matter as a matter of the Special Enforcement Section, which may then be deposited into the Tax Administration Special Fund (codified as HRS § 231-85). Within the Tax Administration Special Fund's expenditure authority, the Department is allowed to retain the first \$500,000 to fund the Section's operations, with the remaining collections being deposited into the General Fund. *See* HRS § 235-20.5, as amended by Section 4 of the Act. The Department was also provided legislative authority at Section 8 of the Act to establish 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.

Since passage of the Cash Economy Enforcement Act, the Department has worked diligently in beginning the implementation of an entirely new operation within the Compliance Division. In the Department's assessment, it believes that it has been successful, to date, in bringing the Special Enforcement Section online given the competing compliance, and other priorities of the Department in the current economy. An update on the activities and accomplishments of the SES include:

- Conducting outreach and public dissemination of information regarding the Special Enforcement Section and the Cash Economy Enforcement Act on Oahu, Maui, Hawaii and Kauai through CPA and Bar Associations, practitioner groups, industry groups and to various groups that requested meetings;
- Reviewing and selecting high-risk cases, including cash-based businesses, potential civil fraud cases, and complex collection matters;
- Conducting field operations where Special Enforcement Section Agents were identifiable. Field operations were conducted at farmer's markets, craft fairs, shopping malls, food courts, industrial parks, restaurants and other locations and included issuing warnings and citations to business who were in violation of Hawaii tax laws;
- Investigating cases relevant to the Special Enforcement Section's mission, including cases involving potential fraud and underreporting of cash receipts, potential false returns, as well as complex collection matters;
- In addition, the SES is currently developing Questions and Answers to be posted on the Department's website and for public dissemination.

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

In Fiscal Year 2011, six positions were funded. Five of these six positions – the Investigator Supervisor and four Investigators - have been filled. The newly hired Investigator Supervisor and Investigators were required to attend an orientation and complete an intensive two-week training program. Upon completion of their training, SES Special Agents were awarded their Investigator badges. In addition, the Department previously hired a Special Agent in an Administrative Rules Capacity who has been assigned to the SES.

For Fiscal Year 2010, SES expenditures were as follows:

Category	Fiscal Year 2010
Personnel	\$19,429
Other Current Expense	\$11,776
Total	\$31,205

As of December 20, 2010, Fiscal Year 2011 SES expenditures were \$58,231 consisting of \$54,747 personnel and \$3,484 other current expense.

II. ADDITIONAL REVENUES RAISED BY THE CASH ECONOMY ENFORCEMENT ACT

In Fiscal Year 2010, the SES generated \$662,186 in revenues.

Since its beginning to date, SES reports the following cumulative statistics:

Complaints filed by anonymous persons:	140
Taxpayer inquiries re: how to comply with tax law:	100
Site visitations throughout the State of Hawaii:	500+
Verbal warnings:	11
Citations issued:	102
Total Fines:	\$ 36,032
Fines rescinded:	\$ 8,840
Fines paid:	\$ 11,982
Number of Audits:	43
Assessments:	\$7.5M
\$ Collected:	\$1.2M