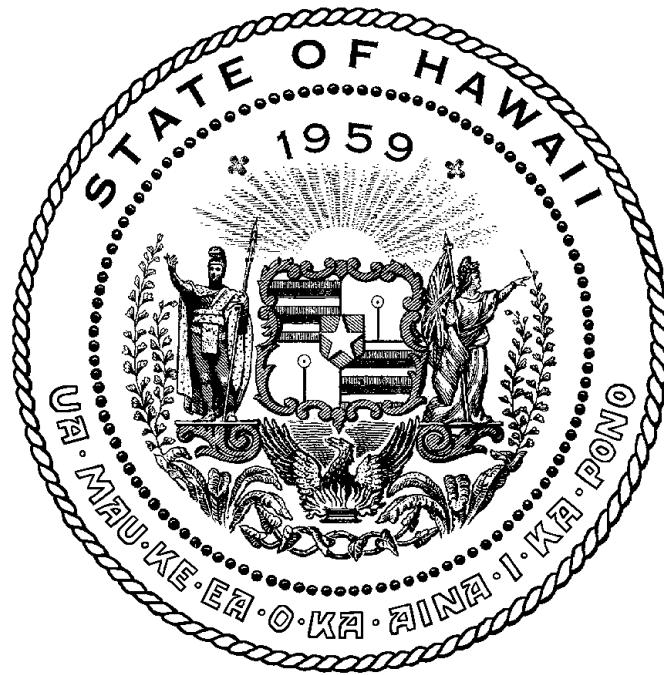


DEPARTMENT OF TAXATION STATE OF HAWAII



ANNUAL REPORT 1997-1998

October 30, 1998

The Honorable Benjamin J. Cayetano
Governor
State of Hawaii

Dear Governor Cayetano:

Despite reductions in personnel and funding every year since 1994, the department has improved its compliance and taxpayer service functions in many areas.

Compliance initiatives include the stellar performance of our criminal tax section, numerous nonfiler projects on each island, and the advent of our self audit program for the collection of use taxes for specific businesses. Your commitment to stepping up enforcement in the federal contracts arena has fostered an excellent working relationship with the military services in ensuring compliance by out-of-state contractors on military construction projects. The professionalism of our senior auditors is assisted by training programs internally as well as with the Internal Revenue Service. In addition, new evaluation forms are to be sent to taxpayers who have been recently audited in order to gauge the level of professionalism and courtesy demonstrated by our senior auditors. The area of concern is with the high pace of tax delinquency referrals and the inability of taxpayers to resolve these delinquencies. Assistance in this regard is being made through liberal payment plans, compromises, and referrals to private collection agencies.

Our taxpayer services function continues to add value for our external customers. At your request, the new Form BB-1 combines our general excise tax application with Department of Labor and Industrial Relation's unemployment insurance application forms. In the past, our personal income tax return was greatly simplified. Simplification this year involved the conversion of our corporate tax return to a single page. Work is in progress to convert our pass-thru entity returns to a single page. Outreach to our practitioners and taxpayers continues to improve through our workshops, training sessions, forums, newsletters, web site, and CD-ROM. Our electronic funds transfer procedures result in immediate deposits for half of our general fund revenues.

Our legislature was well served this year by our staff offices, especially our Tax Research & Planning Office and Rules Office which serviced the revenue estimating and legislative requirements of the Economic Revitalization Task Force, the Executive, and the 1998 Legislature. Dissemination of our technical positions continues at a fast pace with our Rules Office in the form of announcements, tax information releases and rules.

The vendor for our benefits-based Integrated Tax Information Management System was selected. We are now in contract discussions for this ambitious multi-year project which will revolutionize our returns processing, taxpayer services, and tax compliance functions. The system will enable the department to be more facilitating and responsive to our internal (employee) and external (executive, legislative and taxpayer) customers.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Ray K. Kamikawa". The signature is fluid and cursive, written in a professional style.

RAY K. KAMIKAWA
Director of Taxation

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THE YEAR IN REVIEW

TAX SERVICES AND PROCESSING DIVISION

The Tax Services and Processing Division achieves its multiple objectives through the Documents Processing Branch, the Revenue Accounting Branch and the Taxpayer Services Branch.

Efficient processing of all tax returns and documents is the major objective of the Documents Processing Branch. This branch processed more than 97,000 pounds or 2.6 million items of incoming mail, including 1.4 million payment transactions. Tax revenues collected through electronic funds transfer (EFT) exceeded \$1.5 billion, or nearly half of total state tax collections of \$3.3 billion. A pilot program to accept payments by credit card was implemented in March 1998. Transfer of the Data Control Section from the Information Technology Services Office to the Documents Processing Branch was completed during the fiscal year.

As its primary functions, the Revenue Accounting Branch maintains accurate accounting records and prepares timely accounting reports. It controls and accounts for all tax collections, adjustments and refunds.

Providing service and disseminating pertinent information and forms to taxpayers are the primary objectives of the Taxpayer Services Branch. It publishes Tax Facts, which provides relevant information on tax topics of general interest. Other continuing initiatives of this branch include publishing quarterly newsletters for tax practitioners and taxpayers, organizing workshops and forums for practitioners and industry groups, and preparing public service announcements for distribution through radio and television.

Dissemination of information and forms continues through maintenance of the department's web site, the forms-by-fax program, and an annually-updated CD-ROM. A new tax information business card is included with all mailings. The information card provides telephone numbers, addresses of all district offices, and the address of the department's web site.

To simplify filings by businesses, the Department of Taxation developed a new consolidated basic business application form in conjunction with the Department of Labor and Industrial Relations' Unemployment Division to eliminate the need for separate registrations. The corporate income tax return, Form N-30, has been revised to a single page form. This follows prior efforts that reduced the personal income tax returns to a single page. Working with the Internal Revenue Service and the Department of Accounting and General Services, the department has modified the period of validity for tax clearances from two months to six months for most purposes.

COMPLIANCE DIVISION

Voluntary compliance with Hawaii tax laws is the primary objective of the Compliance Division, which consists of the Audit Branches and Collection Branches. To meet its objective in an environment of voluntary compliance and self-assessment, the division has established programs for (1) returns processing and exception handling, (2) auditing, (3) collection, and (4) taxpayer services and information dissemination.

Exception Handling / Error Correction

During the fiscal year, the department processed 937,989 documents related to the net income tax, of which 13.5% contained errors. The Audit Branches were able to perform exception handling and correct errors on-line within established time periods.

The Audit Branches also performed exception handling for general excise, use, transient accommodations, and other miscellaneous taxes. These types of returns represent the largest volume of returns processed by the department and include periodic (monthly, quarterly, and semiannual) and annual tax returns.

Auditing

To support self-assessment and voluntary compliance, the Audit Branches performed both office and field audits throughout the year. Office audits numbered 6,126 and yielded \$8.7 million in assessments, while 403 field audits produced \$74.6 million in assessments. Field audit assessments for fiscal 1998 increased by \$3.6 million when compared with the previous fiscal year. Improvement in the field audit operational results can be credited to the audit staff's increasing experience and sophistication in handling larger and more complex cases. Field audit assessments per work hour increased to \$2,766 from \$2,657. Special audit projects by taxation district included the following:

Oahu District Office

- Office audit of taxpayers with schedule C (proprietorships)
- Office audit of real estate licensees
- Field audits of taxpayers in Virginia, Maryland and northern California with Hawaii income discrepancies
- Field audit of federal contractors
- Field audits of use tax of tow truck companies, building materials companies, boats, publishers, aircraft and parts, and properties purchased from out-of-state direct marketers

Maui District Office

- Comparison of rent paid amount on Form 1099 with reported rental income
- Real estate licensee project
- Business development company project
- Helicopter project

Hawaii District Office

- Nonfiled general excise and transient accommodations taxes on luxury condominiums
- Unreported general excise tax on proprietorship income reported on 1994 Schedule C

Kauai District Office

- Matching of reported income of proprietorships on net income and general excise returns
- Nonfiled income and general excise tax of real estate licensees

Criminal Tax Unit

Within the Field Audit Branch is a Criminal Tax Unit. During fiscal 1998, this unit returned indictments against one unincorporated business and against nine individuals. Complaints were lodged against one corporation and one individual. These indictments and complaints resulted in tax assessments of \$1,269,638 and were directed against a variety of targets: two government workers, a tax practitioner, four contractors, a realtor, an attorney, and a fuel corporation.

In the State of Hawaii's first criminal tax evasion case, a guilty verdict was rendered against Maui publisher Barbara Price, who claimed that she was not required to pay the general excise tax. She was sentenced to a term of six months in jail. Her associate pleaded guilty to a lesser offense and was sentenced to time served.

In the state's first withholding case in which a person was charged with the offense of Theft in the First Degree, defendant Kathea Suzuki-Latham pleaded guilty to the Class B offense. She was not incarcerated but was ordered to pay the State of Hawaii \$54,487 for taxes that had been withheld from her employees but

not paid to the Department of Taxation. The defendant's former husband, Michael Latham, was also indicted and remained a fugitive until apprehended by Oregon authorities. He has been extradited and is awaiting trial for the similar offense of Theft in the First Degree, a Class B felony punishable by a term of up to ten years in prison and/or a fine of \$25,000.

In January 1998, a plea agreement with Pacific Petroleum Services, Inc., a fuel company, resulted in a criminal fine of \$120,000 and taxes of \$450,000. In accordance with the plea agreement, the corporation also agreed to pay for and print in the local news media an apology to the citizens and businesses in Hawaii for its failure to file its general excise and fuel tax returns.

In late 1997, the local news media broke a story concerning a scandal involving the relocation of tenants with city money. The City and County of Honolulu had paid over \$6 million to a handful of businesses and their principal owners for services allegedly performed. In a joint effort with the Honolulu Police Department and the Office of the Prosecuting Attorney, most of the responsible persons were indicted in May 1998 for tax evasion, money laundering, bribery, and theft. The contractors and a government worker were indicted for fraudulently obtaining the monies by submitting false claims and not reporting the illegal monies for tax purposes.

In June 1998, a tax return preparer who had prepared fraudulent tax returns for her clients pleaded no contest to preparing false tax returns. The preparer is accused of fraudulent classification of the clients' marital status and the claiming of false deduction and credits. This violation is a Class C felony and the preparer is scheduled to be sentenced in fiscal 1999. This case required immediate attention because the preparer had increased the number of returns prepared from 240 for tax year 1995 to 340 for 1996 and would have prepared in excess of 400 returns for tax year 1997. The criminal investigation curtailed the preparation of the 1997 returns.

In June 1998, an unincorporated business by the name of Perfect Title Company and its principal, Mr. Donald A. Lewis, were indicted for failing to file a general excise tax return for 1996.

Delinquent Tax Collections

The Collection Program in the Compliance Division experienced another difficult year. By the end of the fiscal year, the statewide total for outstanding delinquent taxes increased \$35.2 million, causing the total delinquent balance to rise to \$218.5 million. Most key program measurements declined, as shown in the accompanying table.

| <u>Measurement</u> | <u>FY 1997-98</u> | <u>FY 1996-97</u> | <u>% Change</u> |
|--|-------------------|-------------------|-----------------|
| Total Delinquent Balance (\$millions)..... | \$218.5 | \$183.3 | 19% |
| Cash Collected (\$millions)..... | \$83.0 | \$91.0 | -9% |
| Number of Payment Plans..... | 1,949 | 2,605 | -25% |
| Number of Liens Filed..... | 2,256 | 3,367 | -33% |
| Number of Levies Served..... | 9,933 | 8,158 | 22% |
| Uncollectible Amounts Written Off (\$millions).. | \$10.0 | \$12.3 | -19% |

During the past two fiscal years, the Oahu Collection Branch has contracted three local collection agencies to collect delinquent taxes. Over 6,200 delinquent accounts with a value exceeding \$6.5 million were referred.

During the two-year period, these agencies collected nearly \$680 thousand in delinquent taxes, penalties and interest.

In a special real estate relicensing project begun in fiscal 1997, collection branch staff obtained information on real estate brokers and salespersons from the data files of the Department of Commerce and Consumer Affairs to identify possible non-filers. In a labor-intensive effort, collection staff manually reviewed tax records of all real estate license holders for both unpaid taxes and non-filed tax returns and then mailed notices of deficiencies. Over a two-year period, this project has yielded \$7.4 million in tax liabilities on returns filed and in collections of \$4.1 million in delinquent taxes, penalties and interest.

As a result of new legislation permitting the collection of cost recovery fees for such actions as delinquent account processing, lien filing, and levies, collection units began collecting the fees in the latter part of the fiscal year. Fees collected amounted to more than \$4,500.

Taxpayer Assistance Provided

Compliance Division staff in the neighbor island district offices provided 94,935 instances of telephone assistance, helped 63,132 taxpayers over-the-counter, rendered 22,762 instances of assistance via correspondence and serviced 7,459 tax clearances. Over-the-counter assistance included preparation of tax returns. All three neighbor island district officers continued to provide speakers to explain tax preparation and other topics for outreach programs such as Tax Counseling for the Elderly, University Extension Service, and the Small Business Administration.

STAFF OFFICES

Administrative Services Office

Fiscal Office

After the Administrative Services Office submitted the department's supplemental budget for fiscal year 1999, the 1998 legislature appropriated \$15.0 million to the department for that fiscal year. During its budget review, the legislature deleted funding for 24 full-time-equivalent positions. The department's budget cut for fiscal 1999 amounted to \$1.5 million.

In carrying out its duties, the Department of Taxation incurred operating expenditures of \$16.9 million for fiscal 1998. With total taxes collected and administered by the department increasing by \$10.1 million as expenditures increased from \$16.5 to \$16.9 million, the cost to collect \$100 of taxes increased from 47 cents in fiscal 1997 to 48 cents in fiscal 1998.

Personnel Management

The department was authorized 343 positions for the fiscal year. Employees were geographically distributed as follows: Oahu 275; Hawaii 29; Maui/Molokai 25; and Kauai 14.

Personnel actions within the department included 19 new civil service hires, three retirements, 114 temporary hires, and 29 resignations. Other personnel actions included the termination of 114 temporary employees hired for the tax season.

STAFFING PATTERN
(Number of Authorized Permanent Positions)

| <u>By Organization/Operating Program</u> | <u>1998</u> | <u>1997</u> | <u>1996</u> | <u>1995</u> |
|---|-------------|-------------|-------------|-------------|
| Headquarters Administration..... | 40 | 49 | 50 | 63 |
| Tax Services and Processing Division..... | 99 | 90 | 90 | 106 |
| Audit Division (Branch)..... | 111 | 112 | 114 | 130 |
| Collection Division (Branch)..... | 93 | 93 | 95 | 109 |
| TOTAL..... | 343 | 344 | 349 | 408 |

Employees participated in various training programs to expand their professional skills, thus increasing their efficiency and effectiveness in performing their duties. Computer software use and leadership training were among the training programs attended by department employees.

Rules Office

The Administrative Rules Office is the department's advisory arm to the director on tax policy. In addition to drafting and commenting on tax proposals, the Rules Office develops tax policy in rules, tax information releases, announcements, directives, and other publications.

For the 1998 legislative session, the Rules Office drafted 13 administration-sponsored tax proposals, prepared 286 testimonies on 191 bills and 13 resolutions, and submitted comments to the Governor's Office on 25 acts passed by the legislature. Members of the Rules Office also testified at legislative committee hearings on behalf of the Director of Taxation.

The Rules Office prepared 75 Governor's letters, 61 Director's correspondences, 15 announcements; six rules, and nine tax information releases. The office also reviewed legislative proposals and rules of other agencies, and provided speakers at several tax forums.

Information Technology Services Office

The Information Technology Services Office (ITSO) is currently testing the General Excise, Withholding, Transient Accommodations, and Rental Vehicle/Tour Vehicle Surcharge Tax (GEW/TAT) system and the Comprehensive Net Income Tax (CNIT) system, as well as the computer and networking components to identify and resolve Year 2000-related problems.

The Department of Taxation is currently involved in the benefits-based procurement of a new integrated tax information management system to replace the existing CNIT and GEW/TAT systems. ITSO has completed the department's basic information technology infrastructure, which is a critical component of the systems replacement project. The Systems Networking staff has completed the installation of the local area network (LAN) with the addition of the Kauai and Hawaii District Offices and the wide area network (WAN) for all district offices. The WAN provides E-mail and file sharing for each departmental user and allows the Systems Networking staff to remotely assist users and manage devices on the neighbor islands.

The Systems Networking staff has begun upgrading the LAN for all of the district offices and 3270-mainframe sessions for the Oahu District Office. The Systems Networking staff continues to troubleshoot problems and

conduct in-house training for the department on basic PC fundamentals, Windows, LAN orientation, GroupWise (network e-mail), and the Internet.

ITSO continues to improve the GEW/TAT system to streamline costs, improve efficiency, and encourage taxpayer compliance. A facility has been implemented to identify taxpayers who should be remitting payments via Electronic Funds Transfer (EFT) but are not. The system has been enhanced to generate correspondence to notify taxpayers whose increase in tax liability requires them to file more frequently. Another enhancement to the processing of small discrepancies in taxpayers' accounts was completed for the delinquent tax collectors, who will no longer have to devote time to resolve them. A combined application form was adopted to help ease the paperwork required when starting a new business. Changes were made to computer system maintenance that will allow department employees to work with a minimum of interruption during periods when the system requires housekeeping. Additional tools were made available to the Tax Research and Planning Office to aid it in monitoring ongoing changes in the state's economy.

As a result of the Economic Revitalization Task Force, the GEW/TAT System was enhanced to accommodate the legislated increase in the transient accommodations tax rate from 6% to 7.25% on January 1, 1999.

ITSO continued performing liaison tasks for the CNIT system. Tasks that were implemented for the 1997 tax law changes include: revision of the requirements for failure to pay penalty on extensions to be similar to the federal requirements by eliminating the requirement for a signature; revision of the N-15 return to include part-year residents and base the liability on a ratio of Hawaii's adjusted gross income (AGI) to worldwide AGI; and the addition of two new credits, the hotel remodeling and renovation tax credit and the motion picture income tax credit. Other tasks that were completed include: implementation of the Child Support Enforcement Agency's (CSEA) Keiki Interface project to assist CSEA in tracking absentee parents; modifications and creation of the judiciary tape to include amounts from the individual income tax return form N-11; concealing of taxpayer's ID number on correspondence and labels; conversion of reports that printed on large computer paper to laser forms; and conversion of all DYL280 programs to Easytrieve Plus.

Tax Research and Planning Office

The Tax Research and Planning Office (TR&P) reviews and analyzes the effect of legislative tax proposals, publishes statistics on income tax and tax credits, and provides administrative and technical support to the Council on Revenues.

In September 1997, the governor and the leaders of the legislature convened the Economic Revitalization Tax Force in an effort to stimulate Hawaii's economy. TR&P provided research and logistical support to the ERTF's Taxation Working Group, which was made up of a diverse cross-section of business, government, community, and academic leaders. TR&P staff responded in timely fashion to requests for revenue analyses of taxation proposals made by working group members and also prepared meeting minutes for distribution to members and the interested public. After the working group submitted its final report to the ERTF and the ERTF distilled its own taxation reform package from that report, TR&P provided revenue impact analyses of the components of the ERTF taxation package.

After the ERTF announced its taxation package, individuals and community organizations responded by making counter-proposals. TR&P provided revenue analyses of these counter-proposals. Once the 1998 legislature convened, legislators made several modifications of the ERTF taxation package based on input from various constituencies. TR&P analyzed these modifications as well as all other legislative bills involving taxation. Legislators relied heavily on TR&P data when they adopted Act 157, which reduced individual income tax rates, broadened tax brackets, and replaced the flat food tax credit with a low-income credit. They also relied on TR&P analyses when they adopted Act 156, which increased the transient accommodation tax (TAT) rate, subjected time share units to this tax, and changed the distribution of TAT revenue.

TR&P provides administrative and technical support to the Council on Revenues, which consists of seven economic experts from the community who provide the state with projections of state general fund revenues and state total personal income. This information determines the state's expenditure ceiling. Actual fiscal 1998 general fund revenues of \$2.85 billion represented a growth rate of 2.8% over fiscal 1997. The Council's latest forecast revision for fiscal 1998 called for a growth rate of 2.3%. For calendar 1997, the Council had projected growth in total personal income at 1.5% over calendar 1996, while actual growth came in at 2.8%.

Each month, TR&P provides a detailed summary of revenue trends to the governor, members of the Council on Revenue, and the directors of taxation, budget and finance, and business, economic development and tourism.

TR&P has the responsibility for compiling the department's annual report. In addition, it prepared two other annual reports using data from the department's own computer files and additional information from Internal Revenue Service data files. These reports are the 1995 tax year editions of "Hawaii Income Patterns - Individuals" and "Tax Credits Claimed by Hawaii Residents".

TAXPAYER ADVOCACY PROGRAM

Currently a one-person operation within the office of the director of taxation, the Taxpayer Advocacy Program provides a one-stop service for taxpayer concerns that cannot be resolved through normal channels. Focus is on the needs of the taxpayer on a case-by-case basis.

This program was implemented on October 1, 1997 and assisted 45 taxpayers during fiscal 1998. Issues addressed included erroneous reports of state tax refund income (Form 1099-G), misplaced letters, misapplied payments, inquiries about refunds and net operating losses, waivers of penalty and interest, assistance with offers in compromise, taxpayer rights, verifications of balances due, erroneous billings, and explanation of letters and billings. Some of the cases were referred from the Office of the Governor or the Internal Revenue Service.

Ten additional cases referred to the taxpayer advocate did not require intervention. Some were resolved by guiding the taxpayer to the right management personnel. Others involved inquiries about tax refunds that had recently been processed. Others involved erroneous payments by taxpayers who thought that the report of prior year state tax refunds (Form 1099-G) was a bill for additional taxes.

During fiscal 1998, the taxpayer advocate coordinated the department's joint "Problem Solving Days" with the Internal Revenue Service on the islands of Oahu, Hawaii (Kona), and Maui. This effort assisted 35 taxpayers with problems concerning non-filing of tax returns, amended tax returns, corrections to tax assessment cases based on IRS adjustments, penalty and interest inquiries, payment plans, and tax information.

In an attempt to be more attuned to taxpayer needs, the department distributed satisfaction surveys to the taxpayers who received refunds (via an attachment to Form 1099-G) and to tax practitioners. Another survey will be sent to taxpayers who have had recent contact with the Field Audit Branch. Responses to the surveys are sent back to the taxpayer advocate for review and as a guide to improving the department.

Most taxpayers have been satisfied with the outcome of their cases, regardless of whether a decision was made in their favor. The taxpayer advocate has focused on taxpayers' needs while maintaining taxpayer confidence that the department will administer Hawaii's tax laws in a consistent, uniform and fair manner.

MANAGEMENT PERSONNEL

OFFICE OF THE DIRECTOR

Director of Taxation Ray K. Kamikawa
Deputy Director of Taxation Susan K. Inouye

STAFF OFFICES

Rules Officer Grant Tanimoto
Tax Research & Planning Officer Francis Okano
Information Technology Services Officer Vacant
Administrative Services Officer Warren Higashi
Personnel Officer Stanley Onaga

OPERATIONS STAFF

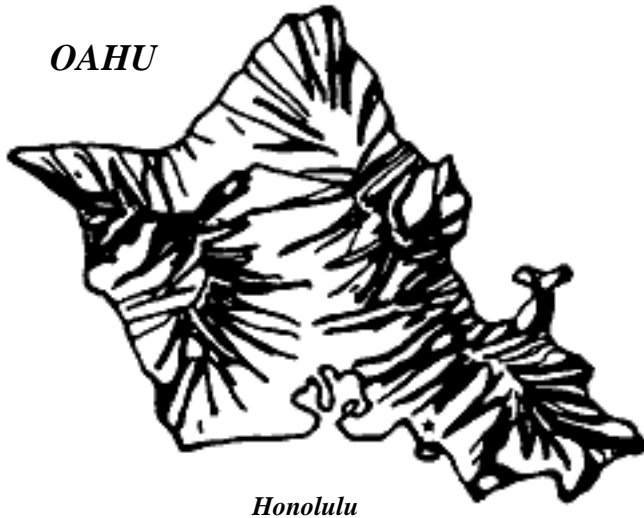
Compliance Division Chief Ronald Randall
Oahu Field Audit Branch Vacant
Oahu Office Audit Branch Vacant
Oahu Collection Branch Gary Fukumura
Maui District Tax Manager Stanley Ching
Hawaii District Tax Manager Ronald Yabe
Kauai District Tax Manager Ernest Balderas

Tax Services and Processing Division Chief Marie Okamura
Taxpayer Services Branch June Yamamoto
Document Processing Branch Jerry Ebesu
Revenue Accounting Branch Deanne Obatake

FIRST TAXATION DISTRICT

Island of Oahu

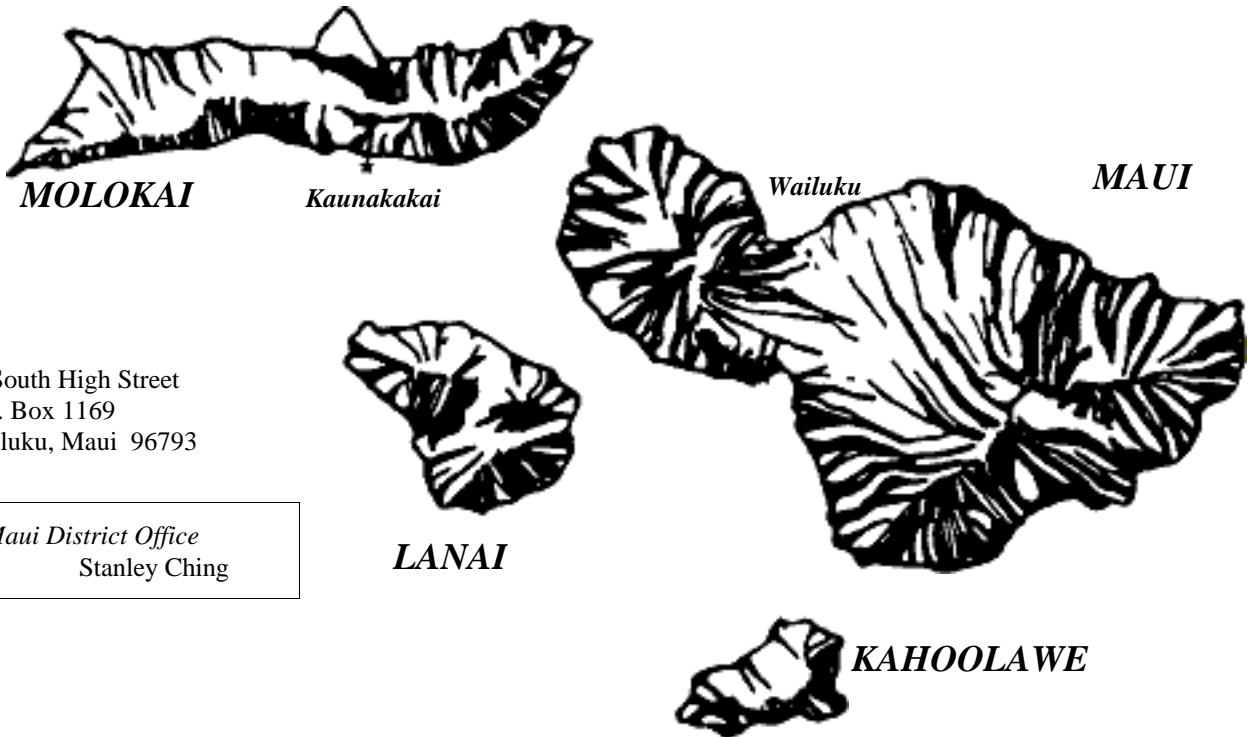
Office: 830 Punchbowl Street
P.O. Box 259
Honolulu, Hawaii 96809



Compliance Division Chief
Ronald Randall
Oahu Office Audit Branch
Vacant
Oahu Field Audit Branch
Vacant
Oahu Collection Branch
Gary Fukumura
Tax Services & Processing Branch Chief
Marie Okamura
Taxpayer Services Branch
June Yamamoto
Document Processing Branch
Jerry Ebesu
Revenue Accounting Branch
Deanne Obatake

SECOND TAXATION DISTRICT

Islands of Maui, Molokai, and Lanai



Office: 54 South High Street
P.O. Box 1169
Wailuku, Maui 96793

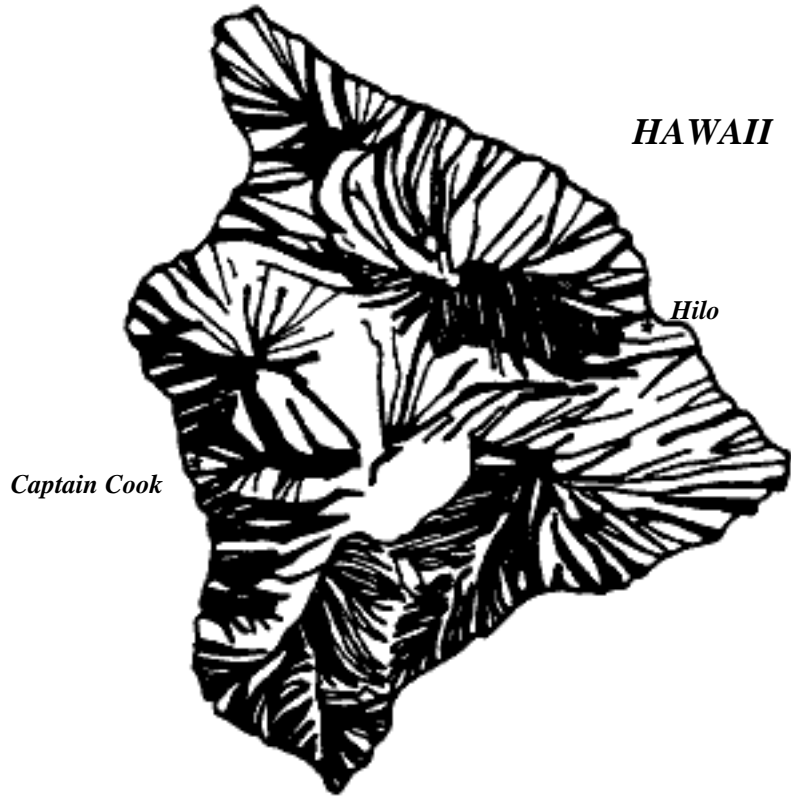
Maui District Office
Stanley Ching

THIRD TAXATION DISTRICT

Island of Hawaii

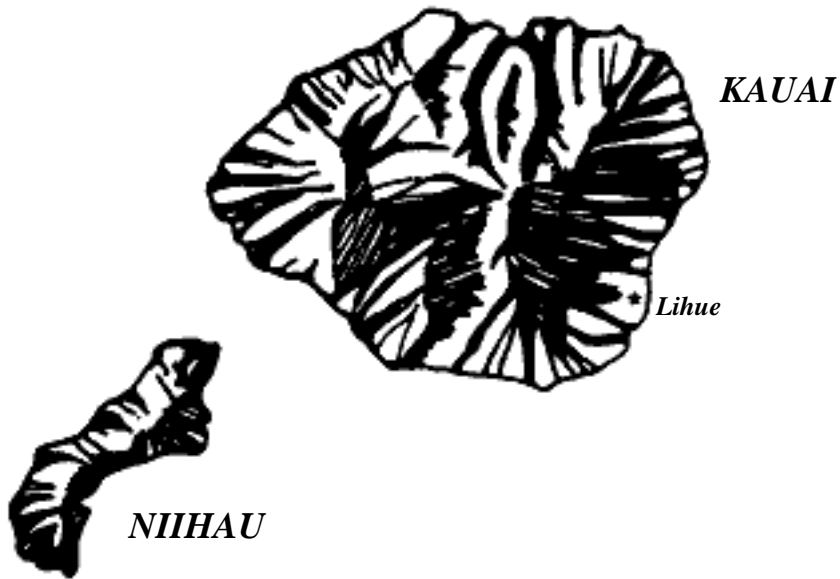
Office: 75 Aupuni Street
P.O. Box 833
Hilo, Hawaii 96721

Hawaii District Office
Ronald Yabe



FOURTH TAXATION DISTRICT

Islands of Kauai and Niihau

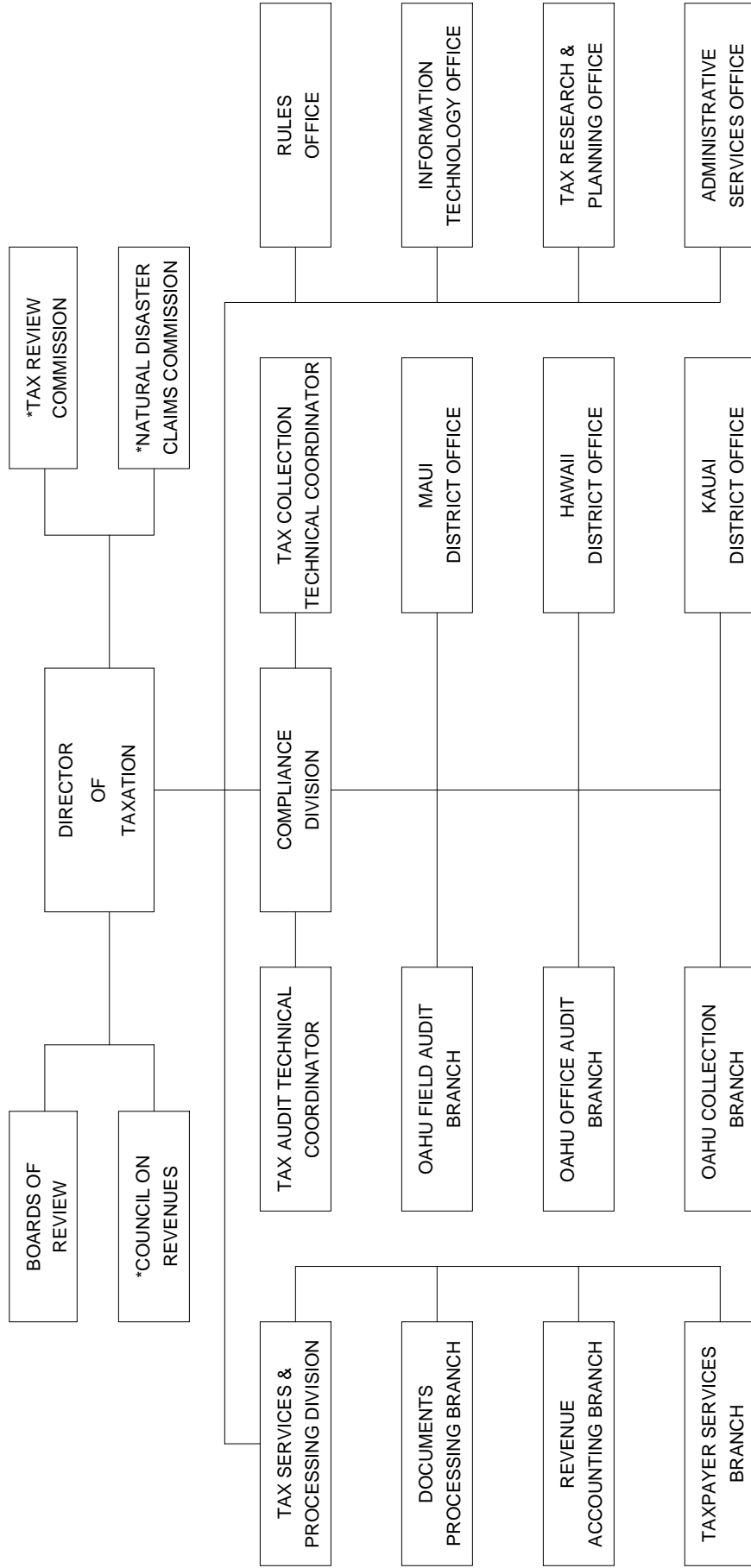


Office: 3060 Eiwa Street #105
Lihue, Kauai 96766

Kauai District Office
Ernest Balderas

ORGANIZATION CHART

Department of Taxation
State of Hawaii



* For administrative purposes.

TAX APPEALS AND LITIGATION

BOARDS OF REVIEW

Each taxation district has a Board of Review consisting of five members. Tax disputes that are not resolved at the district tax office level are presented to the Board of Review. Statewide, the boards began the fiscal year with 71 pending tax appeals. Although 36 appeals were settled, 28 new appeals were filed, resulting in a total of 63 pending at the year end. A summary of the number of appeals before the boards by tax district follows:

| | <u>Oahu</u> | <u>Maui</u> | <u>Hawaii</u> | <u>Kauai</u> | <u>Total</u> |
|----------------------------------|-------------|-------------|---------------|--------------|--------------|
| Appeals Pending - Beginning..... | 62 | 4 | 5 | 0 | 71 |
| New Appeals Filed..... | 15 | 6 | 6 | 1 | 28 |
| Appeals Settled..... | 25 | 6 | 4 | 1 | 36 |
| Appeals Pending - Ending..... | 52 | 4 | 7 | 0 | 63 |

In terms of tax liability in the cases settled, those decided in favor of the state amounted to \$358,413 while those decided in favor of the taxpayer amounted to \$2,336,990.

COURT DECISIONS

In Re Tax Appeal of Bradley Properties, Ltd., T.A. No. 96-5208, Tax Appeal Court of the State of Hawaii

The Tax Appeal Court entered judgment in the department's favor, ruling that amounts received by taxpayer from its real estate agents for certain cost advances and shared costs (including Multiple Listing Service fees, errors and omission insurance, advertising, business cards, property listing fees, and signs) did not qualify as non-taxable reimbursements for purposes of the general excise tax law. The taxpayer has filed an appeal with the Hawaii Supreme Court.

In Re Tax Appeal of United Parcel Service, Inc., T.A. No. 2235, Tax Appeal Court of the State of Hawaii In Re Tax Appeal of Lynden Air Freight, Inc., T.A. No. 97-0203, Tax Appeal Court of the State of Hawaii

The issue in these two cases is whether the preemption of state taxation of air commerce and air transportation and air transportation under federal law extends to revenue from ground transportation that is related to air transportation. The Tax Appeal Court ruled that federal law preempts the imposition of the general excise tax and the public service company tax upon these revenues. The Department of Taxation has appealed the Tax Appeal Court's decision to the Hawaii Supreme Court.

Bruce R. Travis et al. v. Department of Commerce and Consumer Affairs et al., Civ. No. 98-0216(3), Second Circuit Court of the State of Hawaii

Plaintiff, a tax protester, brought a Complaint for Declaratory Judgment challenging the constitutionality of Hawaii's general excise and net income tax laws and claiming money damages for the state's alleged constitutional violations. The Circuit Court granted the state's Motion to Dismiss or in the Alternative Motion for Summary Judgment, holding, in part, that the state, as a sovereign entity, is immune from suits for money damages for alleged constitutional violations. This case is under appeal to the Hawaii Supreme Court.

CASES SETTLED

Consolidated Insurance Premium Tax Cases (Lead case - Balboa Insurance Co. v. Insurance Commissioner, T.A. No. 3062, Tax Appeal Court of the State of Hawaii)

The focal point of this 10-year litigation was whether the insurance premium tax credit discriminates against foreign insurers without rational basis in violation of the Equal Protection Clause. Various foreign insurers and the Insurance Commissioner of the State of Hawaii, agreed to settle the consolidated insurance premium tax cases by Stipulated Judgment. Pursuant to the Stipulated Judgment filed on September 25, 1997, the state received approximately \$25 million in insurance premium taxes and the foreign insurers received a refund of approximately \$3.5 million in taxes.

In Re Tax Appeal of Adelaide Brighton Hawaii, Inc., T.A. No. 96-5372, Tax Appeal Court of the State of Hawaii

Taxpayer, a Hawaii corporation and general partner in a Hawaii partnership, claimed that it was entitled to a capital goods excise tax credit and refund in the amount of \$447,270. The partnership reported the amount of eligible tax credit on its timely filed partnership income tax returns. Taxpayer timely filed its corporate income tax returns but failed to claim the tax credit within the twelve-month statutory period for making the claim. The department maintained that a partnership cannot claim a credit on behalf of its partners, and that taxpayer failed to timely claim its credit. By stipulated judgment, the parties agreed that the state would retain 66% of the credit claimed in the sum of \$293,880.

In Re Tax Appeal of Brown-Forman Corporation; Civ. Nos. 97-5547 and 97-0011, Tax Appeal Court of the State of Hawaii

Taxpayer claimed that the State of Hawaii did not have nexus over its operations for tax purposes because it did not transact business in the state and shipped its goods to Hawaii F.O.B. mainland. The department's position was that nexus had been established by the presence of Taxpayer's employees in Hawaii, and facts supporting Taxpayer's delivery of goods to Hawaii. By stipulated judgment, the parties agreed that the state would receive the sum of \$101,185, representing 57% of the tax in controversy.

In Re Tax Appeal of the Boeing Company, T.A. No. 96-5320, Tax Appeal Court of the State of Hawaii In Re Tax Appeal of Computer Sciences Corporation, T.A. No. 97-5379, Tax Appeal Court of the State of Hawaii

Both cases involved whether taxpayers' work qualifies for the scientific contracts exemption for general excise tax purposes. The department asserted that both taxpayers' computer hardware and software design, development, integration, enhancement, maintenance and operation work did not qualify for the exemption because the work was not paid for with federally appropriated research and development (R & D) funds, was not performed at R & D facilities and did not involve primarily R & D. Both cases were settled by stipulated judgments. In Boeing, the parties agreed that the state would receive the sum of \$532,716, representing 72% of the tax in controversy. In Computer Sciences Corporation, the parties agreed that the state would receive \$65,692, representing approximately 70% of the tax in controversy.

In Re Tax Appeal of the Temple of Lord Chaitanya, T.A. No. 97-4762, Tax Appeal Court of the State of Hawaii

The issue in this case was whether Taxpayer's T-shirt distribution activity at Hanauma Bay and the Halona Blowhole was exempt from the general excise tax as religious activities, or subject to tax as activities designed primarily for the production of income. The parties, by stipulated judgment, agreed that the state would receive full payment of taxes in the sum of \$3,040.

OTHER MATTERS CLOSED

| | |
|---------------------|-----|
| Tax Appeals..... | 18 |
| Bankruptcies..... | 497 |
| Foreclosures..... | 112 |
| Subpoenas..... | 33 |
| Opinions..... | 17 |
| Contracts/Bids..... | 10 |
| Legislation..... | 41 |
| Miscellaneous..... | 30 |
| Criminal..... | 12 |

AMOUNTS COLLECTED

| | |
|--------------------|----------------|
| Tax Appeals..... | \$ 29,459,189 |
| Foreclosures..... | 40,832 |
| Bankruptcies..... | 1,653,305 |
| Miscellaneous..... | 65,134 |
| Criminal..... | <u>729,505</u> |
| Total..... | \$ 31,947,965 |

LEGISLATION

During its regular session, the 1998 legislature passed 19 tax-related bills, one of which was vetoed by the governor. The 18 bills that became law with the governor's approval are summarized here:

Act **Brief Description**

- | | |
|-----|--|
| 66 | Changes the definition of "claimant agency" to include the judiciary for the purposes of collecting outstanding fines and debts. Effective 4/29/98. |
| 103 | Makes wilful falsification of any return, statement, or other document required by the tax laws of Hawaii a class C felony. Provides that misstatements of the use tax shall be a misdemeanor. Effective 6/3/98. |
| 113 | Conforms Hawaii income tax law to Internal Revenue Code but does not adopt certain federal provisions such as the federal safe harbor provisions for underpayment of estimated tax. Effective 6/12/98; applies to taxable years beginning after 12/31/97. |
| 120 | Allows individuals who established an individual housing account (IHA) before 1/1/98 and who have not yet purchased a first residence to elect to be subject to the income reporting requirements that were effective when they originally invested in their IHAs. Effective 6/22/98; applies to taxable years beginning after 12/31/96. |
| 125 | Provides that where the transportation of passengers or property are furnished through arrangements between motor carriers, and the gross income is divided between the carriers, any public service company tax shall apply to each carrier with respect to each carrier's respective portion of the proceeds. Effective 6/22/98. |

- 143 Permits a person engaged in network marketing, multi-level marketing, or other similar business to obtain a single general excise tax license to collect and report general excise and use taxes on behalf of its direct sellers. Effective 7/2/98.
- 153 Permits the state to set off child, spousal, and medical support obligation amounts with state income tax refunds. Effective 7/7/98.
- 154 Establishes a foreign capital depository task force within the Department of Business, Economic Development and Tourism. Effective 7/7/98.
- 156 Increases transient accommodations tax (TAT) rate to 7.25%; subjects time shares to TAT; establishes Hawaii tourism authority; changes TAT revenue distribution. Effective 1/1/99.
- 157 Expands income tax brackets and lowers tax rates in three stages; repeals food tax credit and provides a refundable low-income tax credit. Effective 7/10/98; applies to taxable years beginning after 12/31/98.
- 163 Extends the duration of energy conservation income tax credits for an additional 4.5 years; provides that the credit will be reduced by the amount of any federal energy credits enacted after 6/30/98. Effective 7/1/98.
- 169 Requires a prime contractor who claims a general excise tax subcontract deduction to report the general excise tax number of the subcontractor paying the tax on the amount deducted; repeals the requirement that the subcontractor pay general excise taxes on its portion of the proceeds in order for the prime contractor to claim the deduction. Effective 7/14/98.
- 170 Reduces allocation of conveyance tax revenue to the rental housing trust fund from 25% to 12.5% for fiscal 1999 only and appropriates \$600,000 from the general fund for homeless assistance programs. Effective 7/1/98.
- 208 Clarifies eligibility requirements for the general excise tax exemption for amounts received from the servicing and maintenance of aircraft or from the construction of an aircraft service and maintenance facility. Effective 7/17/98; applies to taxable periods beginning after 6/30/97.
- 214 Exempts from the general excise tax amounts received by management companies as reimbursements of employee payroll costs incurred in managing or operating related entities selling telecommunications services. Effective 7/1/98.
- 245 Provides a general excise tax exemption for amounts received as grants under high technology research and development loans and grants provisions which are given to a business that receives a federal small business innovation research phase I award or contract. Effective 7/1/98.
- 247 Provides a general excise tax exemption for gross proceeds or gross income arising from the sale of tangible personal property imported to Hawaii from a foreign or domestic source to a licensed taxpayer for subsequent resale for the purpose of wholesale. Effective 7/1/98.
- 293 Authorizes the Department of Human Services to use tax offset as one method of recovering Medicaid overpayments. Effective 7/20/98.

INCOME ASSESSMENT AND AUDIT

INDIVIDUAL INCOME TAX

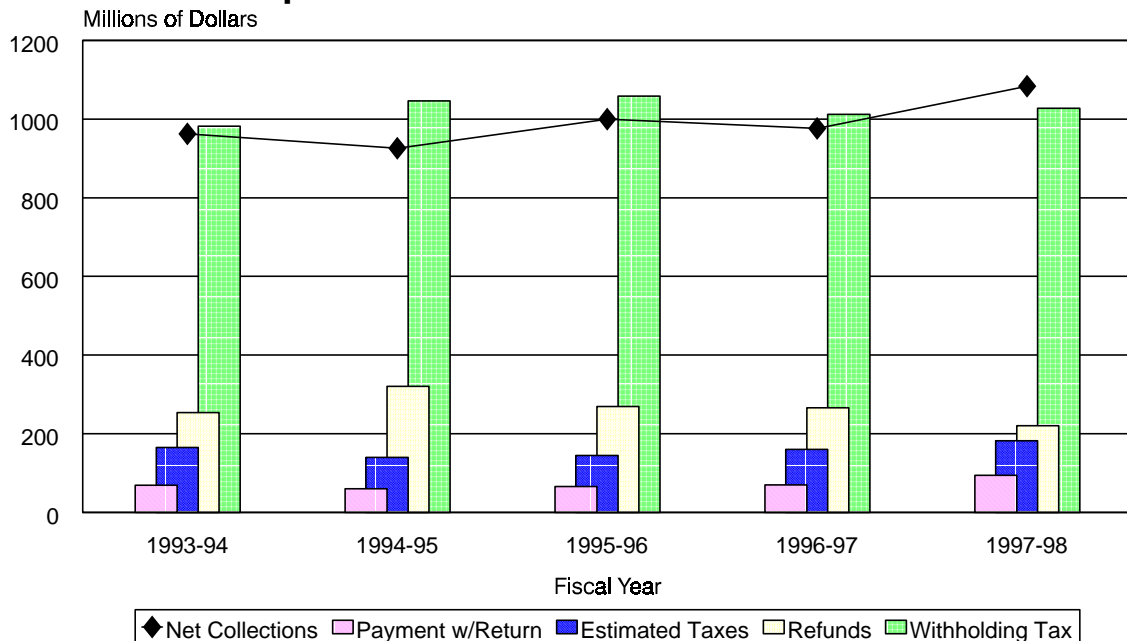
Act 187, SLH 1996, reduced the maximum withholding rate from 10% to 8%, a change implemented in October 1996. In the spring of 1998, taxpayers experienced the effect of a full year's worth of the lower withholding ceiling when they filed their tax year 1997 individual income tax returns. Because less tax was withheld, some taxpayers saw balances due increase as reflected in a 34% jump in the dollar volume of payments with returns. Others saw their refund amounts decrease or disappear altogether. During the primary tax filing season from January through June 1998, the number of taxpayers receiving individual income tax refunds fell by 32,672 or 8% to 418,823 as compared to 451,495 during the same period the previous year. Among those that did receive refunds during this period, the average refund declined to \$449 from \$506.

TAXES PAID BY INDIVIDUALS (In Thousands of Dollars)

| | FY 1998 | FY 1997 | Difference | |
|-------------------------------------|---------------------|-------------------|-------------------|-------------|
| | | | Amount | % |
| Declaration of Estimated Taxes..... | \$ 182,182 | \$ 160,481 | \$ 21,701 | 13.5 |
| Payment with Return..... | 94,194 | 70,281 | 23,913 | 34.0 |
| Withholding Tax on Wages..... | 1,027,746 | 1,011,876 | 15,870 | 1.6 |
| Subtotal..... | \$ 1,304,123 | \$ 1,242,638 | \$ 61,484 | 4.9 |
| Refunds..... | 220,472 | 266,327 | -45,856 | -17.2 |
| NET..... | <u>\$ 1,083,651</u> | <u>\$ 976,311</u> | <u>\$ 107,340</u> | <u>11.0</u> |

NOTE: Due to rounding, details may not add to total.

Components of the Individual Income Tax



These changes, together with a boost in estimated taxes, helped push overall individual income tax revenue for fiscal 1998 \$107 million ahead of the total for fiscal 1997. About \$35 million of this amount was due to the change in the maximum withholding rates. The remaining \$72 million translates into an increase of 6.6% in individual income tax revenue with the withholding effect factored out.

CORPORATE INCOME TAX

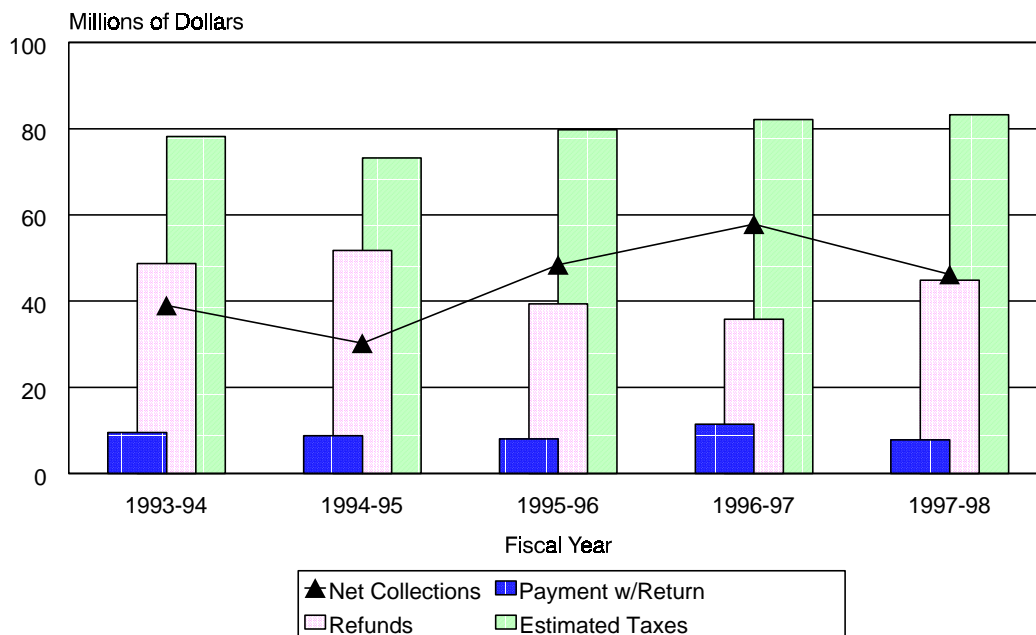
After two years of increases, net corporate income tax revenue declined 20% from \$57.8 million in fiscal 1997 to \$46.2 million in fiscal 1998. This decline was the result of a steep 32% drop in payments with returns and a hefty 25% increase in refunds. The level of estimated taxes remained increased by a slight amount.

TAXES PAID BY CORPORATIONS (In Thousands of Dollars)

| | FY 1998 | FY 1997 | Difference | |
|-------------------------------------|------------------|------------------|-------------------|--------------|
| | | | Amount | % |
| Declaration of Estimated Taxes..... | \$ 83,256 | \$ 82,165 | \$ 1,091 | 1.3 |
| Payment with Return..... | 7,779 | 11,452 | -3,673 | -32.1 |
| Subtotal..... | \$ 91,035 | \$ 93,618 | \$ -2,582 | -2.8 |
| Refunds..... | 44,826 | 35,778 | 9,048 | 25.3 |
| NET..... | \$ <u>46,209</u> | \$ <u>57,839</u> | \$ <u>-11,630</u> | <u>-20.1</u> |

NOTE: Due to rounding detail may not add to totals.

Components of the Corporate Income Tax



GENERAL EXCISE AND USE TAX BASE AND TAXES
FOR FISCAL YEARS ENDING JUNE 30, 1998 & 1997
(In Thousands of Dollars)

| SOURCE OF REVENUE | Rate | 1998 | 1997 | Difference | |
|----------------------------|------|----------------------|----------------------|----------------------|-------------|
| <u>TAX BASE</u> | | | | <u>Amount</u> | <u>%</u> |
| Retailing..... | | \$ 15,262,550 | \$ 16,002,192 | \$ -739,642 | -4.6 |
| Services..... | | 5,324,209 | 5,549,429 | -225,220 | -4.1 |
| Contracting..... | | 2,826,496 | 3,069,784 | -243,288 | -7.9 |
| Hotel Rentals..... | | 1,944,524 | 2,090,774 | -146,250 | -7.0 |
| All Other Rentals..... | | 3,663,879 | 3,816,477 | -152,598 | -4.0 |
| All Others (4%)..... | | <u>2,651,121</u> | <u>2,826,996</u> | <u>-175,875</u> | <u>-6.2</u> |
| Subtotal..... | | \$ <u>31,672,779</u> | \$ <u>33,355,652</u> | \$ <u>-1,682,873</u> | <u>-5.0</u> |
| Sugar Processing..... | | 9,404 | 10,110 | -706 | -7.0 |
| Pineapple Canning..... | | 4,790 | 4,889 | -99 | -2.0 |
| Producing..... | | 493,551 | 476,572 | 16,979 | 3.6 |
| Manufacturing..... | | 556,008 | 593,012 | -37,004 | -6.2 |
| Wholesaling..... | | 8,022,157 | 8,055,644 | -33,487 | -0.4 |
| Use (½%)..... | | 3,864,048 | 4,610,057 | -746,009 | -16.2 |
| Intermediary Services..... | | 286,812 | 290,153 | -3,341 | -1.2 |
| Insurance Commissions..... | | <u>803,617</u> | <u>547,329</u> | <u>256,288</u> | <u>46.8</u> |
| Subtotal..... | | \$ <u>14,040,387</u> | \$ <u>14,587,766</u> | \$ <u>-547,379</u> | <u>-3.8</u> |
| TOTAL-ALL ACTIVITIES..... | | \$ <u>45,713,166</u> | \$ <u>47,943,418</u> | \$ <u>-2,230,252</u> | <u>-4.7</u> |
| <u>TAX</u> | | | | | |
| Retailing..... | 4% | \$ 610,502 | \$ 640,088 | \$ -29,586 | -4.6 |
| Services..... | 4% | 212,968 | 221,977 | -9,009 | -4.1 |
| Contracting..... | 4% | 113,060 | 122,791 | -9,731 | -7.9 |
| Hotel Rentals..... | 4% | 77,781 | 83,631 | -5,850 | -7.0 |
| All Other Rentals..... | 4% | 146,555 | 152,659 | -6,104 | -4.0 |
| All Others..... | 4% | <u>106,045</u> | <u>113,080</u> | <u>-7,035</u> | <u>-6.2</u> |
| Subtotal..... | | \$ <u>1,266,911</u> | \$ <u>1,334,226</u> | \$ <u>-67,315</u> | <u>-5.0</u> |
| Sugar Processing..... | .50% | \$ 47 | \$ 51 | \$ -4 | -7.8 |
| Pineapple Canning..... | .50% | 24 | 24 | 0 | 0.0 |
| Producing..... | .50% | 2,468 | 2,383 | 85 | 3.6 |
| Manufacturing..... | .50% | 2,780 | 2,965 | -185 | -6.2 |
| Wholesaling..... | .50% | 40,111 | 40,278 | -167 | -0.4 |
| Use (½%)..... | .50% | 19,320 | 23,050 | -3,730 | -16.2 |
| Intermediary Services..... | .50% | 1,434 | 1,451 | -17 | -1.2 |
| Insurance Commissions..... | .15% | <u>1,205</u> | <u>821</u> | <u>384</u> | <u>46.8</u> |
| Subtotal..... | | \$ <u>67,389</u> | \$ <u>71,023</u> | \$ <u>-3,634</u> | <u>-5.1</u> |
| Unallocated*..... | | <u>91,051</u> | <u>52,025</u> | <u>39,026</u> | <u>75.0</u> |
| TOTAL-ALL ACTIVITIES..... | | \$ <u>1,425,351</u> | \$ <u>1,457,274</u> | \$ <u>-31,923</u> | <u>-2.2</u> |

NOTE: Due to rounding detail may not add to totals.

*Included are collections from penalty and interest, assessments and corrections, delinquent collections, refunds, protested payments, settlements, etc.

GENERAL EXCISE AND USE TAXES

General excise and use taxes comprise the largest source of revenue for the state of Hawaii. Overall revenue from this source declined 2.2% in fiscal 1998 when compared with fiscal 1997. This represented the first annual decline since 1961. As the accompanying table shows, nearly every general excise transaction category decreased.

TRANSIENT ACCOMMODATIONS TAX

During fiscal 1998, an increase in hotel room rates overcame a decline in hotel occupancy rates, allowing revenue from the transient accommodations tax to increase by \$1.6 million or 1.3% to \$127.1 million. As provided by law, one-sixth of this amount, or \$21.2 million, was deposited into the convention center capital and operations special fund. Of the remaining revenue, 5% or \$5.3 million was deposited into the state general fund to cover the cost of administering the tax. The remaining \$100.6 million was distributed to the counties according to a statutory formula, with 44.1% to Oahu, 22.8% to Maui, 18.6% to Hawaii and 14.5% to Kauai.

TRANSIENT ACCOMMODATIONS TAX

(In Thousands of Dollars)

| | FY 1998 | FY 1997 | Difference | |
|------------------------------------|-----------------|-----------------|--------------|------------|
| | | | Amount | % |
| Transient Accommodations Tax..... | \$ 127,076 | \$ 125,455 | \$ 1,621 | 1.3 |
| Transient Accommodations Fees..... | 5 | 6 | 0 | -5.9 |
| SUB-TOTAL..... | \$ 127,081 | \$ 125,461 | \$ 1,620 | 1.3 |
| Counties Share..... | 100,602 | 99,319 | 1,283 | 1.3 |
| Convention Center Fund..... | 21,179 | 20,909 | 270 | 1.3 |
| Net Addition to General Fund..... | \$ <u>5,300</u> | \$ <u>5,233</u> | \$ <u>67</u> | <u>1.3</u> |

Note: Due to rounding, detail may not add to totals.

FUEL AND MOTOR VEHICLE TAXES

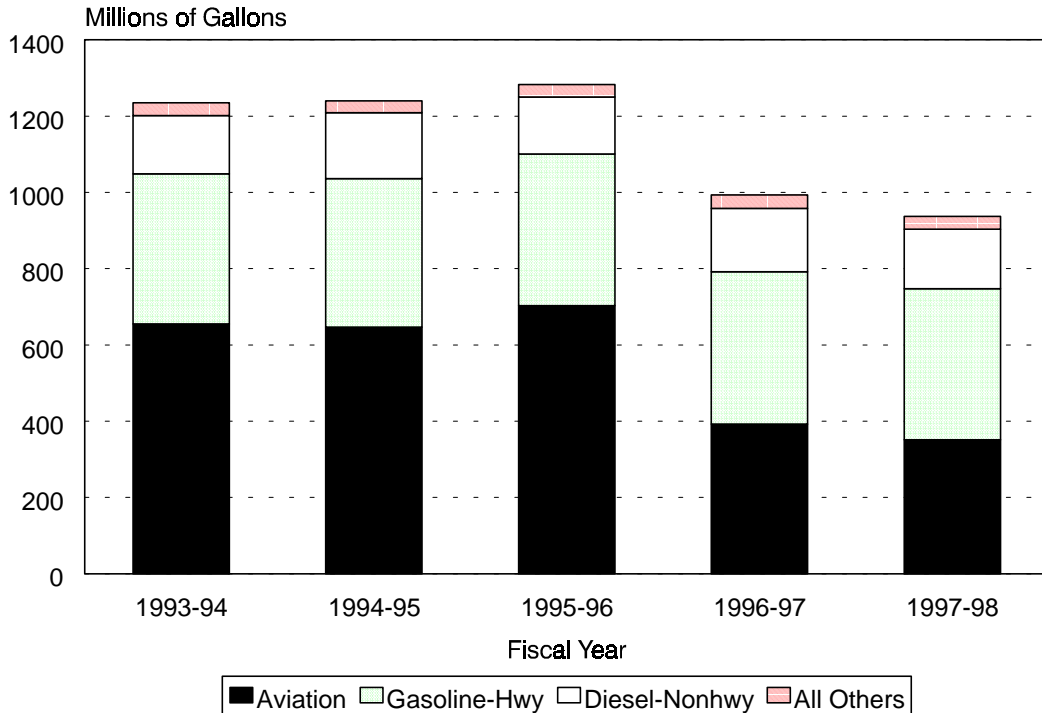
The state highway fund receives 99% of the revenue from state fuel taxes, all of the revenue from state motor vehicle weight taxes and registration fees, and all of the revenue from the state rental and tour vehicle surcharge tax. During fiscal 1998, fuel taxes contributed \$68.8 million to this fund. This represented a decrease of \$1.1 million as a result of a small decline in the consumption of gasoline and other taxable fuels. This decrease was nearly offset by moderate increases in revenue from the motor vehicle and rental vehicle taxes, which contributed \$40.7 and \$22.8 million, respectively, to the state highway fund. Thus, fiscal 1998 deposits into the state highway fund totaled \$132.3 million, only \$0.2 million less than in fiscal 1997.

GALLONS OF FUEL CONSUMED
(In Thousands of Gallons)

| | <u>FY 1998</u> | <u>FY 1997</u> | <u>Difference</u> | |
|----------------------------------|-----------------------|-----------------------|-----------------------|--------------------|
| | | | <u>Amount</u> | <u>%</u> |
| Gasoline..... | 395,866 | 399,327 | -3,462 | -0.9 |
| Diesel Oil - Nonhighway..... | 156,597 | 165,862 | -9,265 | -5.6 |
| Diesel Oil - Highway..... | 29,015 | 31,279 | -2,263 | -7.2 |
| Liq. Pet. Gas - Off Highway..... | 3,446 | 3,462 | -16 | -0.5 |
| Liq. Pet. Gas - Highway..... | 375 | 365 | 11 | 2.9 |
| Small Boats - Gasoline..... | 26 | 45 | -19 | -42.9 |
| Small Boats - Diesel Oil..... | 168 | 183 | -15 | -8.1 |
| Aviation Fuel..... | <u>351,470</u> | <u>392,652</u> | <u>-41,182</u> | <u>-10.5</u> |
| TOTAL-GALLONS..... | <u>936,963</u> | <u>993,175</u> | <u>-56,211</u> | <u>-5.7</u> |
| Environmental Tax (Barrels)..... | 33,928 | 35,624 | -1,696 | -4.8 |

NOTE: Due to rounding detail may not add to totals.

Trends in Fuel Consumption Tax Base

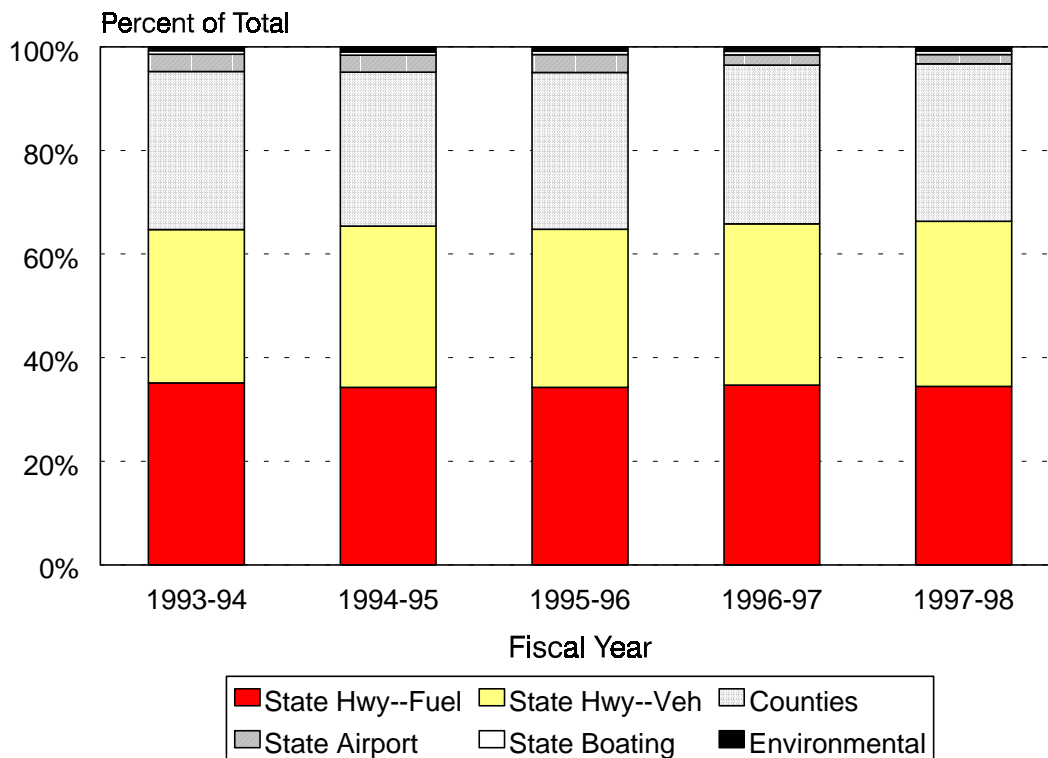


Effective July 1, 1996, the state 1¢ per gallon aviation fuel tax was no longer imposed on the sale of bonded aviation and jet fuel to air carriers departing for or arriving from foreign ports before continuing on to their final destinations. Most of the year-to-year effect of this change was seen between fiscal 1996 and fiscal 1997, as shown in the accompanying chart depicting the taxable fuel consumption base. However, due to the one-month delay between imposition and reporting of fuel taxes, one month's worth of the year-to-year change resulting from the aviation fuel tax change shows up when comparing fiscal 1997 and fiscal 1998. This is the major reason why aviation fuel tax deposited into the state airport fund fell 10.5% from \$3.9 million in fiscal 1997 to \$3.5 million in fiscal 1998.

An environmental response tax of five cents is levied on each barrel of petroleum products sold by a distributor to any retail dealer or end user other than a refiner of petroleum products. This tax, which amounted to \$1.7 million in fiscal 1998, is deposited into a special fund administered by the Department of Health for its oil spill prevention and remediation programs. The state boating fund is the recipient of 1% of all state and county fuel taxes except the aviation fuel tax.

The Department of Taxation collects fuel taxes for both the state and the counties. The county highway funds receive 99% of county fuel taxes. In fiscal 1998, the department distributed \$60.7 million to the county highway funds, down from \$61.7 million the previous year. One percent of all state and county fuel taxes except the aviation fuel tax is reserved for the state boating fund. This fund received \$1.3 million in fuel tax revenue in fiscal 1998.

Distribution of Fuel Tax Collections by Type of Fund



ALLOCATION OF FUEL TAXES

(In Thousands of Dollars; Percent Difference Computed on Unrounded Amounts)

| | <u>FY 1998</u> | <u>FY 1997</u> | <u>Difference</u> | |
|---|-------------------|-------------------|-------------------|---------------|
| | | | <u>Amount</u> | <u>%</u> |
| STATE HIGHWAY FUND: | | | | |
| Gasoline..... | \$ 62,564 | \$ 63,208 | \$ -644 | -1.0% |
| Diesel Oil - Nonhighway..... | 1,552 | 1,644 | -92 | -5.6% |
| Diesel Oil - Highway..... | 4,596 | 4,954 | -358 | -7.2% |
| Liquid Petroleum Gas - Off Highway..... | 34 | 34 | 0 | -0.5% |
| Liquid Petroleum Gas - Highway..... | 41 | 40 | 1 | 2.9% |
| Subtotal..... | <u>\$ 68,787</u> | <u>\$ 69,881</u> | <u>\$ -1,093</u> | <u>-1.6%</u> |
| Motor Vehicle Weight Tax/Reg. Fees..... | 40,710 | 40,021 | 689 | 1.7% |
| Rental Vehicle Surcharge Tax/Fees..... | 22,838 | 22,601 | 238 | 1.1% |
| TOTAL..... | <u>\$ 132,335</u> | <u>\$ 132,502</u> | <u>\$ -166</u> | <u>-0.1%</u> |
| COUNTY HIGHWAY FUNDS: | | | | |
| City & County of Honolulu..... | \$ 45,214 | \$ 46,227 | \$ -1,012 | -2.2% |
| County of Maui..... | 7,212 | 7,215 | -3 | 0.0% |
| County of Hawaii..... | 5,816 | 5,855 | -39 | -0.7% |
| County of Kauai..... | 2,439 | 2,404 | 35 | 1.5% |
| TOTAL..... | <u>\$ 60,681</u> | <u>\$ 61,700</u> | <u>\$ -1,019</u> | <u>-1.7%</u> |
| BOATING SPECIAL FUND..... | <u>\$ 1,308</u> | <u>\$ 1,329</u> | <u>\$ -21</u> | <u>-1.6%</u> |
| STATE AIRPORT FUND: | | | | |
| Aviation Fuel..... | <u>\$ 3,515</u> | <u>\$ 3,927</u> | <u>\$ -412</u> | <u>-10.5%</u> |
| ENVIRONMENTAL TAX FUND..... | <u>\$ 1,696</u> | <u>\$ 1,781</u> | <u>\$ -85</u> | <u>-4.8%</u> |

State fuel tax rates are set by the state legislature while the county councils set the county rates. The effective rates for fiscal year 1998 are summarized below:

FUEL TAX RATES PER GALLON¹

| | <u>State</u> | <u>County</u> | <u>Total</u> |
|--|--------------|---------------|--------------|
| GASOLINE AND DIESEL OIL (HWY. USE):² | | | |
| City & County of Honolulu | 16.0¢ | 16.5¢ | 32.5¢ |
| County of Maui | 16.0¢ | 13.0¢ | 29.0¢ |
| County of Hawaii | 16.0¢ | 8.8¢ | 24.8¢ |
| County of Kauai | 16.0¢ | 10.0¢ | 26.0¢ |
| LIQUID PETROLEUM GAS (HWY. USE): | | | |
| City & County of Honolulu | 11.0¢ | 11.0¢ | 22.0¢ |
| County of Maui | 11.0¢ | 9.0¢ | 20.0¢ |
| County of Hawaii | 11.0¢ | 6.0¢ | 17.0¢ |
| County of Kauai | 11.0¢ | 7.0¢ | 18.0¢ |
| ENVIRONMENTAL RESPONSE TAX (per barrel) | | | |
| All Counties | 5.0¢ | - | 5.0¢ |

¹Gasoline used for agricultural equipment off highways, aviation fuel, and all other fuels used off highways are taxed by the state at 1¢ per gallon.

²Includes 1¢ state license tax on diesel oil.

PUBLIC SERVICE COMPANY TAXES

Public service company taxes paid by public utilities and motor carriers-contract carriers increased 5.2% to \$120.3 million. Collections from public utilities rose \$1.7 million from \$98.3 million to \$100.0 million while revenues from motor carriers-contract carriers advanced \$4.1 million to \$19.6 million.

PUBLIC SERVICE COMPANY TAXES (In Thousands of Dollars)

| | <u>FY 1998</u> | <u>FY 1997</u> | <u>Difference</u> | |
|-----------------------------------|-------------------|-------------------|-------------------|------------|
| | | | <u>Amount</u> | <u>%</u> |
| Public Service Company Taxes..... | \$ 119,651 | \$ 113,871 | 5,780 | 5.1 |
| Penalty & Interest..... | 675 | 493 | 182 | 36.9 |
| TOTAL..... | <u>\$ 120,326</u> | <u>\$ 114,364</u> | <u>5,962</u> | <u>5.2</u> |

NOTE: Due to rounding detail may not add to totals.

ESTATE AND TRANSFER TAXES

Estates settled during fiscal 1998 numbered 2,137, up 7% from 1,996 the year before. The number of taxable estates increased 33% to 398 from 300 the previous year. However, due to the smaller size of the estates settled during fiscal 1998, estate tax revenue declined 5.4% from \$19.9 million to \$18.9 million.

Estates of persons who passed away before June 30, 1983 were subject to the inheritance tax. After that date, only those estates subject to the federal estate tax are subject to the Hawaii estate tax.

ESTATE AND TRANSFER TAXES (In Thousands of Dollars)

| | <u>FY 1998</u> | <u>FY 1997</u> | <u>Difference</u> | |
|-------------------------|------------------|------------------|-------------------|--------------|
| | | | <u>Amount</u> | <u>%</u> |
| Estate Tax..... | \$ 18,859 | \$ 19,930 | \$ -1,071 | -5.4 |
| Penalty & Interest..... | 787 | 2,239 | -1,452 | -64.9 |
| TOTAL | <u>\$ 19,645</u> | <u>\$ 22,169</u> | <u>\$ -2,524</u> | <u>-11.4</u> |

NOTE: Due to rounding detail may not add to totals.

OTHER TAXES

Banks and other financial corporations that are not subject to the corporate income tax must pay a franchise tax instead on their taxable income. Franchise tax collections for fiscal 1998 increased nearly 60% from fiscal 1997, a year characterized by unusually large refunds resulting from net operating losses. Fiscal 1998 franchise tax revenue was 9% less than the \$17.1 million collected in fiscal 1996.

A measure of the dollar volume of real estate transactions, the conveyance tax is imposed at a rate of 10 cents per \$100 of actual consideration and is collected by the Department of Land and Natural Resources. After several years of declines reflecting a deteriorating real estate market, conveyance tax collections increased by 5.9% in fiscal 1997 and then by 15.3% in fiscal 1998. These developments may signify a bottoming out of the real estate market and perhaps a gradual recovery. One-half of conveyance tax collections, or \$3.5 million in fiscal 1998, is deposited into the state general fund. One-fourth is deposited into the state rental housing fund and the remaining fourth is deposited into the state natural area reserve fund.

MISCELLANEOUS TAXES
(In Thousands of Dollars)

| | FY 1998 | FY 1997 | Difference | |
|---|--------------------------|--------------------------|-------------------------|--------------------|
| | | | Amount | % |
| Banks & Other Financial Corporations..... | \$ 15,546 | \$ 9,731 | \$ 5,815 | 59.8 |
| Conveyance* | 6,926 | 6,007 | 919 | 15.3 |
| Employment Security Contributions..... | 155,062 | 169,984 | -14,922 | -8.8 |
| Insurance Premiums..... | 59,443 | 55,847 | 3,596 | 6.4 |
| Liquor & Permits | 38,894 | 38,347 | 547 | 1.4 |
| Tobacco & Licenses..... | 36,098 | 36,427 | -330 | -0.9 |
| General Excise Licenses & Fees..... | 552 | 633 | -80 | -12.7 |
| TOTAL..... | <u>\$ 312,520</u> | <u>\$ 316,975</u> | <u>\$ -4,455</u> | <u>-1.4</u> |

*Includes allocation to "Rental Housing Fund" and "Natural Area Reserve Fund".

NOTE: Due to rounding detail may not add to totals.

COLLECTION AND ACCOUNTING OF TAXES

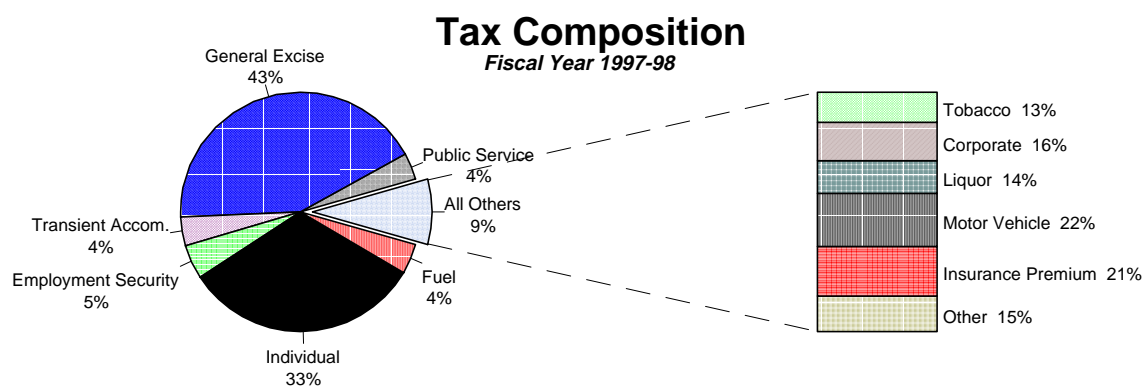
TAX COLLECTIONS

Net tax collections by and for the Department of Taxation amounted to \$3,334.3 million, \$62.7 million or 1.9% more than the amount collected the previous fiscal year. This total includes \$6.9 million in conveyance taxes collected by the Department of Land and Natural Resources, \$59.4 million in insurance premium taxes collected by the Department of Commerce and Consumer Affairs, and \$40.7 million in state motor vehicle weight taxes and registration fees collected by the counties.

TAX COLLECTIONS

| SOURCE OF REVENUE | FY 1998 | | FY 1997 | |
|--|-------------------------------|-----------------------|-------------------------------|-----------------------|
| | Amount Collected | % of Total | Amount Collected | % of Total |
| Banks - Financial Corporations..... | \$15,545,923 | 0.47% | \$9,730,590 | 0.30% |
| Conveyance..... | 6,925,845 | 0.21% | 6,006,707 | 0.18% |
| Employment Security Contributions..... | 155,062,026 | 4.65% | 169,983,877 | 5.20% |
| Fuel..... | 135,986,491 | 4.08% | 138,617,851 | 4.24% |
| General Excise & Use..... | 1,425,351,609 | 42.75% | 1,457,274,037 | 44.54% |
| Income - Corporations..... | 46,209,211 | 1.39% | 57,839,460 | 1.77% |
| Income - Individuals..... | 1,083,650,828 | 32.50% | 976,311,103 | 29.84% |
| Inheritance and Estate..... | 19,645,452 | 0.59% | 22,169,104 | 0.68% |
| Insurance Premiums..... | 59,442,790 | 1.78% | 55,846,717 | 1.71% |
| Liquor & Permits..... | 38,893,767 | 1.17% | 38,347,177 | 1.17% |
| Motor Vehicle Tax* | 63,548,765 | 1.91% | 62,621,240 | 1.91% |
| Public Service Companies..... | 120,326,236 | 3.61% | 114,364,015 | 3.50% |
| Tobacco & Licenses..... | 36,097,674 | 1.08% | 36,427,347 | 1.11% |
| Transient Accommodations Tax..... | 127,075,888 | 3.81% | 125,455,218 | 3.83% |
| All Others..... | 543,323 | 0.02% | 646,805 | 0.02% |
| TOTAL | <u>\$3,334,305,828</u> | <u>100.00%</u> | <u>\$3,271,641,248</u> | <u>100.00%</u> |

*Includes Motor Vehicle Weight Tax, Registration Fees, Commercial Driver's License, Periodic Motor Vehicle Inspection, Rental Vehicle Registration Fees, and Rental Vehicle Surcharge Tax.



Of the total of \$3,334.3 million in taxes collected by and for the state, 85.5% was distributed to the state general fund. The counties received \$161.3 million or 4.8% of the total as their share of fuel and transient accommodation tax revenues. State special funds received the remaining 9.7% of the total. Largest in terms of the dollar volume of the distribution was the \$155.1 million in dedicated employment security contributions that went to the unemployment trust fund administered by the Department of Labor and Industrial Relations. Next in size was the \$132.3 million in fuel and motor vehicle taxes that went to the state highway fund. Third in size was the \$21.2 million in transient accommodations taxes that accrued to the convention center fund. Receiving \$3.5 million in aviation fuel taxes was the state airport fund, while the boating special fund received \$1.3 million, which represented 1% of state and county fuel taxes other than those on aviation fuel. The beneficiary of \$1.7 million from the five-cent-per-barrel tax on petroleum products was the environmental response revolving fund. As was done in previous years, \$5 million in general excise taxes was transferred to the bond reserve fund. The rental housing fund and the natural area reserve fund each received one-fourth of conveyance tax revenue, or \$1.7 million each in fiscal 1998, as required by statute. As authorized by taxpayers who checked the appropriate box on their individual income tax returns, the election campaign fund received \$0.3 million in individual income tax revenue.

DISTRIBUTION OF COLLECTIONS

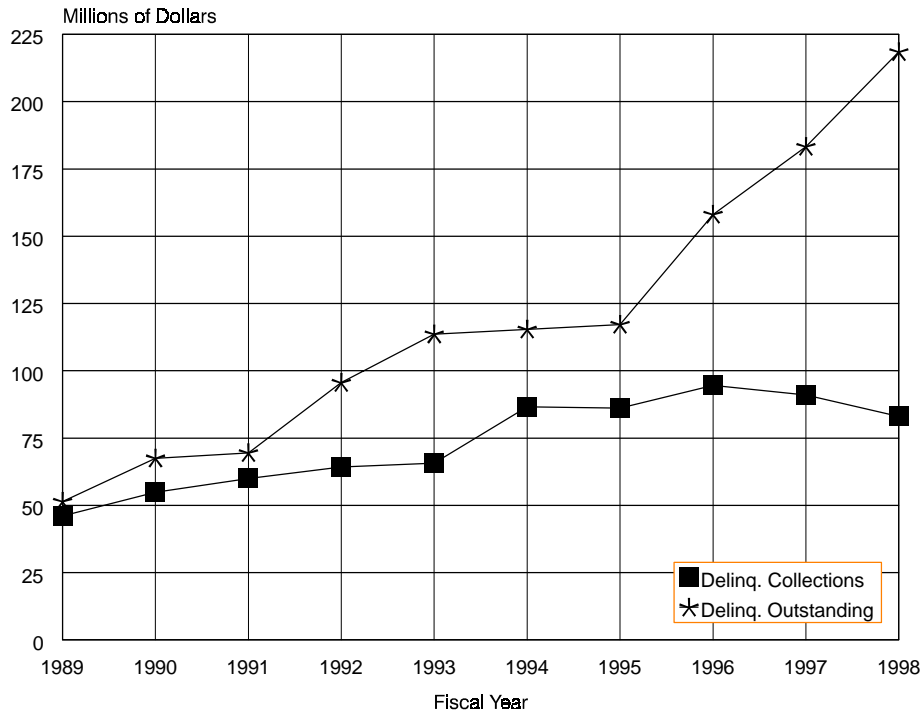
| | FY 1998 | | FY 1997 | |
|--|--------------------------------------|------------------------------|--------------------------------------|------------------------------|
| | Amount Collected | % of Total | Amount Collected | % of Total |
| STATE FUNDS: | | | | |
| State General..... | \$2,849,184,230 | 85.45% | \$2,771,881,205 | 84.72% |
| State Highway..... | 132,335,385 | 3.97% | 132,501,879 | 4.05% |
| State Airport..... | 3,514,701 | 0.11% | 3,926,523 | 0.12% |
| Boating Special Fund..... | 1,307,754 | 0.04% | 1,329,101 | 0.04% |
| Environmental Fund..... | 1,696,415 | 0.05% | 1,781,222 | 0.05% |
| Bond Reserve Fund..... | 5,000,000 | 0.15% | 5,000,000 | 0.15% |
| Unemployment Trust..... | 155,062,026 | 4.65% | 169,983,877 | 5.20% |
| Election Campaign Fund..... | 280,334 | 0.01% | 305,804 | 0.01% |
| Tax Administration Fund..... | 0 | 0.00% | 0 | 0.00% |
| Rental Housing Fund..... | 1,731,461 | 0.05% | 1,501,677 | 0.05% |
| Natural Area Reserve Fund..... | 1,731,461 | 0.05% | 1,501,677 | 0.05% |
| Convention Center Fund..... | 21,179,315 | 0.64% | 20,909,203 | 0.64% |
| Subtotal - State..... | <u>\$3,173,023,082</u> | 95.16% | <u>\$3,110,622,168</u> | 95.08% |
| REVENUES TRANSFERRED TO COUNTIES: | | | | |
| Fuel..... | 60,681,001 | 1.82% | 61,700,365 | 1.89% |
| Transient Accommodations Tax | 100,601,745 | 3.02% | 99,318,714 | 3.04% |
| Subtotal - Counties..... | <u>\$161,282,746</u> | 4.84% | <u>\$161,019,079</u> | 4.92% |
| TOTAL..... | <u><u>\$3,334,305,828</u></u> | <u><u>100.00%</u></u> | <u><u>\$3,271,641,247</u></u> | <u><u>100.00%</u></u> |

NOTE: Due to rounding detail may not add to totals.

DELINQUENT TAXES

Outstanding delinquent taxes at the end of fiscal 1998 stood at \$218.5 million, which was \$35.2 million more than the amount outstanding at the end of fiscal 1997. Meanwhile, cash collected fell \$8.0 million to \$83.0 million.

Delinquent Taxes Collected and Outstanding



BRIEF SUMMARY OF HAWAII'S TAX SYSTEM

Two notable characteristics of Hawaii's tax structure are the high degree of centralization at the state level and the broad-based nature of its primary revenue source, the general excise tax. Hawaii's general excise tax is imposed on most sales of goods and services. Some transactions are exempted because they are subject to other taxes or because the legislature wished to encourage certain economic activities.

To counter the broad-based nature of the general excise tax, the individual income tax has rates that are inversely graduated against income and provides a system of credits, including a flat food credit, an income-based renter's credit, and an income-graduated dependent care credit. Other credits were introduced to encourage specific taxpayer behavior. Examples are the energy device credit, the capital goods excise tax credit, and the child passenger restraint system credit.

Hawaii has seventeen separate tax laws, of which fourteen are administered by the state. The remaining three -- the real property tax, the motor vehicle weight tax, and the public utility franchise tax -- are administered by the counties. Until July 1, 1981, the real property tax law was administered by the state, with revenue from this source accruing to the counties. At present, the counties administer all of the real property functions. Administration of the state and county motor vehicle weight taxes is vested in the counties with the revenue accruing to the state and county highway funds.

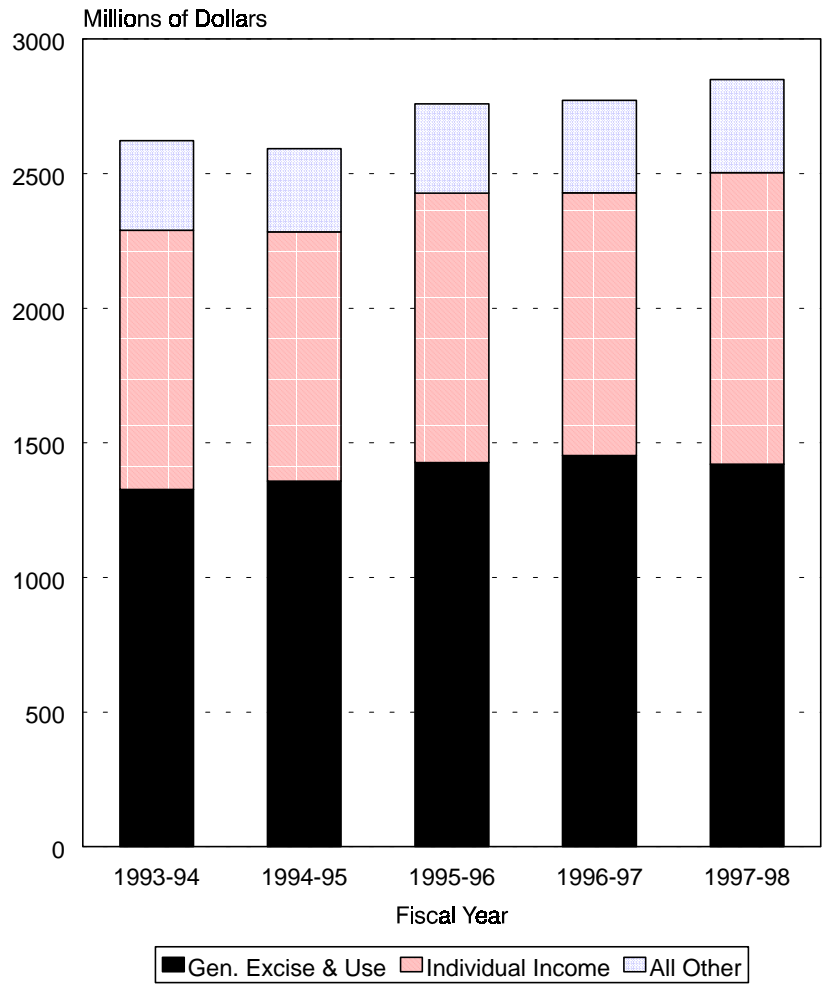
Revenues from eleven of the state-administered taxes go into the state's general fund and are used to provide government services, including public education, which is a state function in Hawaii. Although the fuel tax is administered by the state, it is a source of revenue for both the state and county highway funds. The employment security tax is a dedicated tax used exclusively to provide benefits to covered unemployed workers. Rental motor vehicle and tour vehicle surcharge taxes are deposited into the state highway fund.

STATE GENERAL FUND

| SOURCE OF REVENUE | FY 1998 | | FY 1997 | |
|-------------------------------------|-------------------------------|-----------------------|-------------------------------|-----------------------|
| | Amount Collected | % of Total | Amount Collected | % of Total |
| Banks - Financial Corporations..... | \$15,545,923 | 0.55% | \$9,730,590 | 0.35% |
| Conveyance..... | 3,462,922 | 0.12% | 3,003,353 | 0.11% |
| General Excise & Use..... | 1,420,351,609 | 49.85% | 1,452,274,037 | 52.39% |
| Income - Corporations..... | 46,209,210 | 1.62% | 57,839,460 | 2.09% |
| Income - Individuals..... | 1,083,370,494 | 38.02% | 976,005,299 | 35.21% |
| Inheritance & Estate..... | 19,645,452 | 0.69% | 22,169,104 | 0.80% |
| Insurance Premiums..... | 59,442,790 | 2.09% | 55,846,717 | 2.01% |
| Liquor & Licenses..... | 38,893,767 | 1.37% | 38,347,177 | 1.38% |
| Public Service Companies..... | 120,326,236 | 4.22% | 114,364,015 | 4.13% |
| Tobacco & Licenses..... | 36,097,674 | 1.27% | 36,427,347 | 1.31% |
| Transient Accommodations Tax..... | 5,294,829 | 0.19% | 5,227,301 | 0.19% |
| All Others..... | 543,323 | 0.02% | 646,805 | 0.02% |
| TOTAL..... | <u>\$2,849,184,229</u> | <u>100.00%</u> | <u>\$2,771,881,205</u> | <u>100.00%</u> |

NOTE: Due to rounding detail may not add to totals.

Trends in General Fund Revenue



OUTLINE OF THE HAWAII TAX SYSTEM AS OF JULY 1, 1998

Issued by the Department of Taxation

| KIND OF TAX & LEGAL REFERENCES (HAWAII REVISED STATUTES) | MEASURE AND RATE OF TAX | REPORTS | TAX PAYABLE |
|--|---|---|--|
| <p>(1) Net Income</p> <p>Chapter 235 — Section 235-1 to 235-130</p> | <p>Tax rates for individuals as well as estates and trusts range from 2.0% to 10.0% of taxable income. Act 157, SLH 1998, reduces the income tax rates and phases them in over a 4-year period. For taxable years beginning after December 31, 1998 (and before January 1, 2001), the tax rates range from 1.6% to 8.75% of taxable income. The allowable standard deduction amounts vary by filing status. The standard deduction amount for married filing joint return or surviving spouse with dependent child is \$1,900; single is \$1,500; head of household is \$1,650; and married filing separately is \$950. Tax rates for corporations are 4.4% up to \$25,000, 5.4% over \$25,000 but not over \$100,000, and 6.4% over \$100,000.</p> | <p>Returns due 20th day of 4th month following the close of taxable year. Withholding returns due monthly on or before the 15th day of the following calendar month. When the total tax liability is less than \$1,000 for the calendar year, returns may be filed quarterly on or before the 15th day of the month after the close of each quarter. For employers whose liability for taxes withheld exceeds \$100,000 a year, withholding returns due monthly on or before the 10th day of the following calendar month. An annual employer's return and reconciliation of Hawaii income tax withheld, Form HW-3, must be filed together with a duplicate copy of each employee's tax statement, Form HW-2, on or before the last day of February following the close of the calendar year. Estimates of income of individuals not subject to withholding, estates, trusts, and corporations, April 20th.</p> | <p>In general, at time of filing returns. Estimates of individuals, estates, trusts, and corporations, one-quarter, April 20th; June 20th; September 20th; and January 20th.</p> |
| <p>(2) Estate and Transfer (for decedents dying after 6/30/83)</p> <p>Chapter 236D — Section 236D-1 to 236D-18</p> | <p>Every resident decedent is taxed on transfer of taxable estate equal to federal credit for estate death taxes allowed by IRC section 2011. Credit is allowed for death tax imposed by another state not qualified by reciprocal provision. For nonresident decedent, tax is based on transfer of taxable estate located in Hawaii by use of ratio. Exemption afforded resident estate equally applicable to nonresident, with certain exceptions.</p> <p>For generation-skipping transfers after June 30, 1994, a tax in an amount equal to the federal credit is imposed on every generation-skipping transfer of (1) property located in Hawaii and (2) property from a resident trust.</p> | <p>Report (Form M-6) must be filed by person responsible for filing federal Estate Tax Return (federal Form 706). No report required and no tax due when federal Form 706 not required. To obtain release of property, file Request for Release (Form M-6A).</p> <p>Report (Form M-6GS) must be filed by person responsible for filing Generation-Skipping Transfer Tax Return for Distributions (federal Form 706GS(D)) or Generation-Skipping Transfer Tax Return for Terminations (federal Form 706GS(T)).</p> | <p>On or before the due date for filing federal Form 706, including extensions of time; provided extension is submitted to Hawaii within 30 days of issuance.</p> <p>On or before the due date for filing federal Form 706GS(D) or 706GS(T), including extensions of time; provided extension is submitted to Hawaii within 30 days of issuance.</p> |
| <p>(3) General Excise (Gross Income)</p> <p>Chapter 237 — Section 237-1 to 237-49</p> | <p>This is a business privilege tax measured by gross proceeds of sales or gross income. The tax rate is 1/2 of 1% on wholesaling and intermediary services, producing, manufacturing, sugar processing and pineapple canning; all other activities (retailing business and professional services, contracting, theatre, amusement, radio, interest, commissions, rentals) are taxed 4%, except insurance commissions received by general agents, subagents and solicitors who are taxed at .15%. The licensing fee for general excise tax licensees and nonprofit organizations is a one-time fee of \$20.</p> | <p>Monthly returns are due on or before the last day of the following month. When the total tax liability does not exceed \$2,000 for the calendar or fiscal year, returns may be filed quarterly on or before the last day of the month after the close of each quarter. When the total tax liability does not exceed \$1,000 for the calendar or fiscal year, returns may be filed semiannually on or before the last day of the month after the close of each semiannual period. An annual summary and reconciliation return must be filed on or before the 20th day of the 4th month following the close of the taxable year.</p> | <p>At time of filing returns.</p> |
| <p>(4) Transient Accommodations Tax</p> <p>Chapter 237D — Section 237D-1 to 237D-16</p> | <p>This is a tax levied on the furnishing of a room, apartment, suite, or the like which is customarily occupied by the transient for less than 180 consecutive days for each letting by a hotel, apartment, motel, horizontal property regime or cooperative apartment, rooming house, or other place in which lodgings are regularly furnished to transients for consideration. The tax is imposed at the rate of 6%. The registration fee for transient accommodations operators is a one-time fee of \$5 for each registration consisting of 1 to 5 units and \$15 for 6 or more units. Effective January 1, 1999, Act 156, SLH 1998, increases the transient accommodations tax to 7.25% and imposes the transient accommodations tax of 7.25% on the fair market rental value of time share vacation units.</p> | <p>Monthly returns are due on or before the last day of the following month. When the total tax liability does not exceed \$2,000 for the calendar or fiscal year, returns may be filed quarterly on or before the last day of the month after the close of each quarter. When the total tax liability does not exceed \$1,000 for the calendar or fiscal year, returns may be filed semiannually on or before the last day of the month after the close of each semiannual period. An annual summary and reconciliation return must be filed on or before the 20th day of the 4th month following the close of the taxable year.</p> | <p>At time of filing returns.</p> |

| KIND OF TAX & LEGAL REFERENCES (HAWAII REVISED STATUTES) | MEASURE AND RATE OF TAX | REPORTS | TAX PAYABLE |
|--|--|---|---|
| <p>(5) Use Chapter 238 — Section 238-1 to 238-16</p> | <p>This is an excise tax levied on tangible personal property which is imported or purchased from an unlicensed seller for use in the State. The tax is based upon the purchase price or value of the tangible personal property purchased or imported, whichever is applicable. Rates: 1/2 of 1%, if for resale at retail; 4%, if for use or consumption. For exceptions, see sections 238-3 and 238-4.</p> | <p>Monthly returns are due on or before the last day of the following month. When the total tax liability does not exceed \$2,000 for the calendar or fiscal year, returns may be filed quarterly on or before the last day of the month after the close of each quarter. An annual summary and reconciliation return must be filed on or before the 20th day of the 4th month following the close of the taxable year. These returns have been consolidated with the general excise (gross income) tax returns and are filed simultaneously.</p> | <p>At time of filing returns.</p> |
| <p>(6) Public Service Company Chapter 239 — Section 239-1 to 239-11</p> | <p>Nature of Tax—(1) Public utility business in lieu of general excise and real property taxes. (a) Measurement of assessment—general rule: Gross income from public utility business of public utilities for preceding calendar year. For exception, see section 239-9. (b) Rates: (i) Gross income from passenger fares for transportation between points on a scheduled route by a carrier of passengers, 5.35%. (ii) Sale of its products or services to another public utility which resells such products or services, 1/2 of 1%. (iii) All other revenues: If ratio of net to gross income is 15% or less, 5.885%; for each 1% increase in ratio of net to gross, rate increase .2675%. (2) Motor carrier, common carrier by water and contract carrier business (other than motor carrier business) in lieu of general excise tax. (a) Measurement of assessment—general rule: Gross income from motor carrier, common carrier by water and contract carrier business for preceding calendar year. For exception, see sections 239-9 and 239-11. (b) Rate: 4% of gross income.</p> | <p>Returns filed on or before the 20th day of the 4th month following the close of the taxable year, based upon operations of the preceding taxable year.</p> | <p>First installment at the time of filing return, or, on or before the 20th day of the 4th month. Other installments due on the 20th day of the 2nd, 5th, and 8th month thereafter. If the total tax liability for the taxable year exceeds \$100,000, 1st installment on or before the 10th day of the 1st month. Remaining installments due on or before the 10th day of each calendar month thereafter.</p> |
| <p>(7) Banks, Building and Loan, Financial Services Loan Companies and Certain Other Financial Corporations Chapter 241 — Section 241-1 to 241-7</p> | <p>(1)(a) Assessment Date: January 1. (b) Nature of Tax: a franchise tax on banks; building and loan associations; development companies, financial corporations, financial services loan companies, trust companies, mortgage loan companies, financial holding companies, small business investment companies, or subsidiaries not subject to the tax imposed by chapter 235. Specific exempt activities are enumerated under chapter 237. (2) Measure of Assessment: Net income for the preceding year from all sources as defined by chapter 235 (Income Tax Law) with modifications. (3) Rate: 7.92% of taxable income.</p> | <p>Returns filed on or before the 20th day of the 4th month following the close of the taxable year, based upon operations of the preceding taxable year.</p> | <p>First installment at the time of filing return, or, on or before the 20th day of the 4th month. Other installments due on the 20th day of the 2nd, 5th and 8th month thereafter. If the total tax liability for the taxable year exceeds \$100,000, 1st installment on or before the 10th day of the 1st month. Remaining installments due on or before the 10th day of each calendar month thereafter.</p> |

| KIND OF TAX & LEGAL REFERENCES (HAWAII REVISED STATUTES) | MEASURE AND RATE OF TAX | REPORTS | TAX PAYABLE |
|---|--|--|---|
| (8) Fuel Chapter 243 — Section 243-1 to 243-16 | Distributors, as defined, are required to pay: 1¢ per gallon on aviation fuel; an initial 1¢ per gallon on diesel oil, liquefied petroleum gas for operation of an internal combustion engine and from 24.8¢ to 32.5¢ per gallon on liquid fuels other than the foregoing; also, pay additional taxes from 24.8¢ to 32.5¢ per gallon on diesel oil and from 17¢ to 22¢ per gallon on liquefied petroleum gas used to operate motor vehicles upon the public highways, however, they are not required to pay these additional taxes if purchasers furnish Exemption Certificates, Form M-38. Refunds of liquid fuel used for agricultural equipment not operated upon the public highways or diesel oil and liquefied petroleum gas used for motor vehicles not operated upon the public highways may be claimed on Form M-36. Distributors are required to register and be licensed. Licenses are valid until revoked. An Environmental Response Tax of 5¢ per barrel or a fractional part of a barrel of petroleum product sold by a distributor to a retail dealer or end user is also imposed. | Returns are due monthly on or before the last day of the following month. | At time of filing returns. |
| (9) Liquor Chapter 244D — Section 244D-1 to 244D-17 | This is a gallonage tax imposed upon "dealers" as defined in the law and certain others who sell or use liquor. A \$2.50 liquor tax permit is required and must be renewed before July 1st of each year. See section 244D-4 for exemption from tax. For the period beginning July 1, 1998, and thereafter, the tax rates per wine gallon are \$5.98 on distilled spirits, \$2.12 on sparkling wine, \$1.38 on still wine, \$.85 on cooler beverages, \$.93 on beer other than draft beer, and \$.54 on draft beer. | Returns filed on or before the last day of the following calendar month. | At time of filing returns. |
| (10) Cigarette and Tobacco Chapter 245 — Section 245-1 to 245-15 | "Wholesalers" and "dealers" as defined in the law must pay an excise tax on sale or use of tobacco products equal to 40% of the wholesale price and a fixed tax rate of 5¢ on each cigarette sold, used, or possessed. A \$2.50 tobacco tax license is required and must be renewed before July 1st of each year. | Returns filed on or before the last day of the following calendar month. | At time of filing returns. |
| (11) Conveyance Chapter 247 — Section 247-1 to 247-13 | This tax is imposed on all documents transferring ownership or interest in real property. The rate is 10¢ per \$100 of the actual and full consideration paid or to be paid. Minimum \$1 tax for each taxable transaction. (Documents of certain conveyances are exempted.) | A certificate of conveyance must be filed with the document at the Bureau of Conveyances within 90 days after a taxable transaction; a claim for exemption from the conveyance tax must be filed for certain exempt conveyances. | At time of filing the certificate, but no later than 90 days after the taxable transaction. |
| (12) Rental Motor Vehicle and Tour Vehicle Surcharge Tax Chapter 251 — Section 251-1 to 251-15 | There is a rental motor vehicle surcharge tax of \$2 a day or any portion of a day that a rental motor vehicle is rented or leased. The tax is levied on the lessor. There is also a tour vehicle surcharge tax of \$65 per month for each tour vehicle in the 25 passenger seat and over category and \$15 per month for each tour vehicle in the 8 to 25 passenger seat category. The tax is levied on the tour vehicle operator. There is a one-time \$20 registration fee. | Monthly returns are due on or before the last day of the following month. When the total tax liability does not exceed \$2,000 for the calendar or fiscal year, returns may be filed quarterly on or before the last day of the month after the close of each quarter. When the total tax liability does not exceed \$1,000 for the calendar or fiscal year, returns may be filed semiannually on or before the last day of the month after the close of each semiannual period. An annual summary and reconciliation return must be filed on or before the 20th day of the 4th month following the close of the taxable year. | At time of filing returns. |

| KIND OF TAX & LEGAL REFERENCES (HAWAII REVISED STATUTES) | MEASURE AND RATE OF TAX | REPORTS | TAX PAYABLE |
|---|--|---|--------------------------------------|
| <p>(13) Unemployment Insurance Chapter 383 — Section 383-1 to 383-176</p> | <p>This is a tax on wages paid by employing units with 1 or more employees with certain exemptions. The unemployment tax rate is determined according to a multi-contribution schedule system. Each year, 1 of 8 contribution schedules is applicable depending on the condition of the UI Trust Fund. An employer's contribution rate is not less than 0.00% or greater than 5.40%. There is a .05% employment and training fund assessment on taxable wages paid to all employees by employing units with contribution rates greater than 0.00% but less than 5.40%. Act 194, SLH 1997, temporarily suspended this assessment from July 1, 1997 through December 31, 1998.</p> | <p>Returns filed on or before the last day of the month following the taxable quarter.</p> | <p>At time of filing returns.</p> |
| <p>(14) Insurance Premiums Chapter 431 — Section 431:7-201 to 431:7-207</p> | <p>Tax on insurance companies (Underwriters) based on premiums received in Hawaii. In lieu of all taxes except property tax and taxes on the purchase, use or ownership of tangible personal property. Tax Rates: Life Insurance, 2.75%; Surplus Lines, 4.68%; Ocean Marine, .8775% on gross underwriting profit; and Other Insurance, 4.265%. To insurers who qualify, there is a 1% tax credit to facilitate regulatory oversight. This law is administered and the tax collected by the Insurance Commissioner, who is required to report to the Director of Taxation all amounts of taxes collected under this chapter.</p> | <p>Monthly/Quarterly interim statement is due on or before the last day of the calendar month following the month/quarter in which the tax accrued. Annual Tax Statement is due on or before March 1 with the Insurance Commissioner. Effective January 1, 1999: Quarterly interim statement is due on or before the last day of the calendar month following the quarter in which the tax accrued. Annual Tax Statement is due on or before March 1 with the Insurance Commissioner.</p> | <p>At time of filing statements.</p> |
| | | | |

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