

DEPARTMENT OF TAXATION

ANNUAL REPORT REQUIRED BY ACT 134, SLH 2009, SECTION 9
For the period July 1, 2011 through June 30, 2012

January 16, 2013

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 (SES), 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 SES operations to assist in the funding of the unit. The SES 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 fiscal year 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.

ACTIVITIES AND ACCOMPLISHMENTS

Since passage of the Cash Economy Enforcement Act, the Department has worked diligently in implementing the 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 other competing priorities in the Compliance Division in the Department and the current economy. The emphasis for this fiscal year was on educating the public about the laws as enforced by the Special Enforcement Section. Current 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 industry groups and to various groups that requested meetings;
- Continuing to field complaints and information from the public to determine if there is a valid tax issue for investigation or further review by the Department;
- Conducting site visits where Special Enforcement Section Agents were identifiable. Site visits were conducted at farmers' markets, craft fairs, shopping malls, industrial parks, restaurants and other locations across the state and included issuing acknowledgment forms to vendors to inform them of potential violations of Hawaii and Special Enforcement Section tax laws;
- Through tracking of non-compliant taxpayers at time of the site visit the unit has found that there has been an increase in voluntary compliance;
- 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;
- Working with non-compliant taxpayers under investigation to voluntarily file the requested tax returns. This is vital for the continued filing of the returns by the taxpayers. It has been shown that the voluntary filers continue after the conclusion of the investigation;
- In addition, the SES is currently developing scripts to begin production of Public Service Announcements about the General Excise Tax laws to increase tax education to the public.

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

In Fiscal Year 2012, only three investigators remained in the unit. The three investigators were overseen by Stephen Hironaka, Supervising Criminal Tax Investigator, until December 2011. From December 2011 through May 2012 the unit was supervised by Dan Umemoto, Criminal Tax Investigator, and in June one of the Special Agents began to supervise the unit with oversight from Director, Frederick Pablo.

For Fiscal Year 2012, SES expenditures were as follows:

Category	Fiscal Year 2012
Personnel	\$202,852.89
Other Expenses	\$47,890.60
Total	\$250,743.49

As of November 27, 2012, Fiscal Year 2013 SES expenditures were \$84,520.96 consisting of \$67,646.52 personnel and \$16,874.44 other current expenses.

As SES continues to develop and increase its productivity it has focused on increasing voluntary compliance of taxpayers. One way the SES is trying to accomplish this is by contacting taxpayers who are currently out of compliance and requesting the filing of the any missing tax returns.

SES is also expanding its focus of cash-based businesses to other areas of cash-based businesses that may not be compliant with all tax laws. The main focus of the SES unit site visits have been to craft and art fairs, swap meets, and farmers market in the past. SES is expanding this to include several different areas of cash-based businesses including, but not limited to, car dealers, massage parlors, nail salons, and several other areas of cash business. There is also an increased focus on neighbor island cash-based activity. Once the unit is fully staffed it will allow the unit to expand its focus areas into all cash-based business areas.

II. ADDITIONAL REVENUES RAISED BY THE CASH ECONOMY ENFORCEMENT ACT

In Fiscal Year 2012, the SES generated \$903,559 in revenues.

Since July 1, 2011 through June 30, 2012, SES reports the following statistics:

Complaints filed by anonymous persons:	147
Vendors educated as to how to comply with tax law:	1,608
Site visitations throughout the State of Hawaii:	27
Number of Investigations completed:	32
Number of Investigations sent to Audit:	12
Total Dollars Assessed	\$105,990
Total Dollars Secured Returns	\$1,254,409
Revenue Collected:	\$903,559