

**ANNUAL
REPORT
2018-2019**



**DEPARTMENT OF TAXATION
STATE OF HAWAII**

DAVID Y. IGE
GOVERNOR

JOSH GREEN M.D.
LT. GOVERNOR



RONA M. SUZUKI
DIRECTOR OF TAXATION

DAMIEN A. ELEFANTE
DEPUTY DIRECTOR

STATE OF HAWAII
DEPARTMENT OF TAXATION
P.O. BOX 259
HONOLULU, HAWAII 96809
PHONE NO: (808) 587-1540
FAX NO: (808) 587-1560

December 26, 2019

The Honorable David Y. Ige
Governor, State of Hawaii
Executive Chambers, State Capitol

Dear Governor Ige:

The Department of Taxation (DOTAX) is pleased to present this annual report of the activities undertaken in Fiscal Year (FY) 2019. We have also included more recent information about activities in the first half of FY 2020. The report also includes our goals and objectives for Calendar Year 2020, as required by Act 100, Session Laws of Hawaii 1999.

In FY 2019, total State tax collections were \$8.28 billion, a 4.8% increase from FY 2018 which were \$7.9 billion. **DOTAX collected \$7.87 billion in tax revenue in FY 2019, or 95% of all taxes administered by the State.** General Excise Tax (GET) is Hawaii's largest source of revenue, accounting for 43% of the State's total tax collections. Revenue from the GET rose to \$3.54 billion in FY 2019 from \$3.40 billion in FY 2018, an increase of 4.1%. Revenue from Hawaii's Individual Income Tax (IIT), Hawaii's second largest tax, increased 17.3% to \$2.57 billion in FY 2019 from \$2.19 billion in FY 2018, accounting for 31% of the State's total tax collections.

Operational Highlights

September 2019 marked an important milestone for DOTAX: the **completion of the fifth and final functional phase of work for the Tax System Modernization (TSM) project**. Since the project contract was initiated in July 2015, DOTAX staff have worked to design, test, and deploy the technical configurations and learn the new technologies, while maintaining operations and utilizing multiple systems to do work. With the completion of Rollout Five, we now have all of our tax data in a single computer system and can focus on utilizing this system. This project has impacted every aspect of the DOTAX. I hope you will join me in commending the DOTAX staff for this outstanding accomplishment.

The TSM project introduced taxpayers **Hawaii Tax Online (HTO)**, replacing ELF. Taxpayers are utilizing HTO to securely file returns, make payments, and communicate with DOTAX staff. The implementation of mandatory e-filing requirements will further drive use of this technology.

Table 1. HTO Activity	FY19	FY18	Change
All Tax Accounts	4,307,459	4,240,905	66,554
Active Taxpayer Accounts ¹	1,116,317	280,550	835,767
HTO Accounts	194,633	142,348	52,285
HTO Returns Processed	964,216	816,068	148,148
HTO Payments Received	872,749	679,702	193,047

¹ Taxpayer filed/paid in the last 500 days.

The transition to electronic returns over paper returns continues. DOTAX processed **5.1 million tax returns** in FY 2019. As shown in Figure 1, more than half of the returns processed were electronically filed.

Our **first individual income tax filing season** using our new computer systems was completed in October 2019. The number of electronic filed returns is slowly increasing:

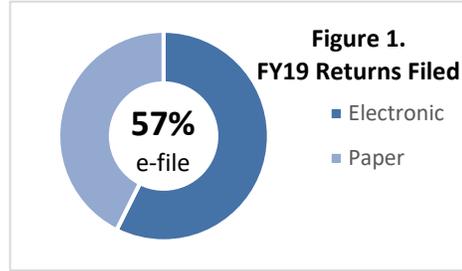


Table 2. Individual Income Tax Filing	FY19	FY18	Change
Resident (Form N-11) Returns Filed	648,716	646,863	1,853
Electronic (HTO, MeF)	499,287	480,024	19,263
Paper	149,429	166,839	(17,590)
Non-Resident (Form N-15) Returns Filed	100,687	101,390	(703)

Additional metrics are provided in Table 3 and described in the report. Our plans for Calendar Year 2020 are presented in Appendix A.

We are proud and appreciative of all that our staff has accomplished during the past year as DOTAX continues to pursue its goals of increased voluntary compliance, improved processing, enhanced productivity, and improved customer service for all our taxpayers. Empowered with new tools and technological enhancements, DOTAX will continue to increase the efficiency and effectiveness of revenue collections to pay for the critical public services for the people of Hawaii.

Thank you for your continued commitment to Team DOTAX!

Very truly yours,

RONAM M. SUZUKI
Director of Taxation

Table 3. DOTAX by the Numbers

	FY19	FY18	Change
Total Taxes Collected (\$)	\$8.28 billion	\$7.90 billion	\$0.38 billion
DOTAX	\$7.87 billion (95% of total taxes)	\$7.49 billion (95% of total taxes)	\$0.38 billion
Other Departments	\$0.41 billion	\$0.41 billion	\$0.0 billion
DOTAX Taxes Collected (\$)²			
General Excise	\$3.54 billion	\$3.40 billion	\$0.14 billion
Individual Income	\$2.57 billion	\$2.19 billion	\$0.35 billion
Other	\$1.76 billion	\$1.69 billion	\$0.07 billion
Active Taxpayers Accounts	1,116,317	280,550	835,767
Returns Processed (#)	5.1 million	5.3 million	(0.2 million)
Paper	2,173,814 (43%)	2,592,896 (49%)	(419,082)
Electronic	2,927,117 (57%)	2,701,208 (51%)	225,909
Transactions Processed			
Payments	2,974,047	2,152,435*	821,612
Refunds	580,744	58,370*	522,374
Taxpayers Served (#)			
Phone	127,092	116,697	10,395
Walk-in (including cashier)	43,572	50,316	(6,744)
Correspondence	70,451	35,187	35,264
Tax Clearances Processed (#)	47,389	53,188	(5,799)
Audit			
Audits Issued (#)	24,490	17,515	6,975
Assessments (\$)	\$132.6 million	\$114.5 million	\$18.0 million
Recoveries (\$, %)	\$33.2 million (25%)	\$28.2 million (25%)	\$5.0 million
Collections			
Starting Delinquent Balance (\$)	\$971.4 million	\$846.3 million	\$125.1 million
New Debts (\$)	\$270.1 million	\$284.4 million	(\$14.3 million)
Recoveries (\$)	\$191.3 million	\$222.0 million	(\$30.7 million)
Uncollectible (\$)	\$21.8 million	\$0.2 million	\$21.6 million
Ending Delinquent Balance (\$)	\$1,037.6 million	\$971.4 million	\$66.2 million
Cases (#)	63,992	59,381	4,611
Operating Costs	\$25.8 million (\$0.33 per \$100 tax collected)	\$23.7 million (\$0.32 per \$100 tax collected)	\$2.1 million
Total FTE Authorized (ACT 153, SLH 2018)	541	530	11

*Does not include ITPS

² Source: Statement of Tax Operations. Includes tax, fees, penalties, interest.

TABLE OF CONTENTS

LETTER OF TRANSMITTAL TO THE GOVERNOR

1.0 COLLECTION AND DISTRIBUTION OF TAXES 1

- 1.1 OVERVIEW..... 1
- 1.2 GENERAL EXCISE AND USE TAXES..... 3
- 1.3 INDIVIDUAL INCOME TAX 6
- 1.4 CORPORATE INCOME TAX..... 8
- 1.5 TRANSIENT ACCOMMODATIONS TAX 10
- 1.6 FUEL TAXES 14
- 1.7 MOTOR VEHICLE TAXES AND FEES 21
- 1.8 CIGARETTE AND TOBACCO TAX 22
- 1.9 PUBLIC SERVICE COMPANY TAX 25
- 1.10 UNEMPLOYMENT INSURANCE TAX 26
- 1.11 INSURANCE PREMIUM TAX..... 27
- 1.12 LIQUOR TAX 28
- 1.13 CONVEYANCE TAX..... 29
- 1.14 TAX ON BANKS AND OTHER FINANCIAL CORPORATIONS 31
- 1.15 ESTATE AND TRANSFER TAX 32
- 1.16 COUNTY SURCHARGE TAX 33
- 1.17 TOTAL TAX COLLECTIONS 35
- 1.18 DISTRIBUTION OF TAXES..... 36
- 1.19 TRENDS IN TAX COLLECTIONS..... 39

2.0 TAX ADMINISTRATION..... 41

- 2.1 OVERALL PERFORMANCE..... 41
- 2.2 TAX SERVICES AND PROCESSING DIVISION 41
- 2.3 COMPLIANCE DIVISION 45
- 2.4 STAFF OFFICES..... 56
- 2.5 MANAGEMENT PERSONNEL 63
- 2.6 ORGANIZATION CHART 64
- 2.7 DISTRICT OFFICES..... 65

3.0 APPEALS AND LITIGATION 67

- 3.1 ADMINISTRATIVE APPEALS OFFICE..... 67
- 3.2 BOARDS OF TAXATION REVIEW 67
- 3.3 CIVIL DECISIONS, SETTLEMENTS AND OTHER LEGAL MATTERS 68

4.0 ADMINISTRATIVELY ATTACHED ENTITIES 80

- COUNCIL ON REVENUES 80
- BOARDS OF TAXATION REVIEW 80

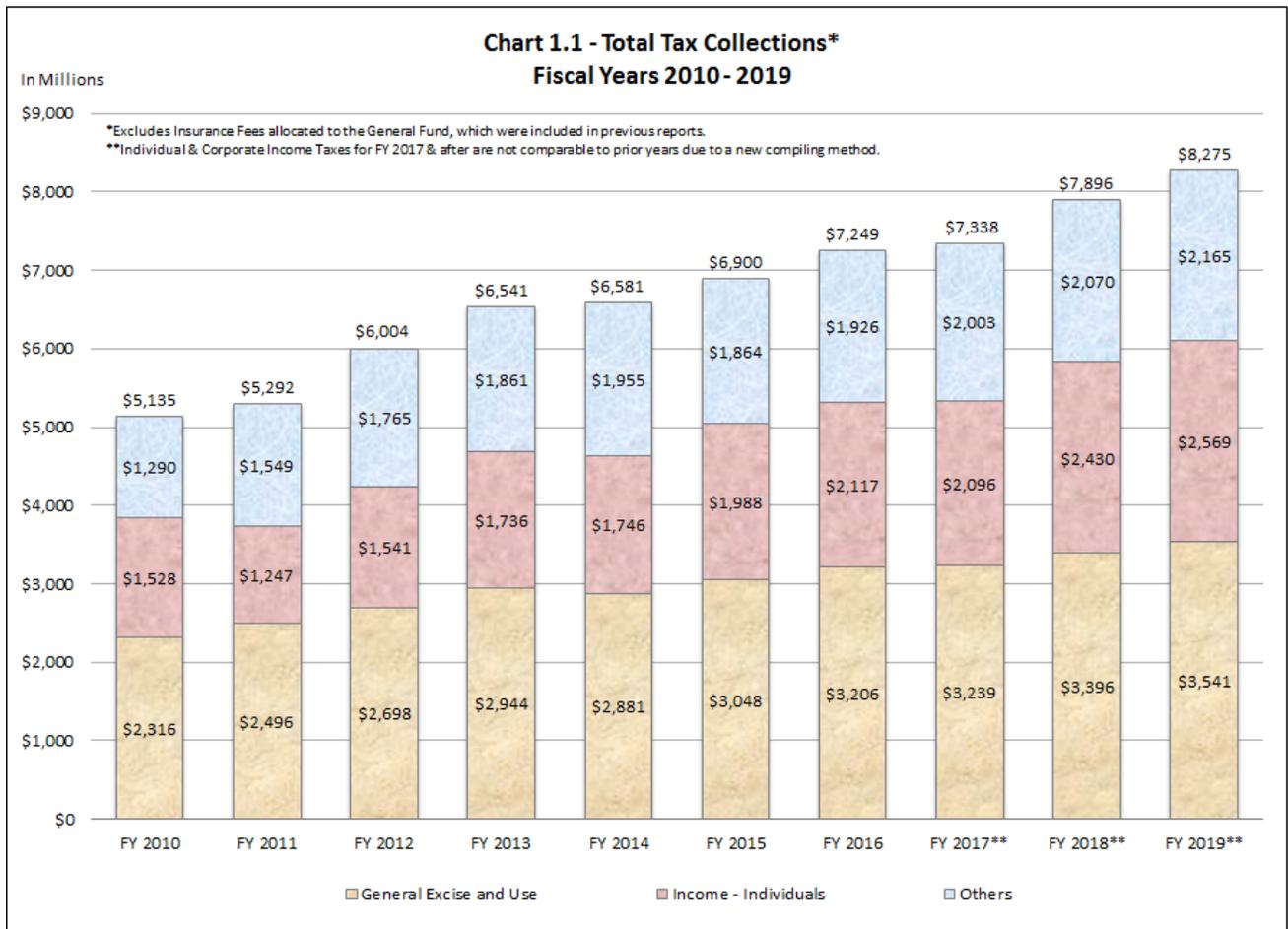
1.0 COLLECTION AND DISTRIBUTION OF TAXES

1.1 OVERVIEW

The Department of Taxation (DOTAX) collects revenues from majority of taxes imposed by the State. In addition, DOTAX collects fuel taxes imposed by the counties, and the county surcharges. In fiscal year (FY) 2019, DOTAX collected a total of \$7.87 billion in net tax revenues, up from \$7.49 billion collected in FY 2018.

Total tax collections, including revenues from taxes collected by DOTAX as well as other State agencies or counties, were \$8.28 billion in FY 2019, up from \$7.90 billion in FY 2018. Total tax collections have risen steadily since the Great Recession in FY 2009 due to new tax measures, an improving economy, and better tax administration.

Chart 1.1 shows the main components of the total tax collections for FY 2010 through FY 2019.

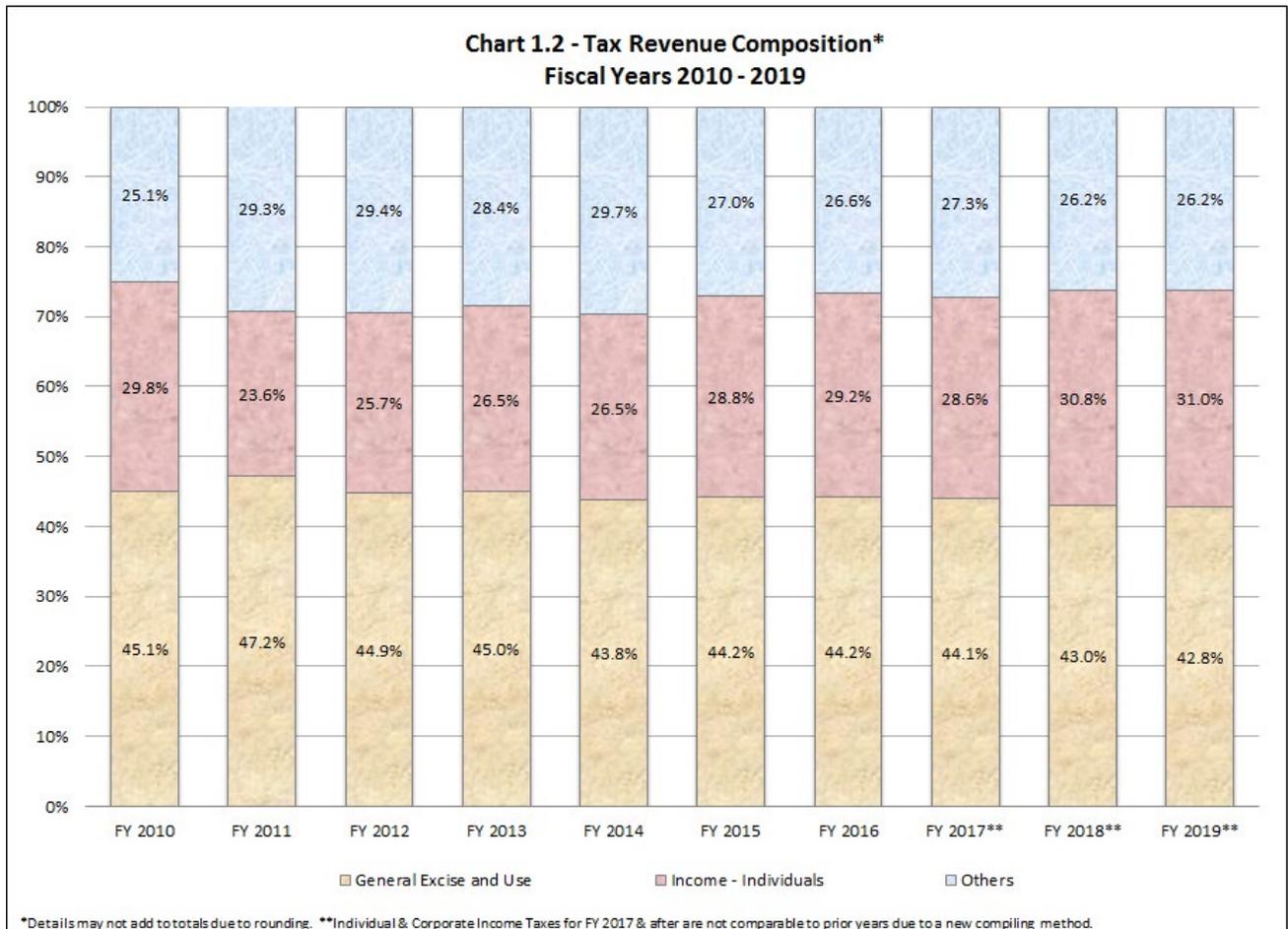


The State's biggest sources of tax revenue are the general excise tax (GET)³ and the individual income tax (IIT). In FY 2019, net GET collections amounted to \$3.54 billion and accounted for

³ Throughout this report, the term "GET" will be used to include collections from both the general excise tax and the use tax. The use tax complements the general excise tax and is levied on imports into the State from an unlicensed seller.

42.8% of total tax collections, and net collections of the IIT amounted to \$2.57 billion and accounted for 31.0% of total tax collections.

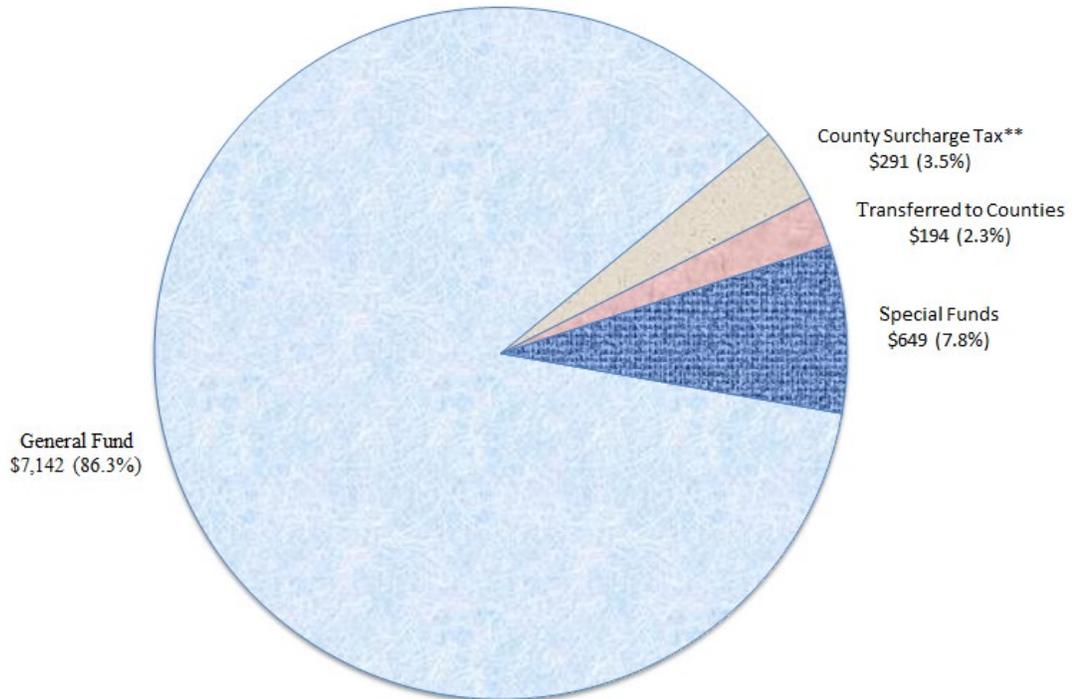
Chart 1.2 shows the shares of total tax collections accounted for by the GET and the IIT for FY 2010 through FY 2019.



Of the total tax collections in FY 2019, \$7.14 billion, or 86.3%, was deposited into the State's General Fund and was used to pay most of the State's operating expenses. An additional \$484.4 million, or 5.9% of the total tax collections, was transferred to the counties. Collections transferred to the counties included transfers of county surcharges, which was \$291 million, or 3.5%, and the fuel taxes and revenues from the transient accommodations tax. The remaining \$648.9 million, or 7.8%, was transferred to various other State special funds.

Chart 1.3 shows how the total tax collections were distributed in FY 2019.

Chart 1.3 - Fiscal Year 2019 Distribution of Tax Revenues*
(In millions of dollars)



*Details may not add to totals due to rounding.
**Includes the new surcharges imposed by the County of Hawaii and by the County of Kauai, starting in January 2019.

1.2 GENERAL EXCISE AND USE TAXES

1.2.1 Overview

Unlike sales tax, Hawaii's GET is imposed on the business rather than on the customer, covering virtually all forms of business activity. The fee for a GET license is a one-time charge of \$20.

Business Activity	Tax Rate
Wholesaling, wholesale services, producing, manufacturing	0.50%
Insurance commissions	0.15%
Other*	4.00%

1.2.2 Revenue

Despite the relatively low tax rates, the GET generates substantial revenue because the tax base is very broad. Revenue from the GET rose from \$3.40 billion in FY 2018 to \$3.54 billion in FY 2019, a rise of 4.3%.

Chart 1.4 shows the total revenues from the GET and from the tax levied on the various categories of income for FY 2010 through FY 2019. Table 1.1 shows collection of the GET in greater detail for

FY 2018 and FY 2019.

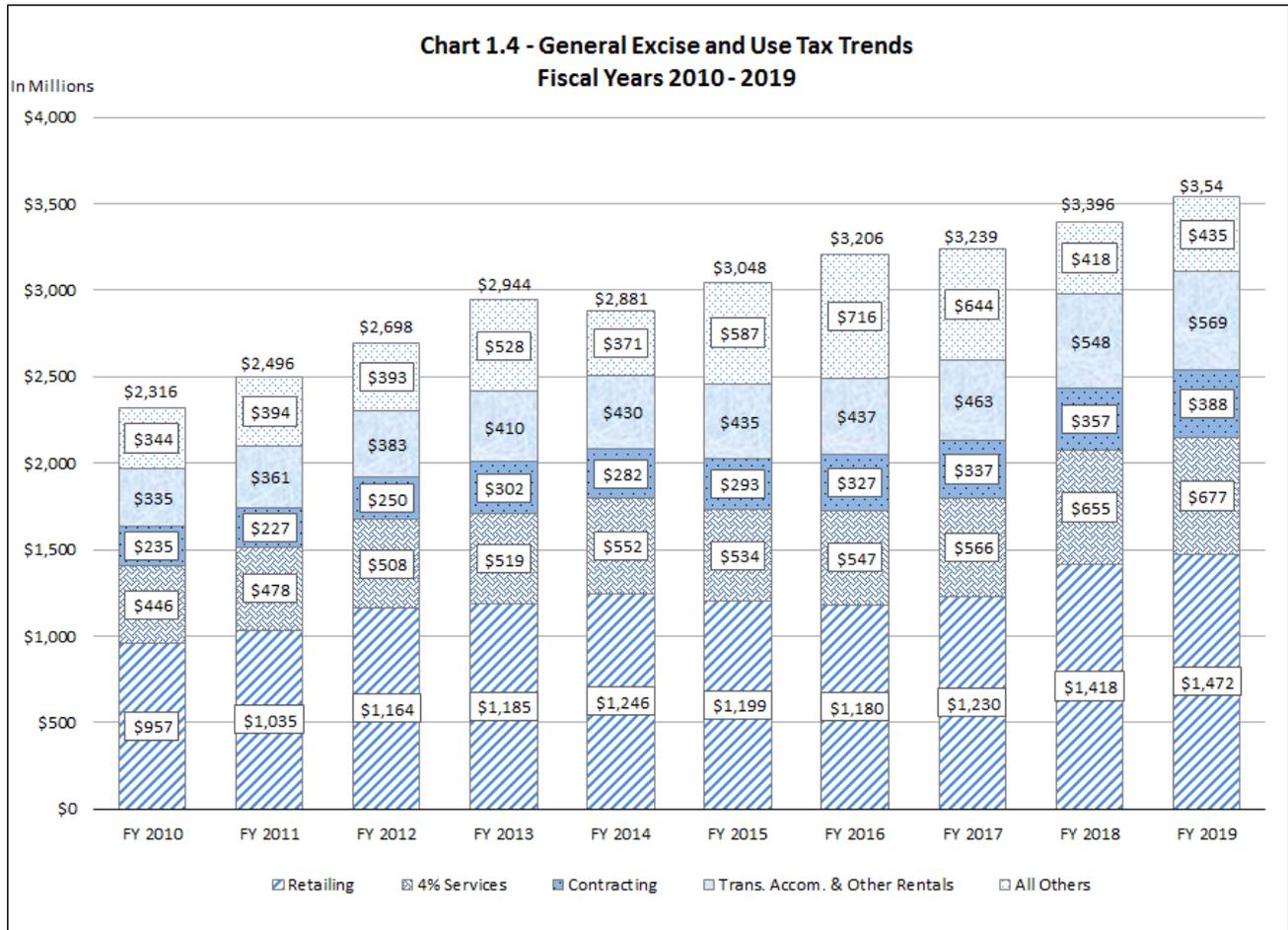


TABLE 1.1 - GENERAL EXCISE AND USE TAX BASE AND TAXES
FOR FISCAL YEARS ENDING JUNE 30, 2019 AND 2018
(In Thousands of Dollars)

SOURCE OF REVENUE	Rate	FY 2019	FY 2018	Difference	
				Amount	% Change
<u>TAX BASE</u>					
Retailing		\$ 36,800,989	\$ 35,454,397	\$ 1,346,591	3.8
Services		16,927,042	16,375,168	551,875	3.4
Contracting		9,706,222	8,914,402	791,821	8.9
Trans. Accom. Rentals		5,669,106	5,527,107	141,998	2.6
All Other Rentals		8,564,302	8,170,571	393,731	4.8
All Others (4%)		<u>6,542,739</u>	<u>6,544,068</u>	<u>(1,329)</u>	<u>(0.0)</u>
Subtotal		\$ 84,210,401	\$ 80,985,714	\$ 3,224,687	4.0
Producing		\$ 295,937	\$ 358,827	\$ (62,889)	(17.5)
Manufacturing		596,190	640,143	(43,952)	(6.9)
Wholesaling		18,061,507	17,590,486	471,022	2.7
Use (1/2%)		7,279,558	7,640,150	(360,593)	(4.7)
Services (Intermediary)		1,005,178	902,755	102,422	11.3
Insurance Solicitors		<u>753,946</u>	<u>650,223</u>	<u>103,723</u>	<u>16.0</u>
Subtotal		\$ 27,992,317	\$ 27,782,584	\$ 209,732	0.8
TOTAL - ALL ACTIVITIES		<u>\$112,202,717</u>	<u>\$108,768,298</u>	<u>\$ 3,434,420</u>	<u>3.2</u>
<u>TAX</u>					
Retailing	4.00%	\$ 1,472,040	\$ 1,418,176	\$ 53,864	3.8
Services	4.00%	677,082	655,007	22,075	3.4
Contracting	4.00%	388,249	356,576	31,673	8.9
Trans. Accom. Rentals	4.00%	226,764	221,084	5,680	2.6
All Other Rentals	4.00%	342,572	326,823	15,749	4.8
All Others (4%)	4.00%	<u>261,710</u>	<u>261,763</u>	<u>(53)</u>	<u>(0.0)</u>
Subtotal		\$ 3,368,416	\$ 3,239,429	\$ 128,987	4.0
Producing	0.50%	\$ 1,480	\$ 1,794	\$ (314)	(17.5)
Manufacturing	0.50%	2,981	3,201	(220)	(6.9)
Wholesaling	0.50%	90,308	87,952	2,355	2.7
Use (1/2%)	0.50%	36,398	38,201	(1,803)	(4.7)
Services (Intermediary)	0.50%	5,026	4,514	512	11.3
Insurance Solicitors	0.15%	<u>1,131</u>	<u>975</u>	<u>156</u>	<u>16.0</u>
Subtotal		\$ 137,323	\$ 136,637	\$ 686	0.5
Unallocated*		<u>\$ 35,650</u>	<u>\$ 19,500</u>	<u>\$ 16,150</u>	<u>82.8</u>
TOTAL - ALL ACTIVITIES		<u>\$ 3,541,389</u>	<u>\$ 3,395,566</u>	<u>\$ 145,823</u>	<u>4.3</u>

*Includes collections from penalty and interest, assessments and corrections, delinquent collections, refunds, protested payments, settlements and business activities of disabled persons.

NOTE: Details may not add to totals due to rounding.

1.2.3 Recent Legislation

Act 39, SLH 2018, increases the aggregate amount of the GET exemption for developing affordable rental housing from \$7 million to \$30 million per year. The Act also extends the exemption from June 30, 2022, to June 30, 2030. The Act is effective July 1, 2018, and applies retroactively to taxable years beginning after December 31, 2017.

Act 41, SLH 2018, provides that a person is engaging in business in the State for the purpose of the general excise tax law if, in the current or immediately preceding calendar year, the person has \$100,000 or more in gross income, or two hundred or more separate transactions, from the sale of tangible personal property delivered in the State, services used or consumed in the State, or intangible property used in the State. The Act is effective July 1, 2018, and applies to taxable years beginning after December 31, 2017.

Act 183, SLH 2018, creates a GET exemption for intangible property used outside the State. The Act also imposes a 4% use tax on intangible property imported into the State. The Act is effective July 10, 2018 and applies to taxable years beginning after December 31, 2018.

Act 2, SLH 2019, defines "marketplace facilitator" to be any person who sells or assists in the sale of tangible personal property, intangible personal property, or services on behalf of another by providing a forum for the listing or advertisement of the item and by collecting payment from the purchaser either directly or indirectly. The Act deems marketplace facilitators to be the sellers of tangible personal property, intangible personal property, and services sold through the marketplace. The Act also deems sales of tangible personal property and of services by sellers to a marketplace facilitator to be sales at wholesale. The Act takes effect January 1, 2020.

1.3 INDIVIDUAL INCOME TAX

1.3.1 Overview

Hawaii's individual income tax (IIT) generally follows the federal definitions for determining net taxable income, but has its own exemptions, tax credits, and tax rates. For taxable years beginning after December 31, 2017, the IIT has twelve tax brackets, with rates ranging from 1.40% to 11.00%.

1.3.2 Revenue

The IIT is the State's second largest source of tax revenue. The biggest part of IIT collections is taxes withheld on employee wages. In FY 2019, withholding tax collections were \$2.10 billion, an increase of 3.4% over the \$2.03 billion withheld in FY 2018. Total IIT refunds in FY 2019 were \$520.3 million, down from \$522.5 million in FY 2018. Net IIT collections in FY 2019 were \$2.57 billion, up by 5.7% over the \$2.43 billion collected in FY 2018.

Chart 1.5 shows total collections of the IIT, along with wage withholding, payments with returns, estimated taxes, and refunds, for FY 2010 through FY 2019. Table 1.2 shows the figures for total collections of the IIT, broken down by its components, in FY 2018 and FY 2019.

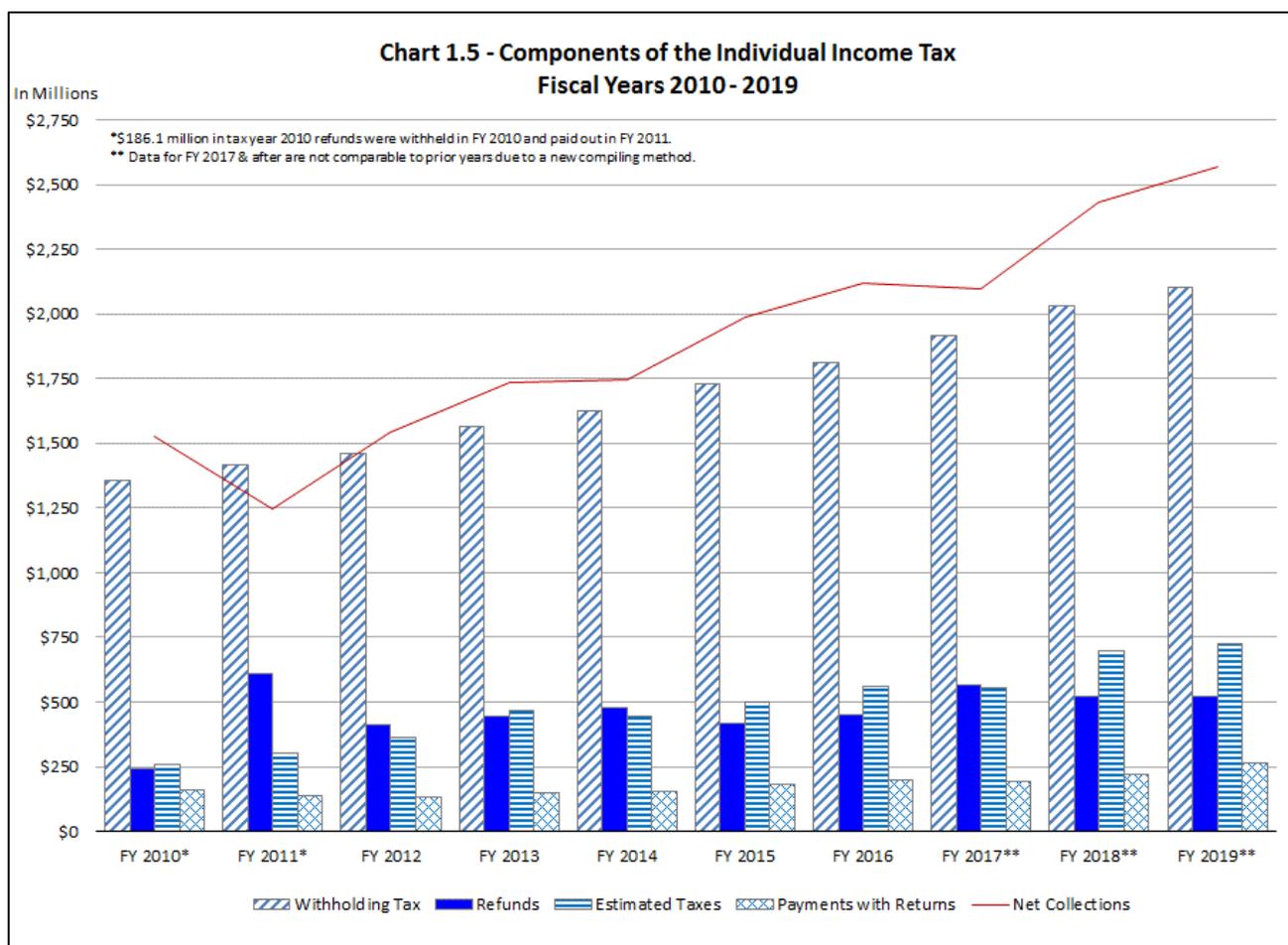


TABLE 1.2 - TAXES PAID BY INDIVIDUALS*
(In Thousands of Dollars)

	FY 2019	FY 2018	Difference	
			Amount	% Change
Declaration of Estimated Taxes	\$ 724,325	\$ 700,017	\$ 24,308	3.5
Payment with Return	262,322	219,989	42,333	19.2
Withholding Tax on Wages	2,102,253	2,032,879	69,374	3.4
Subtotal	\$3,088,900	\$2,952,885	\$136,016	4.6
Refunds	520,284	522,528	(2,244)	(0.4)
NET	\$2,568,616	\$2,430,356	\$138,260	5.7

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

*Data for FY 2017 & after are not comparable to prior years due to a new compiling method.

1.3.3 Recent Legislation

Act 43, SLH 2018, establishes a new tax credit for healthcare preceptors (physicians, advanced

practice registered nurses, and pharmacists). The amount of credit per taxpayer is limited to \$5,000 per year. The tax credit is subject to an aggregate cap of \$1.5 million per year and applies to taxable years beginning after December 31, 2018.

Act 122, SLH 2018, increases the withholding on the amount realized from the disposition of Hawaii real property by nonresidents (HARPTA) from 5% to 7.25%. The Act is effective July 5, 2018, and applies to real estate dispositions that occur on or after September 15, 2018.

Act 170, SLH 2018, amends the income tax check-off for the libraries special fund. The Act increases the amount of a state income tax refund that the taxpayer may donate to the fund, from \$2 to \$5 for a single return and from \$4 to \$10 for a joint return. The Act is effective July 1, 2018, and applies to taxable years beginning after December 31, 2017.

Act 69, SLH 2019, selectively conforms Hawaii income tax and estate tax laws to the Internal Revenue Code (IRC) as of December 31, 2018. For Hawaii's income tax, the Act is effective June 7, 2019, and applies to taxable years beginning after December 31, 2018.

Act 221, SLH 2019, establishes an economic nexus standard for Hawaii's income taxes. The Act states that a person without physical presence is engaging in business in the State if the person has \$100,000 or more in income sourced to the state or has 200 or more transactions sourced to the state. The new nexus standard is similar to the economic nexus standard for the general excise tax established by Act 41, SLH 2018. The Act is effective July 2, 2019 and applies to taxable years beginning after December 31, 2019.

Act 267, SLH 2019, establishes a new, nonrefundable income tax credit for taxpayers who rehabilitate historic structures pursuant to a rehabilitation plan certified by the Department of Land and Natural Resources' State Historic Preservation Division. The credit is equal to 30% of the qualified expenses incurred as part of the certified rehabilitation plan. In addition, the credit is subject to an aggregate cap of \$1 million per year. The Act is effective July 1, 2019, applies to qualified rehabilitation expenditures incurred in taxable years beginning after December 31, 2019, and is repealed on December 31, 2024.

Act 232, SLH 2019, requires income tax withholding for nonresident taxpayers based on the taxpayers' distributive share of income attributable to the State as shown on the partnership's, estate's, and trust's return for the taxable period. The amount withheld is equal to the highest marginal tax rate applicable to a nonresident taxpayer multiplied by the amount of the taxpayer's distributive share of income attributable to the State. Withholding is not required for a publicly traded partnership, as defined by section 7704(b) of the IRC. A publicly traded partnership is required to file an annual information return of each unit holder with income sourced to Hawaii. The Act is effective July 2, 2019 and applies to taxable years beginning after December 31, 2018.

1.4 CORPORATE INCOME TAX

1.4.1 Overview

Hawaii's corporate income tax (CIT) has three tax brackets. The brackets and the corresponding tax rates are as follows: 4.4% on taxable income up to \$25,000; 5.4% on taxable income over \$25,000 but not over \$100,000; and 6.4% on taxable income over \$100,000. The tax rate for corporate capital gains is 4.0%.

1.4.2 Revenue

CIT collections are highly cyclical, but they are a relatively small part of Hawaii's total tax collections. Net CIT collections totaled \$163.7 million in FY 2019, an increase of 24.8% from the previous year's total of \$131.1 million. In FY 2019, the CIT accounted for just 2.0% of total tax collections.

Chart 1.6 shows total collections of the CIT, broken down by its components, for FY 2010 through FY 2019. Table 1.3 shows data on collections of the CIT for FY 2018 and FY 2019.

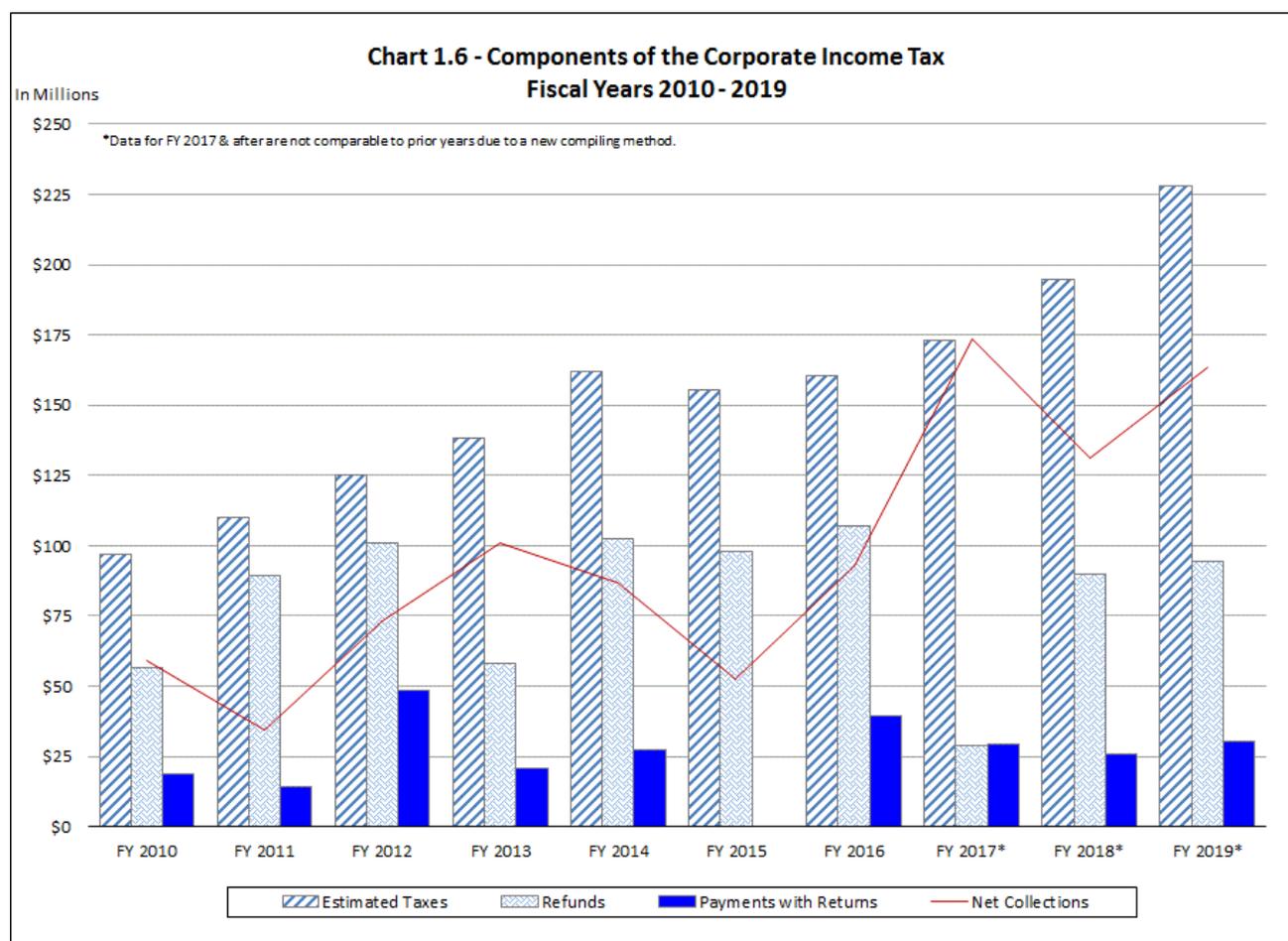


TABLE 1.3 - TAXES PAID BY CORPORATIONS*
(In Thousands of Dollars)

	FY 2019	FY 2018	Difference	
			Amount	% Change
Declaration of Estimated Taxes	\$ 227,904	\$ 194,966	\$ 32,938	16.9
Payment with Return	30,091	25,812	4,279	16.6
Subtotal	\$ 257,995	\$ 220,778	\$ 37,217	16.9
Refunds	94,319	89,660	4,660	5.2
NET	\$ 163,676	\$ 131,119	\$ 32,557	24.8

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

*Data for FY 2017 & after are not comparable to prior years due to a new compiling method.

1.4.3 Recent Legislation

Act 143, SLH 2017, amends the film tax credit by imposing an aggregate cap of \$35 million per year, provided that any excess in claims above the cap can be applied in a subsequent year until December 31, 2025. The Act also extends the sunset date for the tax credit from January 1, 2019 to January 1, 2026. The Act is effective for taxable years beginning after December 31, 2018.

Act 96, SLH 2019, changes the sales factor sourcing rules for sales of services and intangibles. Sales of tangible personal property are already sourced using market sourcing. In general, market sourcing means sales are sourced according to where the taxpayer's sales are located. Previously, sales of services and intangibles were sourced according to where the business activity was located. The Act takes effect June 7, 2019 and applies to taxable years beginning after December 31, 2019.

Act 260, SLH 2019, establishes a new Ship Repair Industry Tax Credit which is intended to offset costs incurred in constructing and placing into service a purpose-built floating drydock at Pearl Harbor for use by the United States Navy, provided that no credit is allowed after December 31, 2026. This Act also repeals the Capital Infrastructure Tax Credit under section 235-17.5, Hawaii Revised Statutes (HRS). The Act is effective on January 1, 2020 and applies to taxable years beginning after December 31, 2021.

Act 261, SLH 2019, amends the Tax Credit for Research Activities (TCRA) such that references to the base amount contained in section 41 of the IRC do not apply, and credit may be taken based upon all qualified research expenses incurred in Hawaii without regard to the amount of expenses for previous years. The Act provides that the Department of Business, Economic Development, and Tourism must certify all claims for the tax credit and establishes an annual aggregate cap of \$5 million. Taxpayers must still claim the federal research credit under IRC section 41 to claim the TCRA. Act 261 extends the TCRA through December 31, 2024. The Act is effective for taxable years beginning after December 31, 2019.

Act 275, SLH 2019, amends the motion picture, digital media, and film production income tax

credit (film credit) by increasing the film credit annual aggregate cap from \$35 million to \$50 million. The Act is effective July 10, 2019 and applies to taxable years beginning after December 31, 2018.

1.5 TRANSIENT ACCOMMODATIONS TAX

1.5.1 Overview

The transient accommodations tax (TAT) is 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. Starting January 1, 2018 through December 31, 2030, the TAT rate is increased from 9.25% to 10.25%. 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 each registration of 6 or more units.

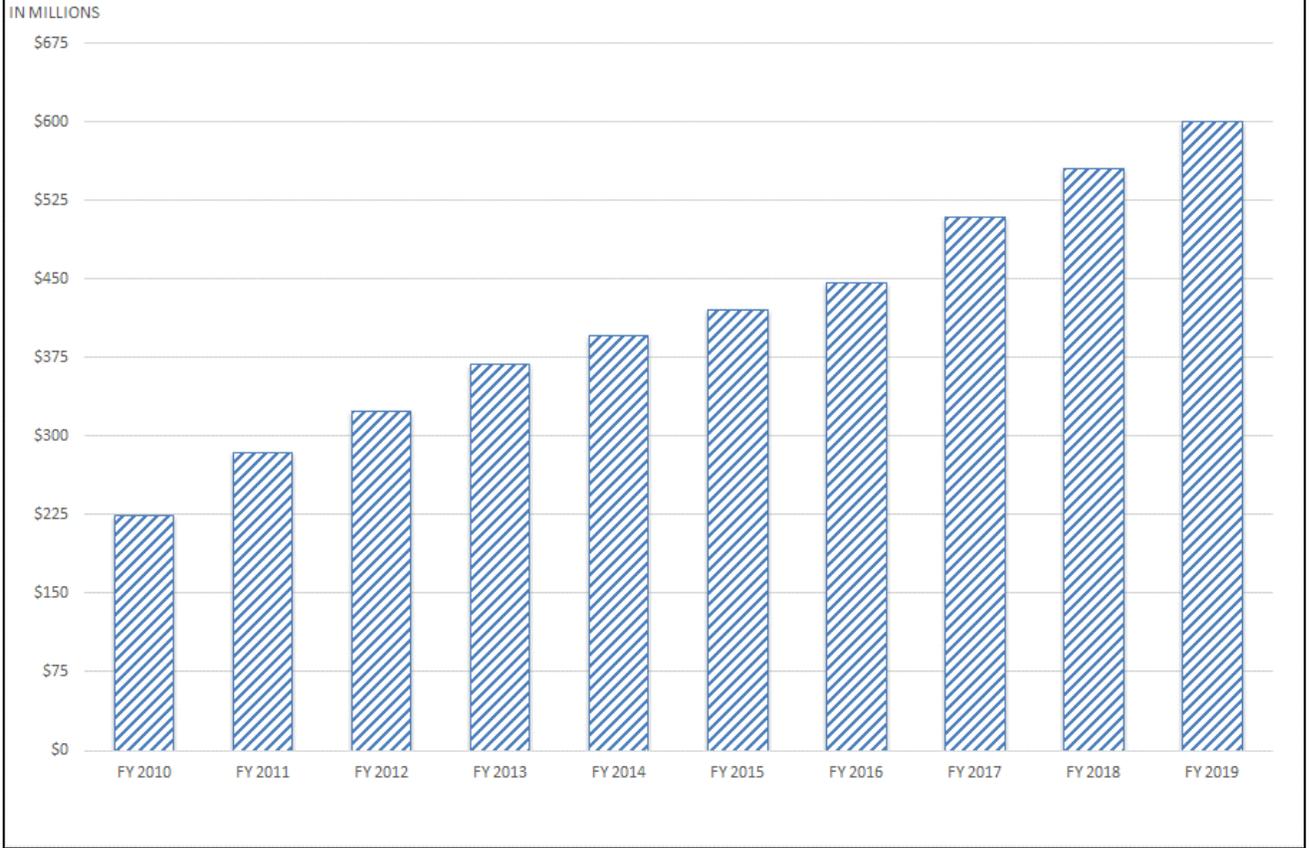
1.5.2 Revenue

TAT collections totaled \$600.3 million for FY 2019, an increase of 8.2% from the \$554.9 million collected in FY 2018.

FY2019 TAT Distribution	
Counties	\$103.0 Million
Convention Center Enterprise Special Fund	\$16.5 Million
Tourism Special Fund	\$79.0 Million
Turtle Bay Conservation Easement Special Fund	\$1.5 Million
Special Land and Development Fund	\$3.0 Million
Mass Transit Fund	\$57.4 Million
General Fund	\$340 Million

Chart 1.7 shows collections of the TAT for FY 2010 through FY 2019. Chart 1.8 shows the allocations of the tax among the various funds. Table 1.4 shows TAT collections and allocations in FY 2018 and FY 2019.

Chart 1.7 - Transient Accommodations Tax
Fiscal Years 2010 - 2019



**Chart 1.8 - Transient Accommodations Tax Distributions
Fiscal Years 2010 - 2019**

In Millions

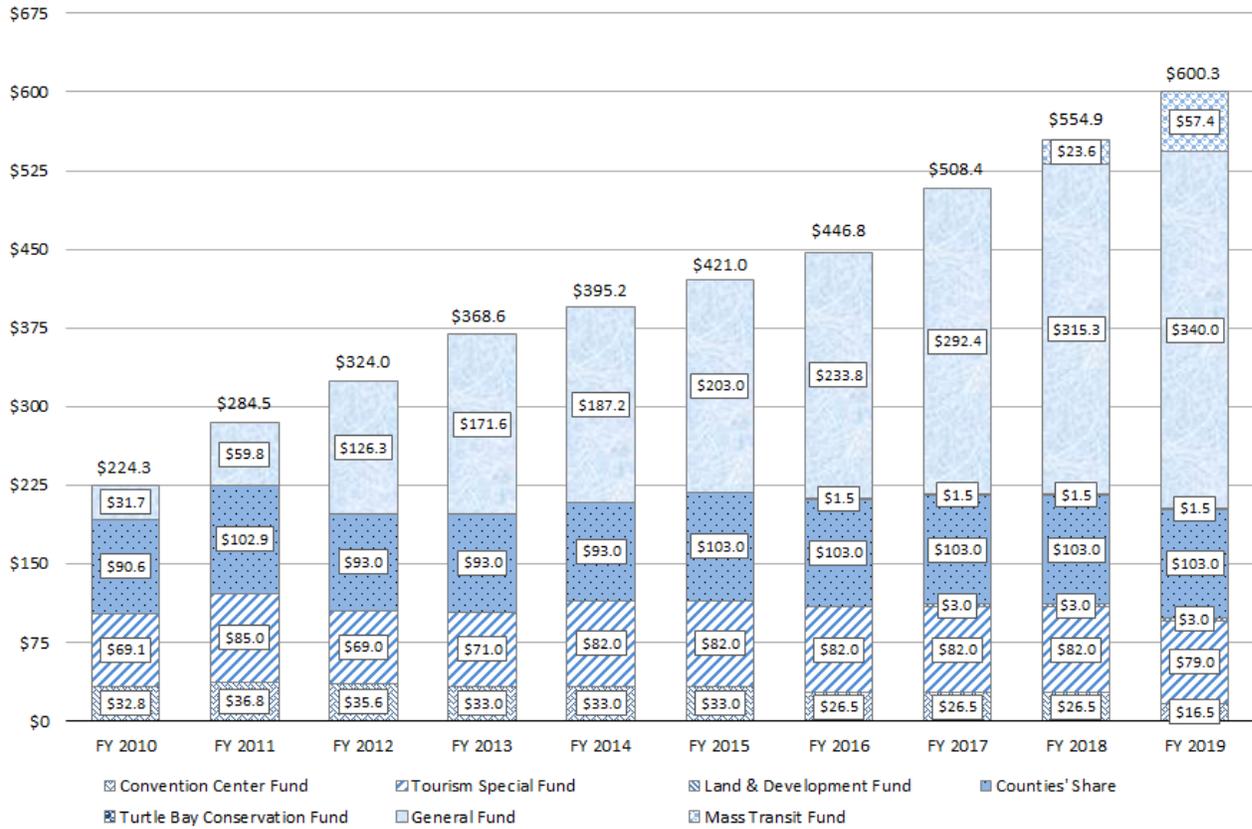


TABLE 1.4 - TRANSIENT ACCOMMODATIONS TAX
(In Thousands of Dollars)

	FY 2019	FY 2018	Difference	
			Amount	% Change
Collection				
Trans. Accom./Time Share Occ. Tax	\$ 600,310	\$ 554,890	\$ 45,419	8.2
Trans. Accom./Time Share Occ. Fees	24	22	2	10.9
Total	\$ 600,334	\$ 554,912	\$ 45,422	8.2
Distribution*				
Counties Share	\$ 103,000	\$ 103,000	\$ -	-
Convention Center Fund	16,500	26,500	(10,000)	(38)
Tourism Special Fund	79,000	82,000	(3,000)	(4)
Turtle Bay Special Fund	1,500	1,500	-	-
Land & Development Fund	3,000	3,000	-	-
Mass Transit Fund	57,354	23,626	33,727	143
General Fund	339,980	315,286	24,694	7.8
Total	\$ 600,334	\$ 554,912	\$ 45,422	8.2

*For details on distribution see section 237D-6.5, HRS.

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

1.5.3 Recent Legislation

Act 86, SLH 2018, reduces the allocations of TAT to the Convention Center Special Fund from \$26.5 million to \$16.5 million and the Tourism Special Fund from \$82 million to \$79 million. The Act is effective July 1, 2018.

Act 211, SLH 2018, imposes the TAT on transient accommodations brokers, travel agencies, and tour packagers that enter into arrangements to furnish transient accommodations at noncommissioned negotiated contract rates on their share of the proceeds. The Act is effective July 1, 2018, and applies to taxable years beginning after December 31, 2018.

Act 20, SLH 2019, imposes the transient accommodations tax on resort fees and defines resort fees as "any mandatory charge or surcharge imposed by an operator, owner, or representative thereof to a transient for the use of the transient accommodation's property, services, or amenities." The Act formally supports DOTAX's long-standing position on resort fees.

1.6 FUEL TAXES

1.6.1 Overview

The State and county fuel taxes are imposed on the distributors. The State Legislature sets the State fuel tax rates, whereas county councils set the county rates. There is also an environmental response tax (officially renamed as the "environmental response, energy and food security tax" by

Act 73, SLH 2010) that is levied on each barrel of petroleum products and each million British thermal units (MMBtu) of non-petroleum fossil fuels sold by a distributor to any retail dealer or end user. The effective rates for the fuel taxes and for the environmental response tax are shown on page 15.

1.6.2 Revenue

Fuel tax collections (including the environmental response tax) amounted to \$206.3 million in FY 2019, an increase of 2.3% from the \$201.8 million collected in FY 2018. Total taxable fuel consumption increased from 920.5 million gallons in FY 2018 to 953.3 million gallons in FY 2019. The biggest consumption of taxable fuel was gasoline (463.3 million gallons) and the second biggest consumption was aviation fuel (260.5 million gallons). Together, gasoline and aviation fuel accounted for 75.9% of the total consumption of taxable fuel in FY 2019.

The revenues from fuel taxes are distributed to several special funds. One percent of the fuel taxes paid on liquid fuel, not including aviation fuel, are deposited into the Boating Special Fund. Fuel taxes paid on sales of aviation fuel are deposited into the Airport Revenue Fund. Remaining revenues from the State fuel taxes are deposited into the State Highway Fund, whereas remaining revenues from county fuel taxes are deposited into the counties' highway funds.

Collections of the environmental response tax amounted to \$28.0 million in FY 2019, an increase of 3.6% from the \$27.0 million collected in FY 2018. The environmental response tax rate on each barrel of petroleum product was \$1.05. The tax was levied on 25.2 million barrels of petroleum in FY 2019, up from 24.7 million barrels in FY 2018. The environmental response tax rate on each MMBtu of non-petroleum fossil fuels was nineteen cents. The tax was levied on 8.0 million MMBtu of non-petroleum fossil fuels in FY 2019, up from 5.8 million MMBtu in FY 2018.

Revenues from the environmental response tax were distributed as follows in FY 2019: For each barrel taxed at \$1.05, five cents went to the Environmental Response Revolving Fund administered by the Department of Health for oil spill prevention and remediation programs; fifteen cents went to the Energy Security Special Fund administered by the Department of Business, Economic Development, and Tourism to support the Hawaii clean energy initiative program; fifteen cents went to the Agricultural Development & Food Security Special Fund administered by the Department of Agriculture to fund activities intended to increase agricultural production or processing that may lead to reduced importation of food, fodder, or feed from outside the state; ten cents went to the Energy Systems Development Special Fund, and the remainder (sixty cents) went to the General Fund. For each MMBtu taxed at nineteen cents, one cent went to the Environmental Response Revolving Fund, three cents went to the Energy Security Special Fund, three cents went to the Agricultural Development & Food Security Special Fund, two cents went to the Energy Systems Development Special Fund, and the remainder (ten cents) went to the General Fund.

Chart 1.9 shows collections of the fuel taxes and the gallons consumed of the various fuel types, for FY 2010 through FY 2019. Data for taxable gallons consumed in FY 2018 and FY 2019 are given in Table 1.5. Table 1.6 shows how the fuel taxes and the environmental response tax were

allocated in FY 2018 and FY 2019. The table also shows allocations of motor vehicle taxes and fees, and rental motor vehicle taxes to the State Highway Fund.

SCHEDULE OF FUEL TAX RATES PER GALLON ⁴
(Effective July 1, 2018)

TYPE OF FUEL	STATE TAX	COUNTY TAX	TOTAL TAX
GASOLINE AND DIESEL OIL (HIGHWAY):			
City & County of Honolulu	16.0 ¢	16.5 ¢	32.5 ¢
County of Maui	16.0	23.0	39.0
County of Hawaii ³	16.0	19.0	35.0
County of Kauai	16.0	17.0	33.0
LIQUEFIED PETROLEUM GAS (HIGHWAY):			
City & County of Honolulu	5.2 ¢	5.4 ¢	10.6 ¢
County of Maui	5.2	11.5	16.7
County of Hawaii ³	5.2	6.3	11.5
County of Kauai	5.2	5.6	10.8
ETHANOL (HIGHWAY):			
City & County of Honolulu	2.4 ¢	2.4 ¢	4.8 ¢
County of Maui	2.4	11.5	13.9
County of Hawaii ³	2.4	2.8	5.2
County of Kauai	2.4	2.5	4.9
METHANOL (HIGHWAY):			
City & County of Honolulu	1.9 ¢	1.8 ¢	3.7 ¢
County of Maui	1.9	11.5	13.4
County of Hawaii ³	1.9	2.1	4.0
County of Kauai	1.9	1.9	3.8
BIODIESEL (HIGHWAY):			
City & County of Honolulu	4.0 ¢	8.3 ¢	12.3 ¢
County of Maui	4.0	0.0	4.0
County of Hawaii	4.0	0.0	4.0
County of Kauai	4.0	0.0	4.0
NAPHTHA (Power-Generating Facility): All Counties	2.0 ¢	0.0 ¢	2.0 ¢
COMPRESSED NATURAL GAS (HIGHWAY):			
City & County of Honolulu	4.0 ¢	8.2 ¢	12.2 ¢
County of Maui	4.0	11.4	15.4
County of Hawaii ³	4.0	9.4	13.4
County of Kauai	4.0	8.4	12.4
LIQUEFIED NATURAL GAS (HIGHWAY):			
City & County of Honolulu	4.0 ¢	8.2 ¢	12.2 ¢
County of Maui	4.0	11.4	15.4
County of Hawaii ³	4.0	9.4	13.4
County of Kauai	4.0	8.4	12.4
ENVIRONMENTAL RESPONSE, ENERGY, & FOOD SECURITY TAX			
All Counties, per barrel of petroleum products ¹	105.0 ¢	0.0 ¢	105.0 ¢
All Counties, per million BTU of fossil fuels ²	19.0	0.0	19.0

¹ Does not include aviation fuel.

² Does not include petroleum products. BTU = British thermal unit.

³ Effective July 1, 2018, pursuant to Hawaii County Resolution No. 212-17, Draft 2.

⁴ Gasoline used for agricultural equipment off highways, aviation fuel, and diesel oil used off highways are taxed by the State at 1 cent per gallon.

**Chart 1.9 - Fuel Tax and Trends in Fuel Consumption
Fiscal Years 2010 - 2019**

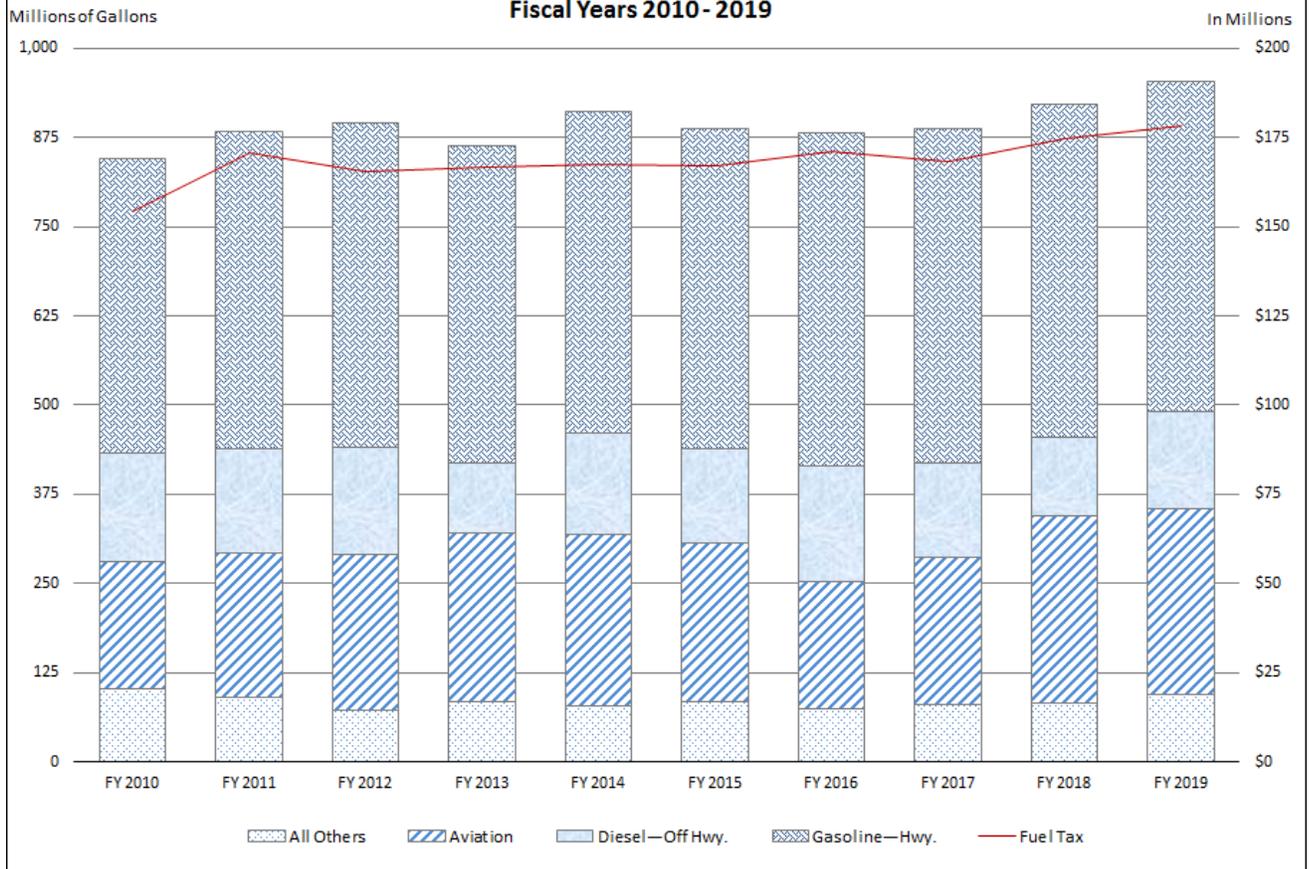


TABLE 1.5 - TAXABLE GALLONS OF FUEL CONSUMED
(In Thousands of Gallons)

	FY 2019	FY 2018	Difference	
			Amount	% Change
Gasoline	463,318	465,973	(2,655)	(0.6)
Diesel Oil - Off Highway	135,732	109,612	26,121	23.8
Diesel Oil - Highway	48,029	49,108	(1,078)	(2.2)
Liq. Pet. Gas - Highway	7	26	(19)	(73.1)
Small Boats - Gasoline	1,547	1,403	143	10.2
Small Boats - Diesel Oil	3,103	3,001	102	3.4
Aviation Fuel	260,491	263,192	(2,701)	(1.0)
Other Fuel ¹	41,022	28,172	12,850	45.6
Total Gallons	953,250	920,486	32,763	3.6
Environmental Tax				
Petroleum Products (Barrel) ²	25,177,846	24,652,884	524,962	2.1
Fossil Fuels (MMBtu) ³	7,969,937	5,812,564	2,157,373	37.1

¹ Other fuel includes ethanol, methanol, biodiesel, naphtha, compressed natural gas, and liquefied natural gas.

² Barrel = 42 U.S. gallons of petroleum products.

³ MMBtu = 1 million British thermal units.

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

TABLE 1.6 - ALLOCATION OF FUEL TAXES
(In Thousands of Dollars)

	FY 2019 ¹	FY 2018 ²	Difference	
			Amount	% Change
STATE HIGHWAY FUND				
Gasoline	\$ 73,551	\$ 73,957	\$ (405)	(0.5)
Diesel Oil - Off Highway	1,374	1,129	246	21.8
Diesel Oil - Highway	7,608	7,779	(171)	(2.2)
Liq. Pet. Gas - Highway	0	1	(1)	(73.1)
Other Fuel ³	854	623	231	37.0
Subtotal	\$ 83,388	\$ 83,489	\$ (100)	(0.1)
Motor Vehicle	138,126	138,395	(268)	(0.2)
Rental Vehicle	57,991	54,844	3,147	5.7
TOTAL	\$279,505	\$276,727	\$ 2,778	1.0
COUNTY HIGHWAY FUNDS				
City & County of Honolulu	\$ 51,140	\$ 51,790	\$ (650)	(1.3)
County of Maui	16,430	16,450	(19)	(0.1)
County of Hawaii	17,343	12,988	4,355	33.5
County of Kauai	5,729	5,718	11	0.2
TOTAL	\$ 90,643	\$ 86,946	\$ 3,697	4.3
BOATING SPECIAL FUND	\$ 1,758	\$ 1,722	\$ 36	2.1
STATE AIRPORT FUND				
Aviation Fuel	\$ 2,605	\$ 2,632	\$ (27)	(1.0)
ENVIRONMENTAL RESPONSE REVOLVING FUND	\$ 1,339	\$ 1,291	\$ 48	3.7
ENERGY SECURITY FUND	\$ 4,016	\$ 3,872	\$ 143	3.7
ENERGY SYSTEMS DEVELOPMENT FUND	\$ 2,677	\$ 2,582	\$ 96	3.7
AGRICULTURAL DEVELOPMENT & FOOD SECURITY FUND	\$ 4,016	\$ 3,872	\$ 143	3.7
GENERAL FUND	\$ 15,904	\$ 15,373	\$ 531	3.5

¹ Includes amounts totaling \$183 thousand in undistributed fuel tax from previous years that were included in several monthly reports in fiscal year 2019. Fuel tax collections were \$206,162 thousand for fiscal year 2019.

² Includes amounts totaling \$475 thousand in undistributed fuel tax from previous years that were included in several monthly reports in fiscal year 2018. Fuel tax collections were \$201,303 thousand for fiscal year 2018.

³ Other fuel includes ethanol, methanol, biodiesel, naphtha, compressed natural gas, and liquefied natural gas.

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

1.7 MOTOR VEHICLE TAXES AND FEES

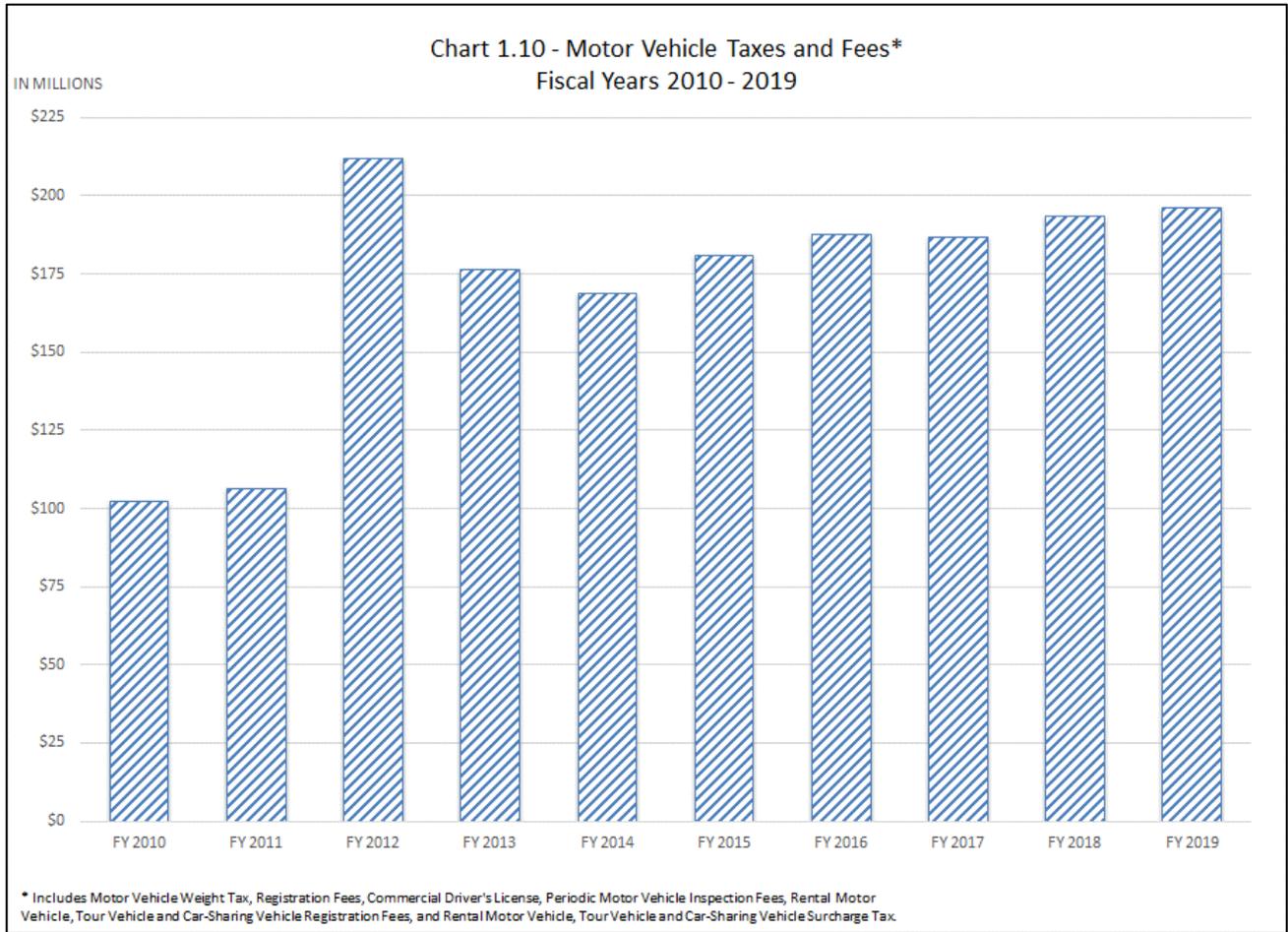
1.7.1 Overview

The State levies an annual registration fee per vehicle and a tax based on vehicle weight. The State also levies the rental motor vehicle, tour vehicle, and car-sharing vehicle surcharge tax (RVST). The tax on rentals of motor vehicles is imposed on the lessor. The rate of the tax was increased from \$3.00 per day to \$5.00 per day effective July 1, 2019. The tax on tour vehicles is imposed on the tour vehicle operator. The rate of the tax is \$65 per month for each tour vehicle in the 26 passenger seat and over category, and \$15 per month for each tour vehicle in the 8 to 25 passenger seat category. The tax on motor vehicles that are rented or leased by a car-sharing organization is imposed on the car-sharing organization. The rate of the tax is 25 cents per half-hour. There is a one-time \$20 registration fee for those subject to any part of the RVST.

1.7.2 Revenue

For FY 2019, the State's motor vehicle taxes and fees (including the RVST) totaled \$196.1 million, compared to \$193.2 million in FY 2018, an increase of 1.5%.

Chart 1.10 shows the total motor vehicle taxes and fees for FY 2010 through FY 2019. The large increase in FY 2012 was caused by a temporary increase in the rate of the RVST to \$7.50 per day, which was in place from July 1, 2011 to June 30, 2012. The collections for FY 2013 also reflect one month of collections at the higher tax rate, since the collections lag the liabilities incurred by one month.



1.7.1 Recent Legislation

Act 215, SLH 2018, imposes an additional \$2 per day surcharge tax on rental motor vehicles when the lessee does not have a valid Hawaii driver's license. The Act also increases the tour vehicle surcharge tax by \$1 per month. The Act is effective January 1, 2019.

Act 174, SLH 2019, repeals the \$2 per day rental motor vehicle surcharge on lessees without a valid Hawaii driver's license and increases the rate of the rental motor vehicle surcharge tax from \$3 per day to \$5 per day. The repeal of the \$2 per day surcharge was necessary, because it may have been unconstitutional under the dormant commerce clause of the United States Constitution. The Act also repeals the special allocations of the \$2 per day surcharge to the various counties and deposits the full \$5 per day into the highway fund. The Act is effective July 1, 2019.

1.8 CIGARETTE AND TOBACCO TAX

1.8.1. Overview

Wholesalers and dealers, as those terms are defined in section 245-1, HRS, must pay an excise tax on the sale or use of tobacco products and on each cigarette or little cigar sold, used, or possessed. The tax per cigarette or little cigar was increased to 16 cents for sales on and after July 1, 2011. The

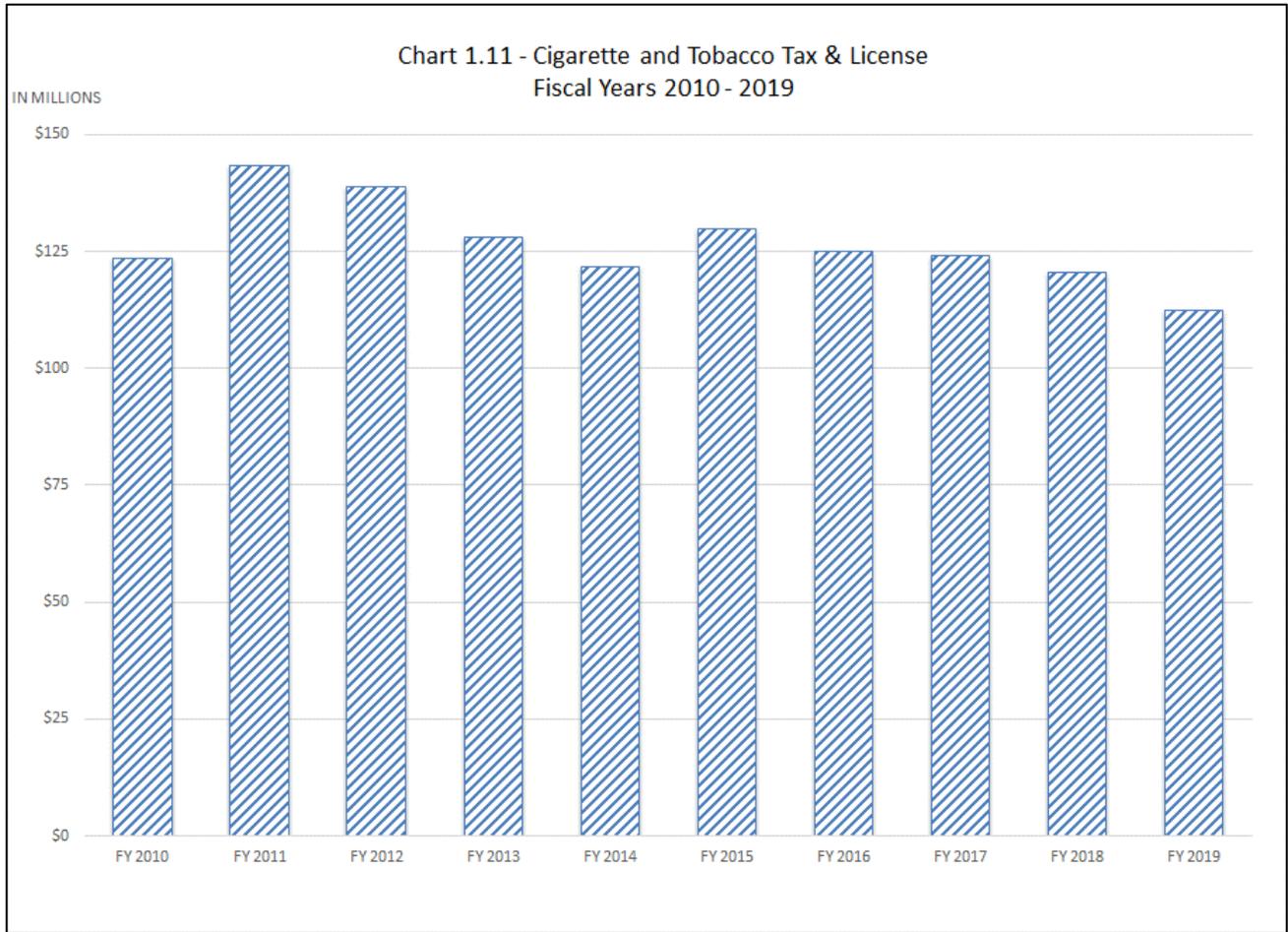
excise tax on large cigars is 50% of the wholesale price and the excise tax on all other tobacco products (tobacco in any form except cigarettes, little cigars or large cigars) is 70% of the wholesale price. A \$2.50 tobacco tax license is required and must be renewed annually before July 1. Cigarette wholesalers and dealers are required to affix a stamp to each individual cigarette package as proof the tax has been paid. Every retailer engaged in the retail sale of cigarettes and other tobacco products is required to obtain a \$20 retail tobacco permit that must be renewed annually before December.

1.8.2 Revenue

During FY 2019, collections of the cigarette and tobacco tax (including tobacco licenses) totaled \$112.5 million, compared to \$120.5 million in FY 2018, or a decrease of 6.6%. The 16 cent tax per cigarette was distributed to various special funds with the remainder going to the General Fund. Additionally, a total of \$1.8 million went to the Cigarette Stamp Administrative Fund and the Cigarette and Stamp Enforcement Fund. The remainder of the cigarette and tobacco tax went to the General Fund.

FY2019 16 Cent Tax Per Cigarette Distribution	Cents
Hawaii Cancer Research Special Fund	2.000
Trauma System Special Fund	1.125
Community Health Centers Special Fund	1.250
Emergency Medical Services Special Fund	1.250
General Fund	10.375

Chart 1.11 shows the total collections of the tax for FY 2010 through FY 2019. Table 1.7 shows collections of the tobacco taxes and how the revenues were allocated in FY 2018 and FY 2019.



**TABLE 1.7 - CIGARETTE & TOBACCO TAX
(In Thousands of Dollars)**

	FY 2019	FY 2018	Difference	
			Amount	% Change
Collection				
Tobacco & Licenses	\$ 112,518	\$ 120,522	\$ (8,005)	(6.6)
Distribution*				
Hawaii Cancer Research Fund	\$ 12,993	\$ 13,917	\$ (924)	(6.6)
Trauma System Fund	6,989	7,400	(411)	(6)
Emergency Medical Services Fund	8,122	8,700	(578)	(7)
Community Health Centers Fund	8,122	8,700	(578)	(7)
Cigarette Stamp Administrative & Enforcement Funds	1,766	1,892	(126)	(6.6)
General Fund	74,526	79,914	(5,388)	(6.7)
Total	\$ 112,518	\$ 120,522	\$ (8,005)	(6.6)

*Details on distributions of the revenues are given in section 245-15, HRS.

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

1.9 PUBLIC SERVICE COMPANY TAX

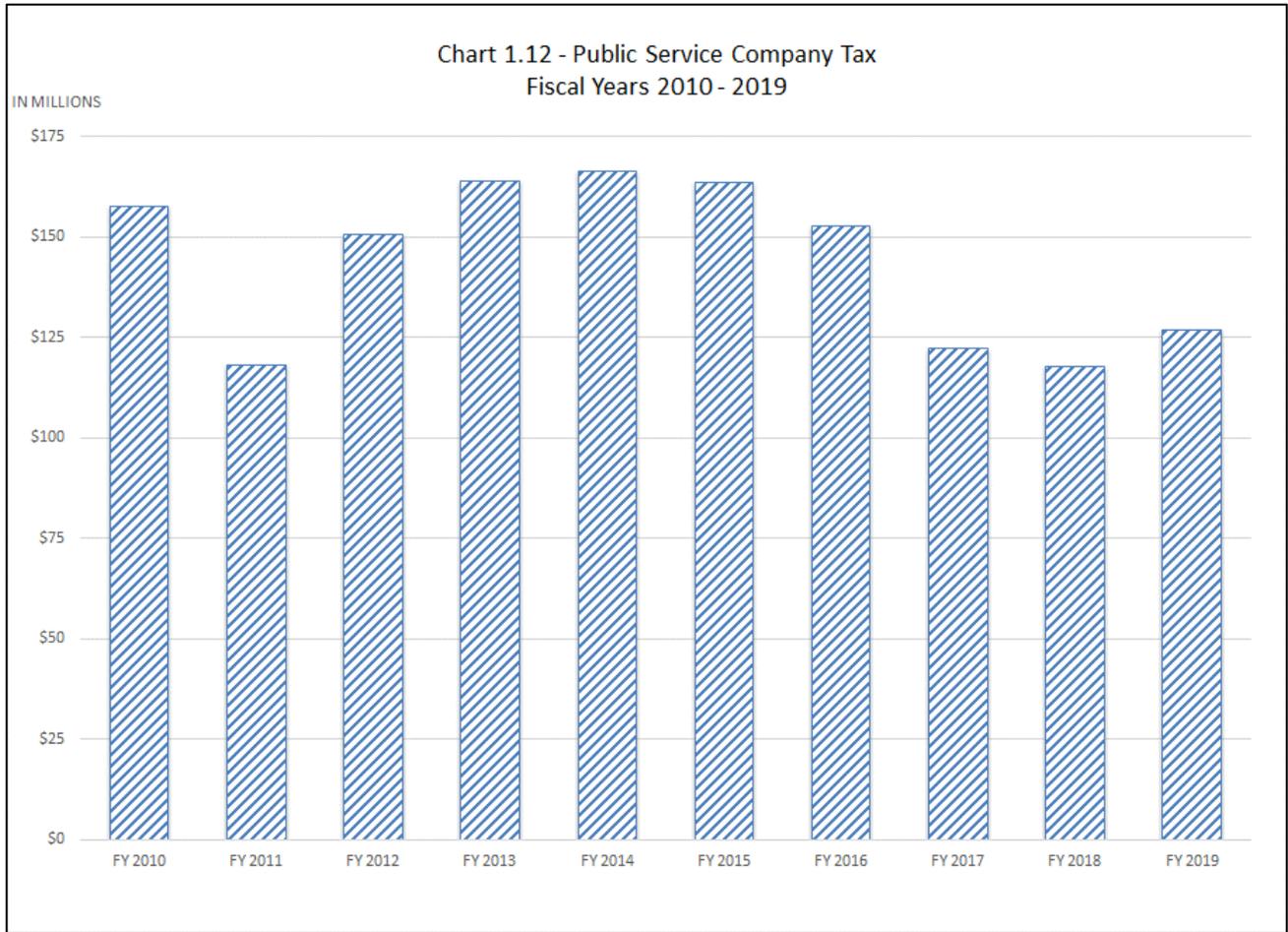
1.9.1 Overview

The public service company (PSC) tax is levied on public utility businesses in lieu of all taxes except income taxes, vehicular taxes imposed under chapter 249, HRS, the franchise tax on public utilities imposed under chapter 240, HRS, and the use tax imposed under chapter 238, HRS. Generally, the tax is applied to gross income from the business for the preceding calendar year. The tax rates on the PSC's range from 0.50% (levied on sales for resale) to 8.20%. For a public utility, only the first 4.0% is realized by the State; any excess over 4.0% is distributed to counties that provide a real property tax exemption for property used by the public utility in its business. For a carrier of passengers by land between points on a scheduled route, the gross income from passenger fares is taxed at 5.35%, all of which is realized by the State.

1.9.2 Revenue

The PSC tax yielded \$126.7 million in tax, penalty, and interest in FY 2019, an increase of 7.7% from the \$117.6 million collected in FY 2018. All of the revenues from the PSC tax are allocated to the General Fund.

Chart 1.12 shows the total collections of the tax for FY 2010 through FY 2019.



1.10 UNEMPLOYMENT INSURANCE TAX

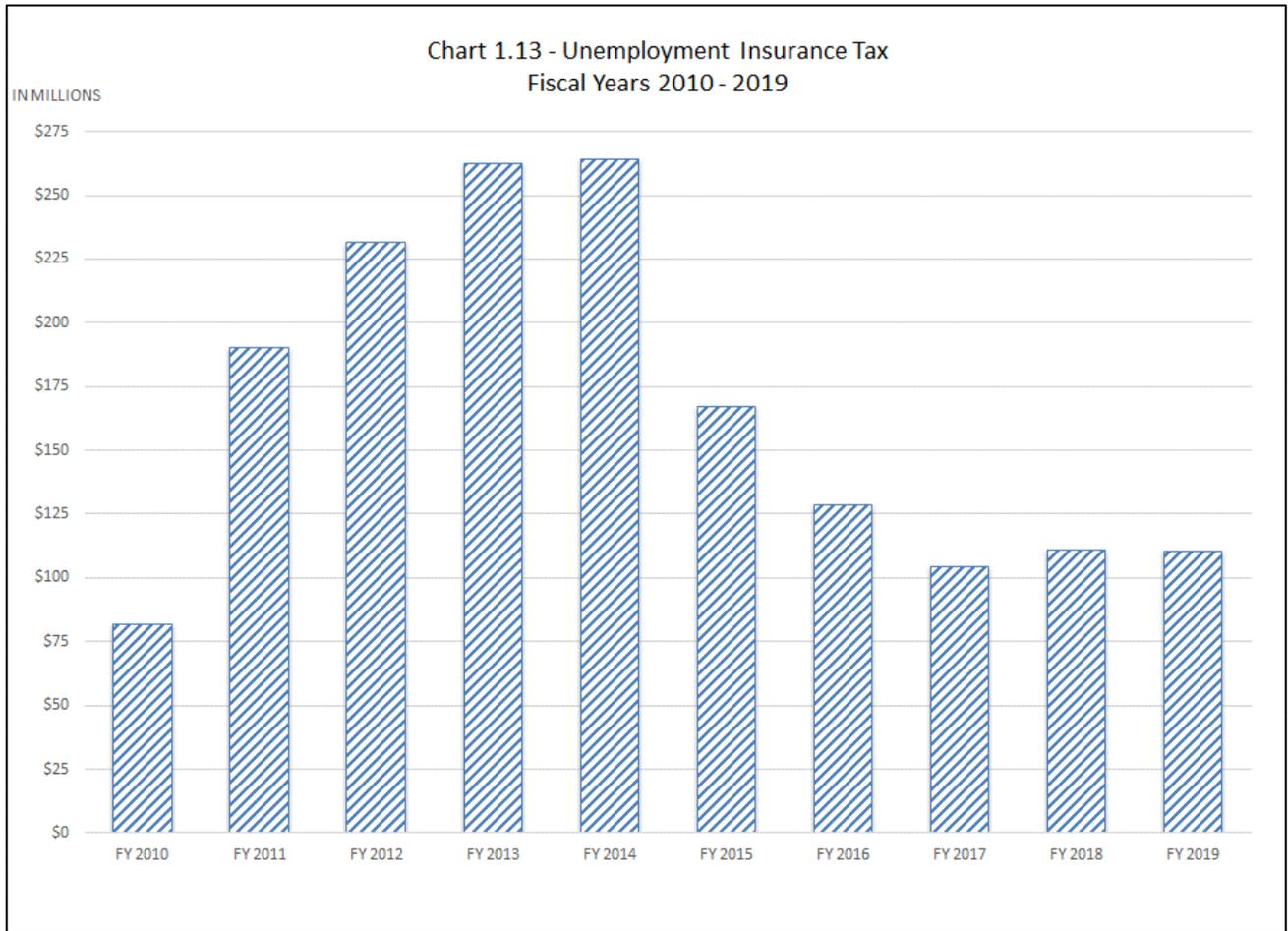
1.10.1 Overview

The unemployment insurance (UI) tax (officially "employment security contributions") is imposed on wages paid by employers with one or more employees, with certain exemptions. The tax is experience rated. The UI tax rate for each year depends on the condition of the UI Trust Fund. The tax base represents the state's average annual wages reported by employers contributing to the Unemployment Trust Fund. For FY 2018, the tax base ranged from \$44,000 in CY 2017 to \$45,900 in CY 2018 and the contribution rate for new employers was 2.4% in both CY 2017 and CY 2018. Revenues from the tax go to the Unemployment Trust Fund. The Department of Labor and Industrial Relations administers the UI tax and DOTAX collects the tax.

1.10.2 Revenue

For FY 2019, revenue from the UI tax totaled \$110.3 million, down by 0.5% from \$110.9 million collected in FY 2018.

Chart 1.13 shows collections of the UI tax for FY 2010 through FY 2019.



1.11 INSURANCE PREMIUM TAX

1.11.1 Overview

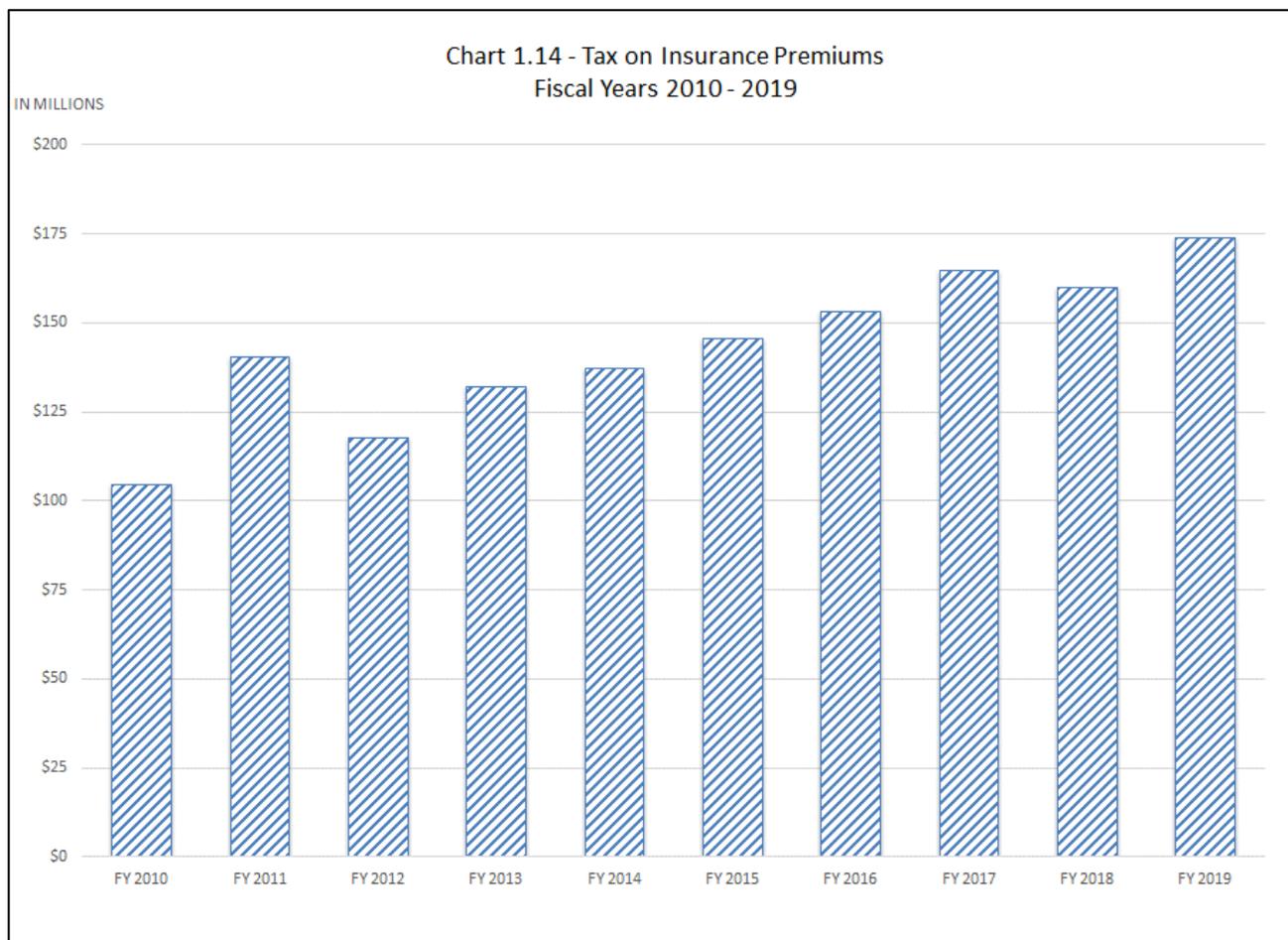
The tax on insurance premiums applies to insurance companies (underwriters) based on premiums written in Hawaii. The insurance premium tax is in lieu of all taxes except property tax and taxes on the purchase, use or ownership of tangible personal property. To insurers who qualify, there is a 1.0% tax credit to facilitate regulatory oversight. The tax is administered and collected by the Insurance Commissioner at the Department of Commerce and Consumer Affairs, who is required to report to the Director of Taxation the amounts of all taxes collected under chapter 431, HRS.

Insurance Premium Tax Rates	%
Life Insurance	2.75%
Surplus Lines	4.68%
Ocean Marine (on gross underwriting profit)	0.8775%
Other Insurance	4.265%

1.11.2 Revenue

For FY 2019, the tax on insurance premiums totaled \$173.8 million, compared to \$159.8 million in FY 2018, an increase of 8.8%.

Chart 1.14 shows collections of the tax for FY 2010 through FY 2019.



1.12 LIQUOR TAX

1.12.1 Overview

The tax on liquor is a gallonage tax imposed on dealers as defined in section 244D-1, HRS, and upon certain others who sell or use liquor. A \$2.50 liquor tax permit is required and must be renewed annually before July 1. See section 244D-4, HRS, for exemptions from the tax. The tax rates per wine gallon are \$5.98 on distilled spirits, \$2.12 on sparkling wine, \$1.38 on still wine, \$0.85 on cooler beverages, \$0.93 on beer other than draft beer, and \$0.54 on draft beer.

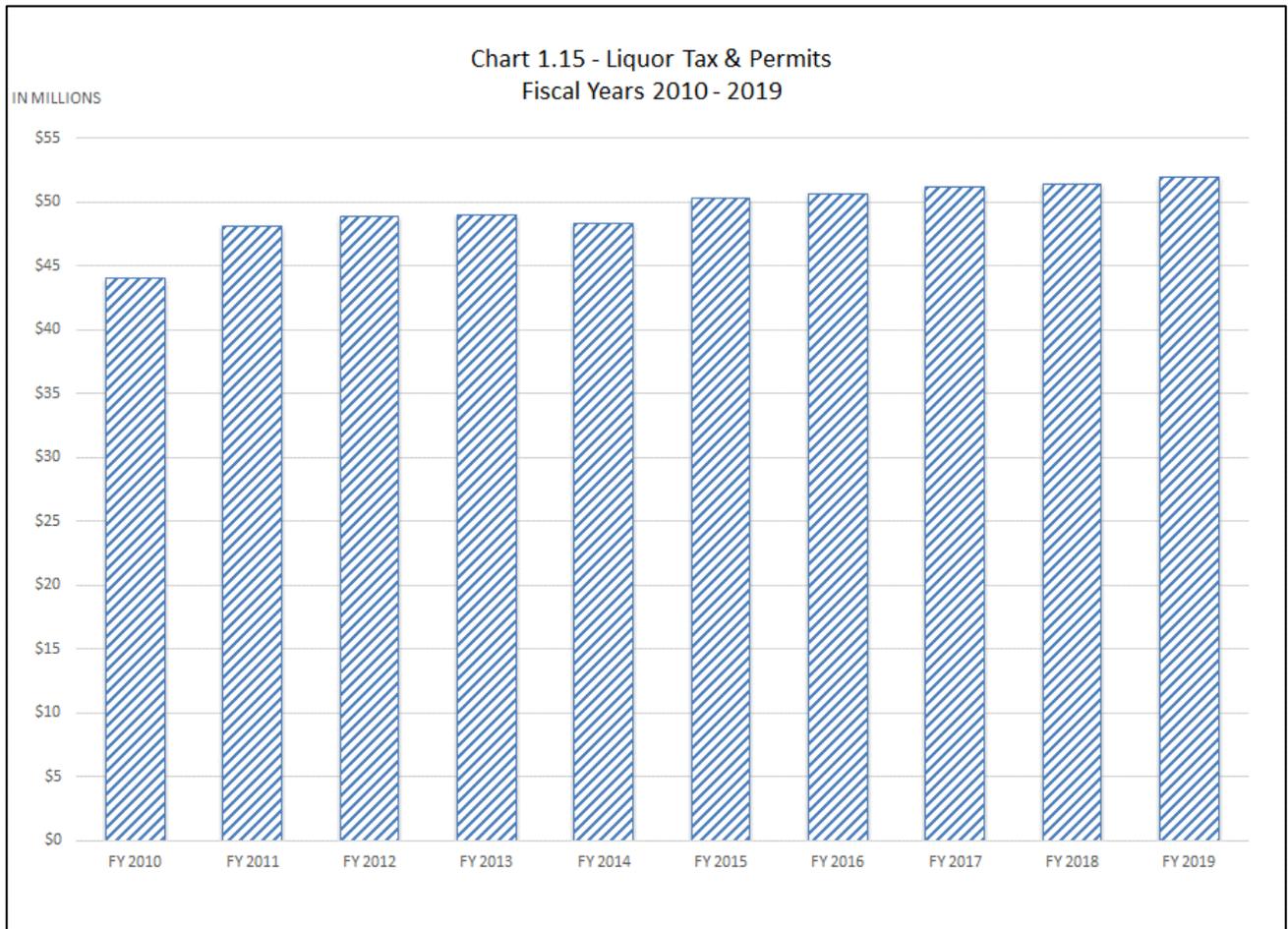
Liquor Tax Rates (per wine gallon)	\$
Distilled Spirits	\$5.98

Sparkling Wine	\$2.12
Still Wine	\$1.38
Cooler Beverages	\$0.85
Beer (Other than draft beer)	\$0.93
Draft Beer	\$0.54

1.12.2 Revenue

For FY 2019, the liquor tax and permit fees totaled \$51.9 million, an increase of 1.0% from the \$51.4 million collected in FY 2018.

Chart 1.15 shows collections of the liquor tax and permit fees for FY 2010 through FY 2019.



1.13 CONVEYANCE TAX

1.13.1 Overview

The conveyance tax is imposed on all documents transferring ownership or interest in real

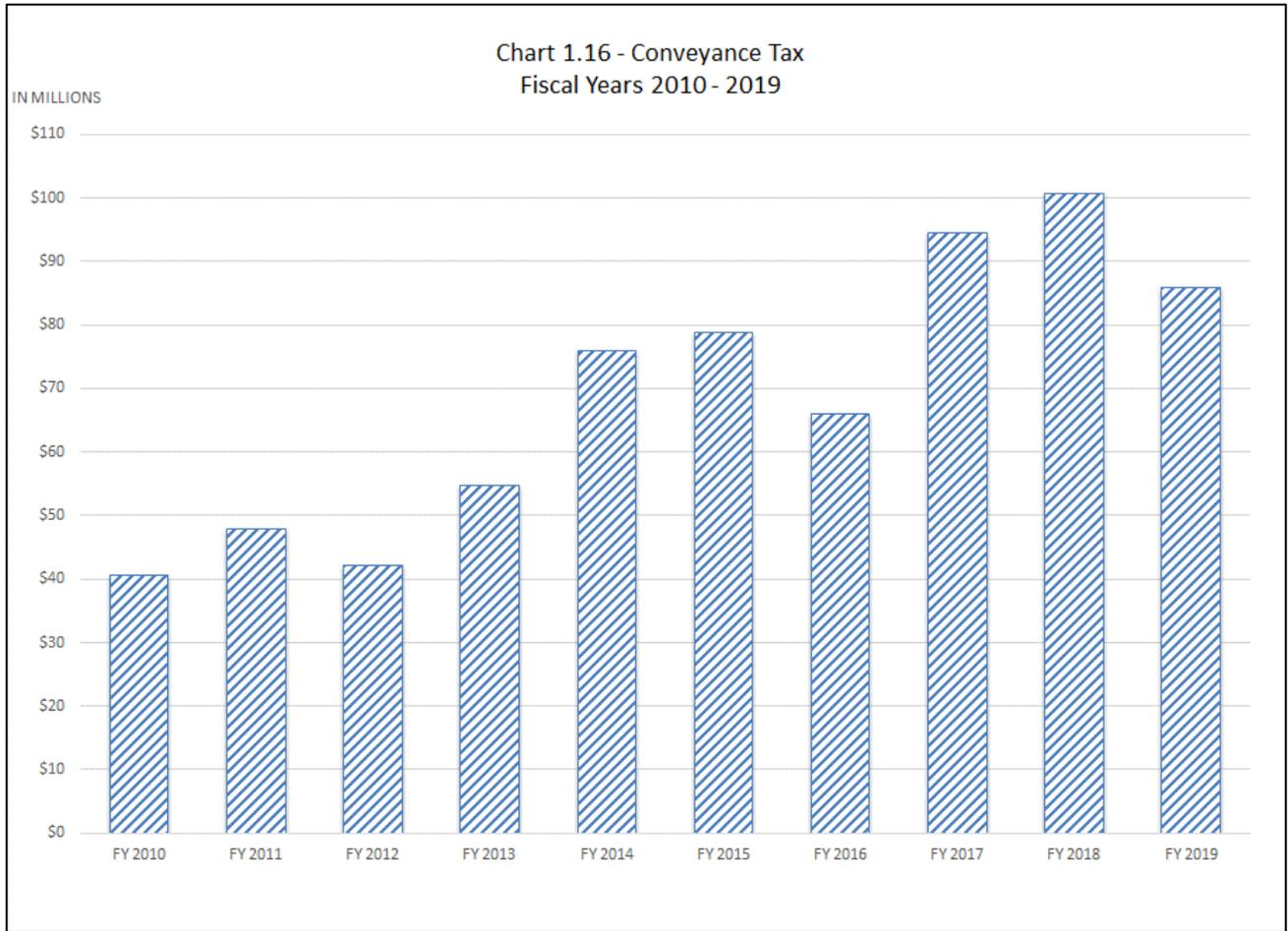
property and is based on actual and full consideration paid or to be paid. For a sale of a condominium or single family residence, the rate of the conveyance tax depends on whether the purchaser is eligible for a county homeowners' exemption from the real property tax. If the purchaser is eligible for the exemption, or if the sale is of real property other than a condominium or single family residence, then the tax rate ranges from 10 cents per \$100 for properties with a value of less than \$600,000 to \$1 per \$100 for properties with a value of \$10,000,000 or more. If the purchaser is ineligible for the exemption, the tax rate for a sale of a condominium or single family residence ranges from 15 cents per \$100 for properties with a value of less than \$600,000 to \$1.25 per \$100 for properties with a value of \$10,000,000 or more. The conveyance tax is administered by DOTAX, but is collected by the Bureau of Conveyances in the Department of Land and Natural Resources.

1.13.2 Revenue

For FY 2019, revenue from the conveyance tax totaled \$86.0 million, compared to \$100.6 million in FY 2018, a decrease of 14.6%.

FY2019 Conveyance Tax Distribution	%
Land Conservation Fund (Provided excess of \$6.8 million in any FY is deposited into the General Fund)	10%
Rental Housing Trust Fund (Provided excess of \$38 million in any FY is deposited into the General Fund)	50%
General Fund	40%

Chart 1.16 shows collections of the conveyance tax for FY 2010 through FY 2019.



1.14 TAX ON BANKS AND OTHER FINANCIAL CORPORATIONS

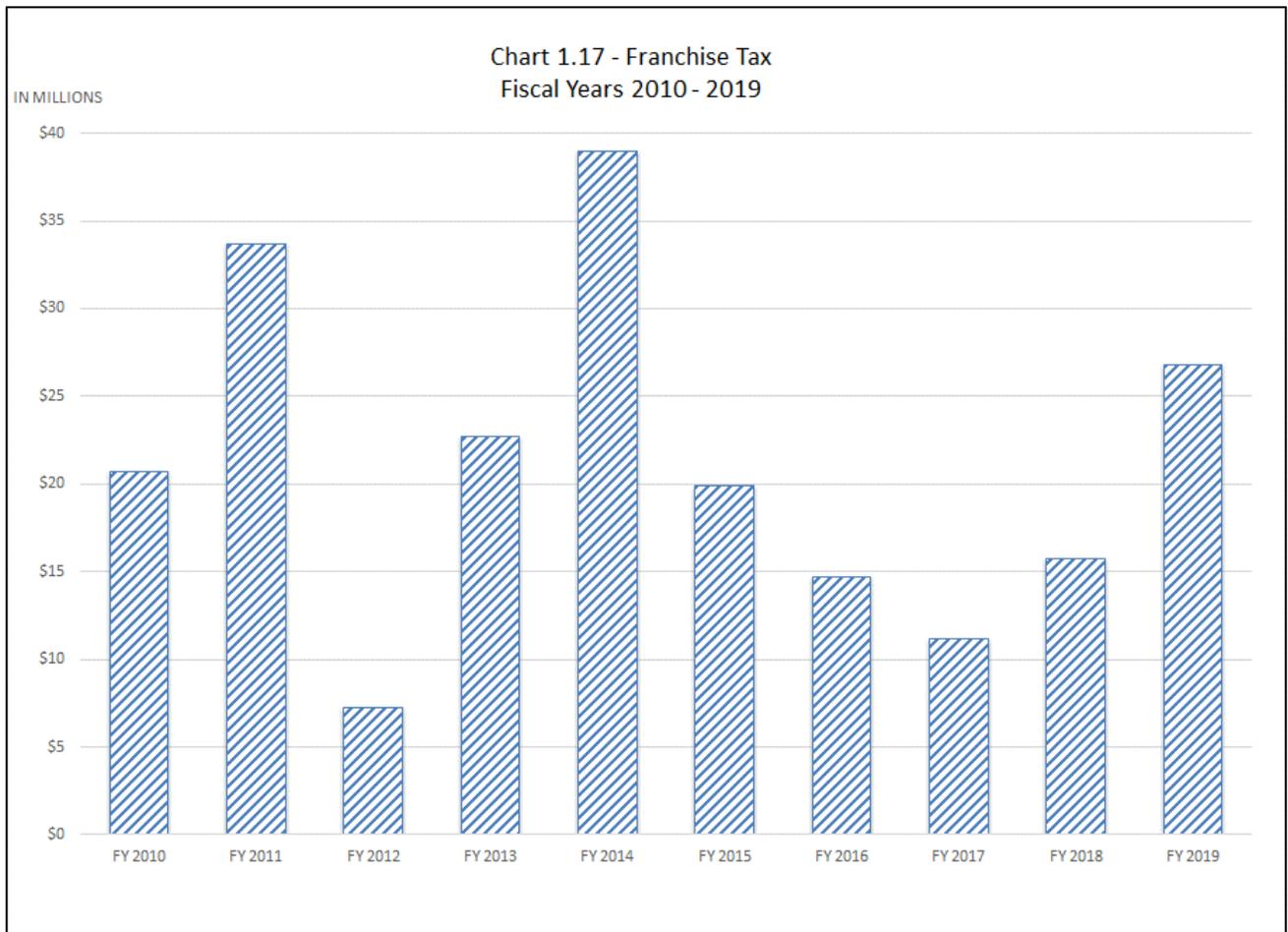
1.14.1 Overview

The tax on banks and other financial corporations (the franchise tax) is levied on net income of 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, and subsidiaries not subject to the tax imposed by chapter 235, HRS. The tax is in lieu of the net income tax imposed under chapter 235, HRS, and of the GET, but it uses the definition of net income from chapter 235, with modifications. The tax is levied on net income at the rate of 7.92%. The assessment date is January 1 of each year.

1.14.2 Revenue

For FY 2019, franchise tax collections totaled \$26.8 million, compared to \$15.7 million in FY 2018, an increase of 70.6%.

Chart 1.17 shows collections of the franchise tax for FY 2010 through FY 2019. Collections of the tax were low in FY 2012, due partly to a one-time transfer of \$16.5 million to the Litigated Claims Fund).



1.15 ESTATE AND TRANSFER TAX

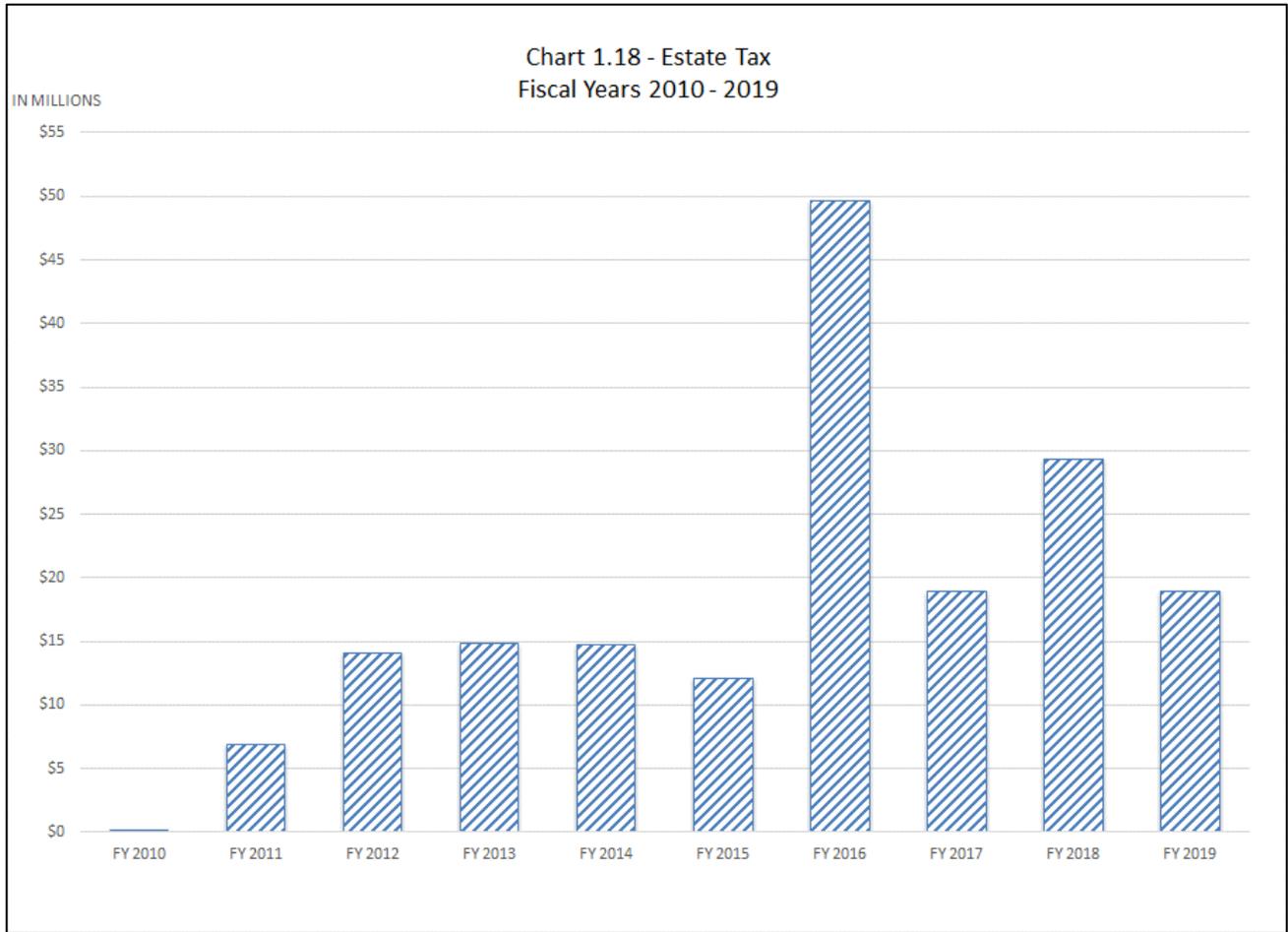
1.15.1 Overview

Hawaii's estate and transfer tax is levied on the transfer of a taxable estate. "Taxable estate" is based on the federal definition (with adjustments for nonresidents), but the State has its own tax rate schedule with rates varying from 10.0% to 15.7%. The generation skipping tax is also based on the federal taxable transfer, but has its own tax rate, which is currently 2.25%.

1.15.2 Revenue

For FY 2019, estate tax collections totaled \$18.9 million, compared to \$29.4 million collected in FY 2018.

Chart 1.18 shows collections of the estate and transfer tax for FY 2010 through FY 2019.



1.15.3 Recent Legislation

Act 3, SLH 2019, is effective April 4, 2019 and applies to decedents dying after December 31, 2019. The act establishes a new estate tax rate bracket for taxable estates exceeding \$10 million.

Act 69, SLH 2019, selectively conforms Hawaii income tax and estate tax laws to the Internal Revenue Code (IRC) as of December 31, 2018. The Act clarifies that for Hawaii's estate tax, the exclusion amount is fixed at the level that applied to decedents dying on December 31, 2017, which was \$5,490,000. The Act is effective June 7, 2019, and applies to taxable years beginning, and to decedents dying, after December 31, 2018.

1.16 COUNTY SURCHARGE TAX

1.16.1 Overview

Act 247, SLH 2005, granted counties the authority to impose a county surcharge of no more than 0.5% on gross income that is subject to the State's 4.0% GET to fund county public transportation systems. DOTAX is required to administer and collect the surcharge for the counties.

The following counties have adopted the surcharge:

City and County of Honolulu: The county surcharge rate is 0.5% and is effective from January 1, 2007 through December 31, 2030.

County of Hawaii: The county surcharge rate is 0.25% for the period from January 1, 2019 through December 31, 2019 and 0.5% for the period from January 1, 2020 through December 31, 2030.

County of Kauai: The county surcharge rate is 0.5% and is effective from January 1, 2019 through December 31, 2030.

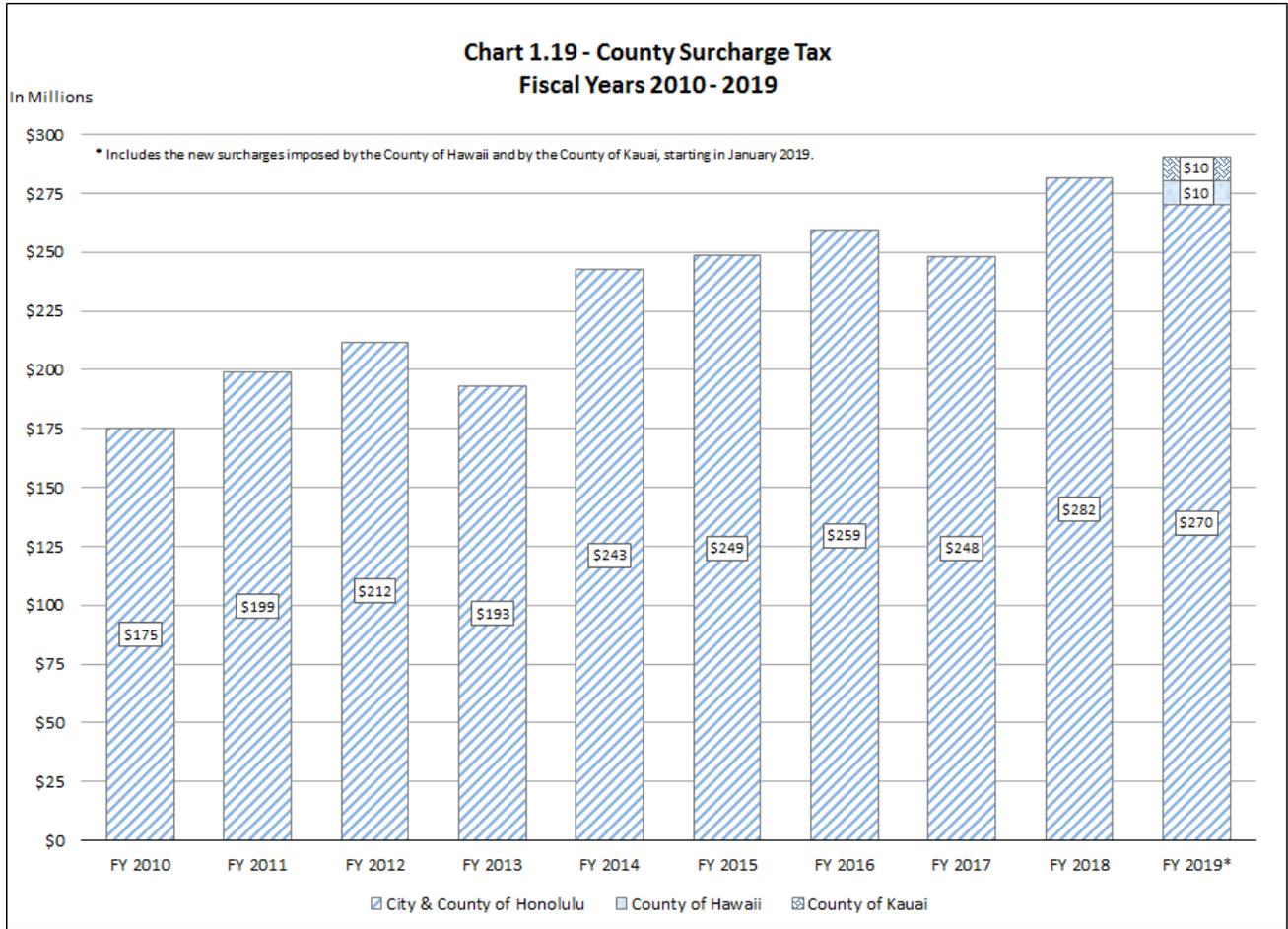
Starting September 5, 2017, the amount deducted from the county surcharge collections to reimburse the State for administrative costs decreased from 10% to 1%.

1.16.2 Revenue

For FY 2019, collections of county surcharges totaled \$290.7 million, an increase of 3.2% from the \$281.6 million collected in FY 2018. However, this was the first year surcharges imposed by the County of Hawaii and by the County of Kauai were included in the collections, which totaled \$20.7 million.

FY2019 County Surcharge Tax Distribution		\$
City and County of Honolulu		\$270.0 million
County of Hawaii		\$10.2 million
County of Kauai		\$10.5 million

Chart 1.19 shows collections of the county surcharges for FY 2010 through FY 2019.



1.16.3 Recent Legislation

Act 1, SSLH 2017, authorized the City and County of Honolulu to extend the sunset of its county surcharge from December 31, 2027 to December 31, 2030, which the County did by ordinance. The Act also authorized the other counties to establish a county surcharge, which may be levied from January 1, 2019 to December 31, 2030. New county surcharges were established by ordinance by Hawaii County (0.25%, from January 1, 2019 to December 31, 2020) and by Kauai County (0.50%, from January 1, 2019 to December 31, 2030). The Act reduced the amount that is deducted from the county surcharge collections to reimburse the State for administrative costs from 10% to 1%. The Act took effect September 5, 2017.

Act 11, SLH 2018, extends the period in which a county may adopt a surcharge on state tax, under certain conditions, from March 31, 2018 to March 31, 2019.

1.17 TOTAL TAX COLLECTIONS

Total tax collections in FY 2019 amounted to \$8.28 billion, up by 4.8% from the \$7.90 billion collected in FY 2018. DOTAX collected \$7.87 billion, the great majority of the total taxes. The counties collected \$138.1 million in State motor vehicle weight taxes and registration fees, the

Insurance Commissioner collected \$173.8 million in insurance premium taxes, and the Bureau of Conveyances collected \$86.0 million in conveyance taxes.

The total collections are shown in Table 1.8.

TABLE 1.8 - TAX COLLECTIONS ⁶
(In Thousands of Dollars)

SOURCE OF REVENUE	FY 2019		FY 2018	
	Amount Collected	% of Total	Amount Collected	% of Total
Banks - Financial Corps.	\$ 26,808	0.32	\$ 15,712	0.20
Conveyance	85,965	1.04	100,603	1.27
Employment Security Contributions	110,309	1.33	110,885	1.40
Fuel & Environmental ^{3,4}	206,345	2.49	201,778	2.56
General Excise & Use	3,541,389	42.80	3,395,566	43.01
County Surcharge ⁵	290,719	3.51	281,589	3.57
Income - Corporations	163,676	1.98	131,119	1.66
Income - Individuals	2,568,616	31.04	2,430,356	30.78
Inheritance and Estate	18,921	0.23	29,351	0.37
Insurance Premiums	173,844	2.10	159,814	2.02
Liquor & Permits	51,913	0.63	51,383	0.65
Motor Vehicle Tax ¹	196,120	2.37	193,241	2.45
Public Service Companies	126,691	1.53	117,641	1.49
Tobacco & Licenses	112,518	1.36	120,522	1.53
Trans. Accom. Fees	24	0.00	22	0.00
Trans. Accom. Tax	600,310	7.25	554,890	7.03
All Others ²	855	0.01	1,236	0.02
TOTAL	\$ 8,275,024	100.00	\$ 7,895,708	100.00

¹ Includes motor vehicle weight tax, registration fees, commercial driver's license, periodic motor vehicle inspection fees, rental motor vehicle, tour vehicle and car-sharing vehicle registration fees, and rental motor vehicle, tour vehicle and car-sharing vehicle surcharge tax.

² Includes fuel retail dealer permits, fuel penalty and interest, permitted transfers tax, and general excise fees.

³ Includes amounts totaling \$183 thousand in undistributed fuel tax from previous years that were included in several monthly reports in fiscal year 2019. Fuel tax collections were \$206,162 thousand for fiscal year 2019.

⁴ Includes amounts totaling \$475 thousand in undistributed fuel tax from previous years that were included in several monthly reports in fiscal year 2018. Fuel tax collections were \$201,303 thousand for fiscal year 2018.

⁵ Includes the new surcharges imposed by the County of Hawaii and by the County of Kauai, starting in January 2019.

⁶ Individual & corporation income taxes for FY 2017 & after are not comparable to prior years due to a new compiling method.

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

1.18 DISTRIBUTION OF TAXES

Of the \$8.28 billion in total tax collections in FY 2019, \$7.14 billion or 86.3% was deposited into the State's General Fund. The four counties received \$193.6 million from county fuel taxes and the

TAT. In addition, \$290.7 million of county surcharge was collected for the City and County of Honolulu, for the County of Hawaii and for the County of Kauai (before deducting the administrative fee imposed by the State). The remaining tax revenues not deposited into the General Fund or transferred to the counties were distributed among various State special funds. The State Highway Fund received the largest portion, \$279.5 million. All of the unemployment insurance tax (the employment security contributions) went into the Unemployment Trust Fund for unemployment benefits.

Table 1.9 shows allocations of taxes to the State's General Fund in FY 2018 and FY 2019. The distributions of the total tax collections among all funds in FY 2018 and FY 2019 are shown in Table 1.10.

TABLE 1.9 - STATE GENERAL FUND **
(In Thousands of Dollars)

SOURCE OF REVENUE	FY 2019		FY 2018	
	Amount Collected	% of Total	Amount Collected	% of Total
Banks - Financial Corps.	\$ 24,808	0.35	\$ 13,712	0.20
Conveyance	41,165	0.58	55,803	0.82
General Excise & Use	3,541,389	49.59	3,395,566	49.96
Income - Corporations	163,676	2.29	131,119	1.93
Income - Individuals	2,568,114	35.96	2,429,836	35.75
Inheritance and Estate	18,921	0.26	29,351	0.43
Insurance Premiums	173,844	2.43	159,814	2.35
Liquor & Permits	51,913	0.73	51,383	0.76
Public Service Companies	126,691	1.77	117,641	1.73
Tobacco & Licenses	74,526	1.04	79,914	1.18
Trans. Accom. Tax	339,956	4.76	315,264	4.64
Environmental Tax	15,904	0.22	15,373	0.23
All Others *	882	0.01	1,260	0.02
TOTAL	\$ 7,141,790	100.00	\$ 6,796,036	100.00

* Includes fuel retail dealer permits, fuel penalty and interest, permitted transfers tax, general excise fees, trans accom fees and rental vehicle fees.

** Individual & corporation income taxes for FY 2017 & after are not comparable to prior years due to a new compiling method.

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

TABLE 1.10 - DISTRIBUTION OF COLLECTIONS
(In Thousands of Dollars)

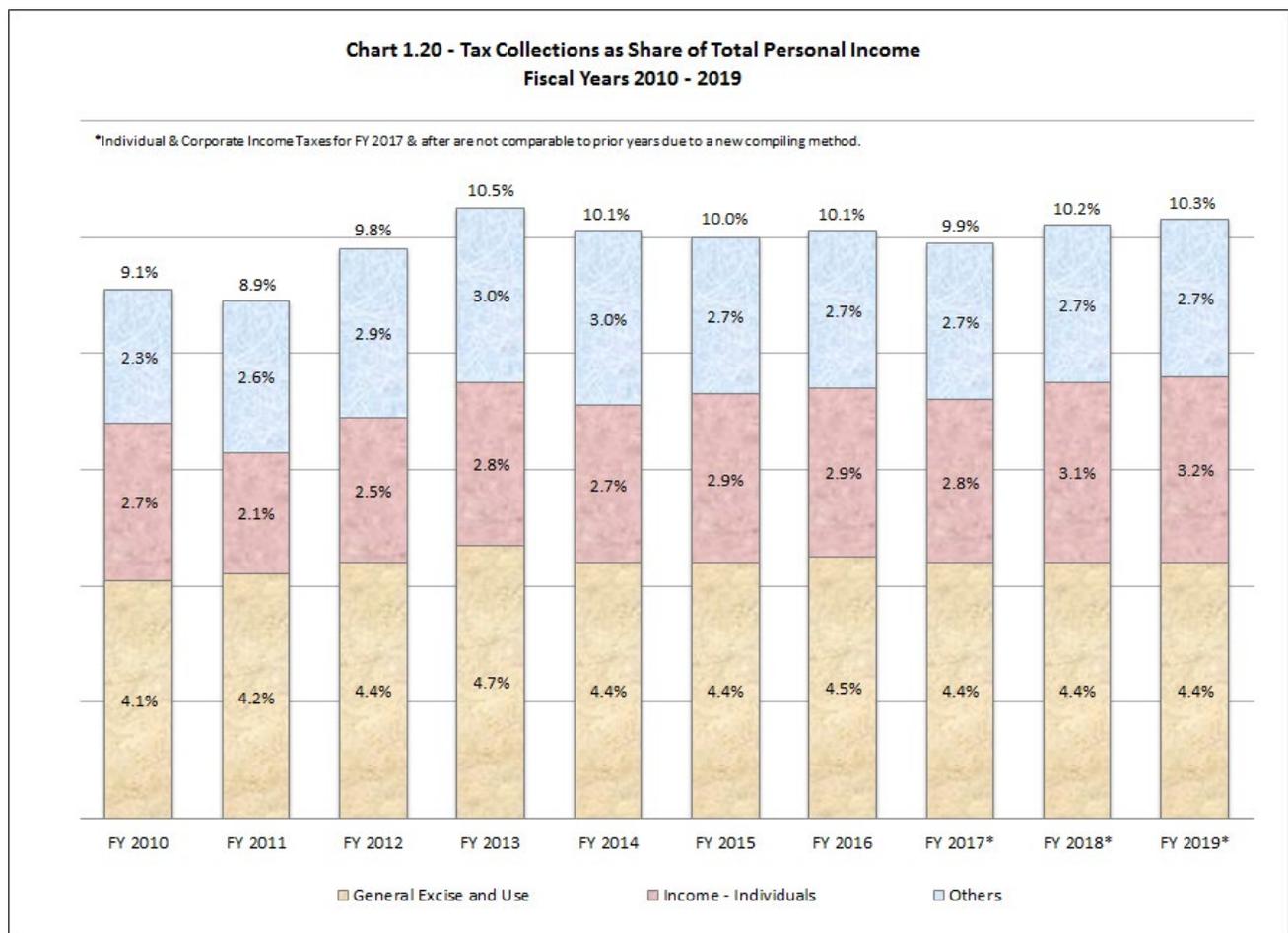
	FY 2019		FY 2018	
	Amount Distributed	% of Total	Amount Distributed	% of Total
<u>STATE FUND</u>				
State General Fund	\$ 7,141,790	86.31	\$ 6,796,036	86.07
State Highway Fund	279,505	3.38	276,727	3.50
State Airport Fund	2,605	0.03	2,632	0.03
Boating Special Fund	1,758	0.02	1,722	0.02
Environmental Fund	1,339	0.02	1,291	0.02
Cigarette Stamp Admin/Enf. Fund	1,766	0.02	1,892	0.02
Compliance Resolution Fund	2,000	0.02	2,000	0.03
Unemployment Trust Fund	110,309	1.33	110,885	1.40
Election Campaign Fund	146	0.00	195	0.00
Tourism Special Fund	79,000	0.95	82,000	1.04
Rental Housing Fund	38,000	0.46	38,000	0.48
Convention Center Fund	16,500	0.20	26,500	0.34
Public Libraries Fund	138	0.00	75	0.00
School Repairs & Maintenance Fund	71	0.00	80	0.00
Land Conservation Fund	6,800	0.08	6,800	0.09
Domestic Violence\Child Abuse Neglect Fund	147	0.00	170	0.00
Cancer Research Fund	12,993	0.16	13,917	0.18
Trauma System Fund	6,989	0.08	7,400	0.09
Emergency Medical Service Fund	8,122	0.10	8,700	0.11
Community Health Centers Fund	8,122	0.10	8,700	0.11
Energy Security Fund	4,016	0.05	3,872	0.05
Energy Systems Development Fund	2,677	0.03	2,582	0.03
Agricultural Development & Food Security Fund	4,016	0.05	3,872	0.05
Land and Development Fund	3,000	0.04	3,000	0.04
Turtle Bay Conservation Easement Fund	1,500	0.02	1,500	0.02
Mass Transit Special Fund	57,354	0.69	23,626	0.30
Subtotal - State	\$ 7,790,663	94.15	\$ 7,424,174	94.03
<u>COUNTY SURCHARGE *</u>	\$ 290,719	3.51	\$ 281,589	3.57
<u>REVENUES TRANSFERRED TO COUNTIES</u>				
Other County Revenues				
Fuel Tax	\$ 90,643	1.10	\$ 86,946	1.10
Trans. Accom. Tax	103,000	1.24	103,000	1.30
Subtotal - Counties	\$ 193,643	2.34	\$ 189,946	2.41
TOTAL	\$ 8,275,024	100.00	\$ 7,895,708	100.00

*Includes the new surcharges imposed by the County of Hawaii and by the County of Kauai, starting in January 2019.
NOTE: Due to rounding, details may not add to totals.

1.19 TRENDS IN TAX COLLECTIONS

The overall ratio of State tax obligation to total personal income has remained relatively stagnant. Table 1.11 provides data on total tax collections for FY 2010 through FY 2019. Chart 1.20 shows total tax collections relative to total personal income (TPI) in the State for FY 2010 through FY 2019.⁴

Article VII, Section 9 of the 1978 Hawaii State Constitution imposes a ceiling on appropriations from the General Fund, exclusive of federal funds: the appropriations are not allowed to grow faster than the estimated growth in total personal income. The ceiling is based on the ceiling in the prior year.



⁴ The chart uses the most recent figures from the Bureau of Economic Analysis (BEA) for TPI. The Bureau periodically updates TPI figures and the updates often extend back for a number of years.

TABLE 1.11 - HISTORICAL COLLECTIONS FOR SELECTED TAXES
(In Thousands of Dollars)

SOURCE OF REVENUE	Fiscal Year				
	2010	2011	2012	2013	2014
General Excise and Use	\$2,316,434	\$2,495,807	\$2,697,951	\$2,944,487	\$2,880,541
Income - Individuals	1,528,110	1,247,153	1,541,051	1,736,007	1,745,810
Transient Accom. Tax & Fees	224,252	284,472	323,951	368,576	395,242
Unemployment Insurance	82,017	190,511	231,669	262,290	264,178
Motor Vehicle Tax ¹	102,319	106,166	211,742	176,295	168,726
Fuel and Environmental ⁴	155,703	195,336	193,101	193,949	193,550
Public Service Companies	157,661	117,940	150,528	163,930	166,179
Tobacco and Licenses	123,489	143,293	138,798	127,881	121,742
Insurance Premiums ²	104,721	140,456	117,617	131,906	137,179
Income - Corporations	59,186	34,573	73,026	100,988	87,021
Liquor and Permits	44,074	48,054	48,854	48,962	48,305
Conveyance	40,634	47,906	42,106	54,686	75,831
Banks - Financial Corporations	20,666	33,677	7,229	22,673	38,983
Total Collections ³	\$5,134,807	\$5,292,193	\$6,004,268	\$6,541,300	\$6,581,424

SOURCE OF REVENUE	Fiscal Year				
	2015	2016	2017 ⁵	2018 ⁵	2019 ⁵
General Excise and Use	\$3,048,207	\$3,206,154	\$3,239,225	\$3,395,566	\$3,541,389
Income - Individuals	1,988,194	2,116,859	2,095,898	2,430,356	2,568,616
Transient Accom. Tax & Fees	420,981	446,794	508,377	554,912	600,334
Unemployment Insurance	167,248	128,577	104,313	110,885	110,309
Motor Vehicle Tax ¹	180,755	187,704	186,490	193,241	196,120
Fuel and Environmental ⁴	193,082	198,136	194,761	201,778	206,345
Public Service Companies	163,481	152,760	122,159	117,641	126,691
Tobacco and Licenses	129,851	125,093	124,066	120,522	112,518
Insurance Premiums ²	145,679	153,173	164,688	159,814	173,844
Income - Corporations	52,319	93,036	173,666	131,119	163,676
Liquor and Permits	50,281	50,590	51,167	51,383	51,913
Conveyance	78,702	66,083	94,537	100,603	85,965
Banks - Financial Corporations	19,930	14,691	11,174	15,712	26,808
Total Collections ³	\$6,900,042	\$7,249,205	\$7,338,382	\$7,895,708	\$8,275,024

¹ Includes State Motor Vehicle Weight Tax, Registration Fees, Commercial Driver's License, Periodic Motor Vehicle Inspection Fees, Rental Motor Vehicle, Tour Vehicle and Car-Sharing Vehicle Registration Fees, and Rental Motor Vehicle, Tour Vehicle and Car-Sharing Vehicle Surcharge Tax.

² Excludes Insurance Fees allocated to the General Fund, which were included in previous reports.

³ Includes the Inheritance and Estate Tax, the County Surcharge, fuel permits, interest and penalties on fuel taxes, general excise fees, and permitted transfers tax.

⁴ Fuel tax collections were \$198,404 thousand for fiscal year 2016. Of the collections, \$268 thousand could not be distributed because the corresponding tax returns were not yet available. Fuel tax collections were \$195,151 thousand for fiscal year 2017. Of the collections, \$390 thousand could not be distributed because the corresponding tax returns were not yet available. Fuel tax collections were \$201,303 thousand for fiscal year 2018. A total of \$475 thousand in undistributed fuel tax from previous years were included in several monthly reports in fiscal year 2018. Fuel tax collections were \$206,162 thousand for fiscal year 2019. A total of \$183 thousand in undistributed fuel tax from previous years were included in several monthly reports in fiscal year 2019.

⁵ Individual and Corporate Income Taxes for FY 2017 & after are not comparable to prior years due to a new compiling method.

2.0 TAX ADMINISTRATION

2.1 OVERALL PERFORMANCE

DOTAX consists of two (2) divisions, seven (7) staff offices, a Public Information Officer, and a Taxpayer Advocate. The two divisions are the Tax Services and Processing Division and the Compliance Division. The seven staff offices are the Administrative Services Office, the Rules Office, the Tax Research and Planning Office, the Information Technology Services Office, the Technical Services Office, the Administrative Appeals Office, and the Tax Practitioner Priority Office. The total number of permanent, civil service staff in DOTAX was 339 in FY 2019.

In FY 2019, DOTAX's operating expenses were \$25.5 million, up from \$23.7 million in FY 2018. DOTAX collected \$7.87 billion in taxes in FY 2019, so the **cost of collecting each \$100 dollars of taxes was about 32 cents**.

DOTAX continues to encourage taxpayers to use electronic transmissions rather than paper returns. There has been a significant increase in electronic filing of tax returns and payments, of the 5.1 million returns processed in the fiscal year 57% were processed electronically. In April 2019, DOTAX started using its mandatory e-filing authority (HRS 231-8.5). **All legally authorized mandatory e-filing requirements will be in effect by July 2020.**

2.2 TAX SERVICES AND PROCESSING DIVISION

2.2.1. Overview

The Tax Services and Processing Division (TSP) is comprised of three branches: Taxpayer Services, Document Processing, and Revenue Accounting. Aside from providing various services to both individual and business taxpayers, the Taxpayer Services Branch (TPS) performs functions relating to licensing and taxpayer account management. The Document Processing Branch (DP) manages the receiving, editing and centralized processing of tax information and processes payments received from both paper and electronic filings, and is further responsible for securing and depositing tax payments. The Revenue Accounting Branch (RA) maintains revenue control and reconciliation functions for all State tax revenues. RA is also responsible for the preparation of various revenue related reports, such as the monthly Preliminary Report (on revenues collected) and the Statement of Tax Operations (STO).

In FY19, **65% of all general excise and transient accommodation taxpayers used HTO for filing returns**. This is an increase of 15% over FY18. HTO offers efficiencies for both the taxpayer and the Tax Services and Processing Division.

2.2.2 Taxpayer Services Branch

The Taxpayer Services (TPS) Branch is made up of three main sections:

1. Customer Inquiry – provides information and taxpayer assistance pertaining to all taxes administered by DOTAX

2. Account Management – performs computer-based error correction activities to allow expedient processing, posting, and updating of tax returns and payments
3. Licensing – processes, issues, and updates all licenses and permits issued by DOTAX

Customer Inquiry

Customer Inquiry provides taxpayer assistance by phone and at the windows. **The volume of incoming calls and walk-in taxpayers decreased in FY2019.**

Total Incoming Calls include those calls handled by the interactive voice recognition system and attendants (staff) in the call center. Total Calls to Attendants is the number of callers attempting to talk to an attendant. Total Answer Rate is the percentage of calls requesting to speak to a person.

While the volume of incoming calls has decreased, the **number of calls answered has increased:**

FY	Total Incoming Calls	Total Calls To Attendants	Total Calls Answered	Answer Rate
2019	270,290	170,168	127,092	75%
2018	346,644	158,414	116,697	74%
2017	671,606	131,299	90,786	69%

The number of taxpayers walking into the Punchbowl office also decreased in FY 2019. The average number of taxpayers served each month by fiscal year is as follows:

<u>FY</u>	<u># of Taxpayers</u>
2019	3,631
2018	4,193
2017	4,529
2016	3,582
2015	3,558

Account Management

The primary function of Account Management is to review, analyze, and correct errors or other inconsistencies on returns and payments. These inconsistencies were identified by our computer system during processing and placed on a work list for manual review.

In FY 2019, the team **reviewed and posted 209,319 returns, payments, and other documents** to the system that the system was initially unable to process. **Corrections have decreased by 25%** this year. The table below reflects monthly average postings of documents work-listed since FY 2015:

<u>FY</u>	<u># of Postings</u>
2019	17,444
2018	23,843
2017	22,135
2016	18,162

Licensing

The Licensing Section process business license applications and renewals. In FY2019, 41,232 business license applications were processed, compared to 37,978 applications the previous fiscal year. 29,853 or 72% of the applications were filed online versus 65% in FY 2018. Taxpayers are using DOTAX's online business license application options: Hawaii Business Express (7%), and HTO (93%).

The Section also processed 2,350 cancellations, a 50% decrease from FY 2018, which was inflated due to the clean-up preparing for the TSM rollouts.

2.2.3 Document Processing Branch

The main function of the Document Processing Branch (DP) is to accurately and efficiently process all tax returns and documents; to receive, secure, deposit, and account for tax payments; to ensure proper electronic storage and retrieval of documents; and to perform various functions relating to electronic filing. DP is comprised of six sections: Receiving and Sorting, Data Preparation, Imaging and Data Entry, Monetary Control, File Maintenance, and Electronic Processing.

Although there has been an increase in electronic filing of tax returns and payments, **over 2.17 million paper tax returns and other documents were manually processed** by DP.

For FY 2019, there were 2,173,814 (43%) paper tax returns, and 2,922,117 (57%) electronic tax returns processed. There was over \$8.39 billion in tax-related payments received, an increase of nearly \$500 million from FY 2018. 95% of the payments were processed in 7 days or less.

2.2.4 Revenue Accounting Branch

The main function of the Revenue Accounting Branch (RA) is to maintain accounting records for all tax revenues, refunds and adjustments, district transfers and closing adjustments, and preparation of all Journal Vouchers and Summary Warrant Vouchers. RA is also responsible for error resolution, reconciliation and reporting functions for all State tax revenues. Specific tasks include the preparation of the Daily Cash Collection Report (Oahu District), the Preliminary Report, the Statement of Tax Operations (STO).

The monthly Preliminary Report, which is released by the fifth working day of each month, is a summary of all revenues received by DOTAX, less the amount of tax refunds paid. The STO is a formal, detailed report of State revenues that is based on the Preliminary Report and is prepared by the tenth working day of each month. The RA Branch has consistently and diligently met the critical deadlines for these reports throughout this fiscal year, as well as in past years.

The RA Branch also performs manual accounting activities for all miscellaneous tax collections (with the exception of the estate and transfer tax), prepares journal entries associated with the various administratively-established trust accounts and for other legislatively mandated purposes,

maintains the manual accounting system for all protested payments and tax appeals, provides allocation reports to the Department of Accounting & General Services (DAGS) and the Department of Budget & Finance (B&F), accounts for all tax refunds, and handles all refund exception activities, such as returned checks, tracers, or forgeries.

2.3 COMPLIANCE DIVISION

2.3.1 Overview

The objective of the Compliance Division is to maximize taxpayer compliance with Hawaii's tax laws in a consistent, uniform, and efficient manner. The Compliance Division is composed of the Oahu Office Audit Branch, the Oahu Field Audit Branch, the Oahu Collections Branch, and the Maui, Hawaii, and Kauai District Tax Offices. In addition to these branches, there are also the Criminal Investigation Section (CIS), Special Enforcement Section (SES), and the Tax Fraud Unit (TFU). The Division has the following three programs to meet the objectives of the voluntary compliance, self-assessment tax system: (1) auditing/examination, (2) collection, and (3) taxpayer services (information dissemination).

In FY19, both the Office Audit Branch and Field Audit Branch increased assessments by 16.5% (see Section 2.3.2, Chart 2.8, and Table 2.1) and 14.5% (see Section 2.3.5) respectively. The Criminal Investigation Section recovered \$4.8 million in restitution, assessments, penalties, and interest (see Section 2.3.8). \$8.5 million in impact revenue was collected from taxpayers resulting from the efforts of the Special Enforcement Section (see Section 2.3.9).

2.3.2 Office Audit Branch

The Office Audit Branch performed examinations to enhance voluntary compliance. In FY 2019, the Office Audit Branch completed **24,326 cases**, an increase of 40.2% (6,970 cases) compared to FY 2018. The **total dollars assessed was \$87.3 million**, an increase of 16.5% (\$12.3 million) compared to FY 2018. In FY 2019, the Office Audit Branch processed the Estate and Transfer Tax returns and collected \$4.3 million for estate tax returns. Charts 2.7 and 2.8 (on the following page) show the number of audits completed and the dollars assessed by Office Audit for FY 2008 through FY 2019.

2.3.3 Field Audit Branch

The Field Audit Branch utilizes auditing procedures to enhance voluntary compliance. In FY 2019, the number of audits completed by Field Audit Branch was **164 cases**, an increase of 3.1% (5 cases) compared to FY 2018. Total dollars assessed was **\$45.3 million**, an increase of 14.5% (\$5.7 million). Charts 2.9 and 2.10 show the number of audits completed and the dollars assessed by Field Audit for FY 2008 through FY 2019.

Chart 2.7 - Office Audit: Number of Completed Audits

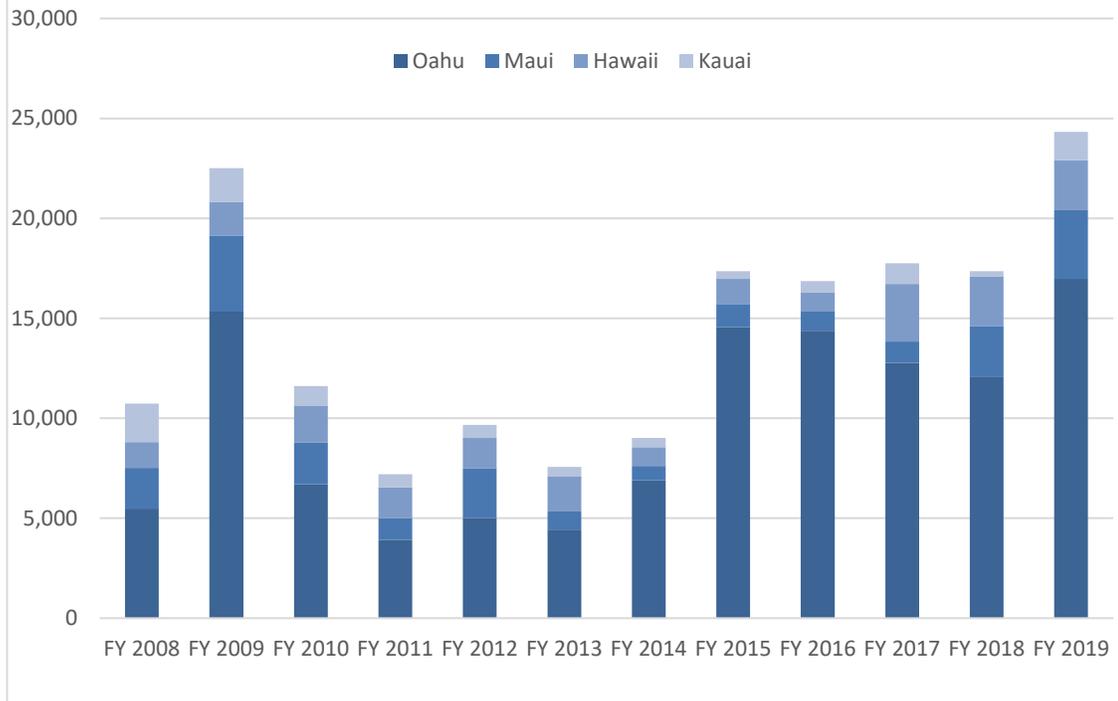
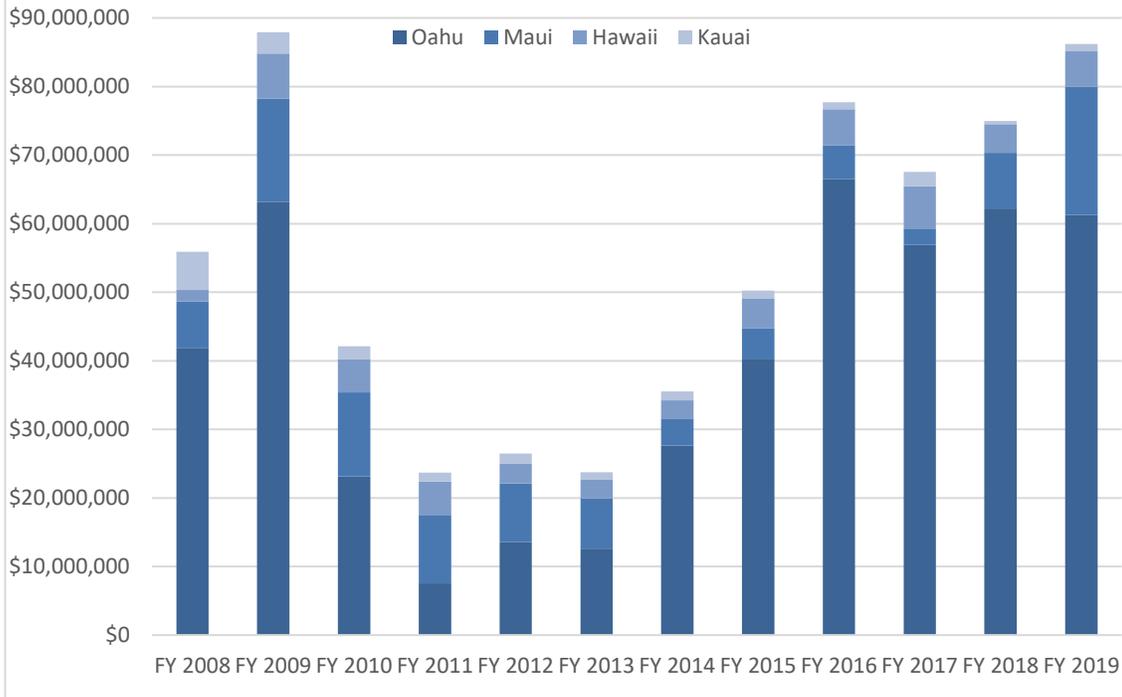
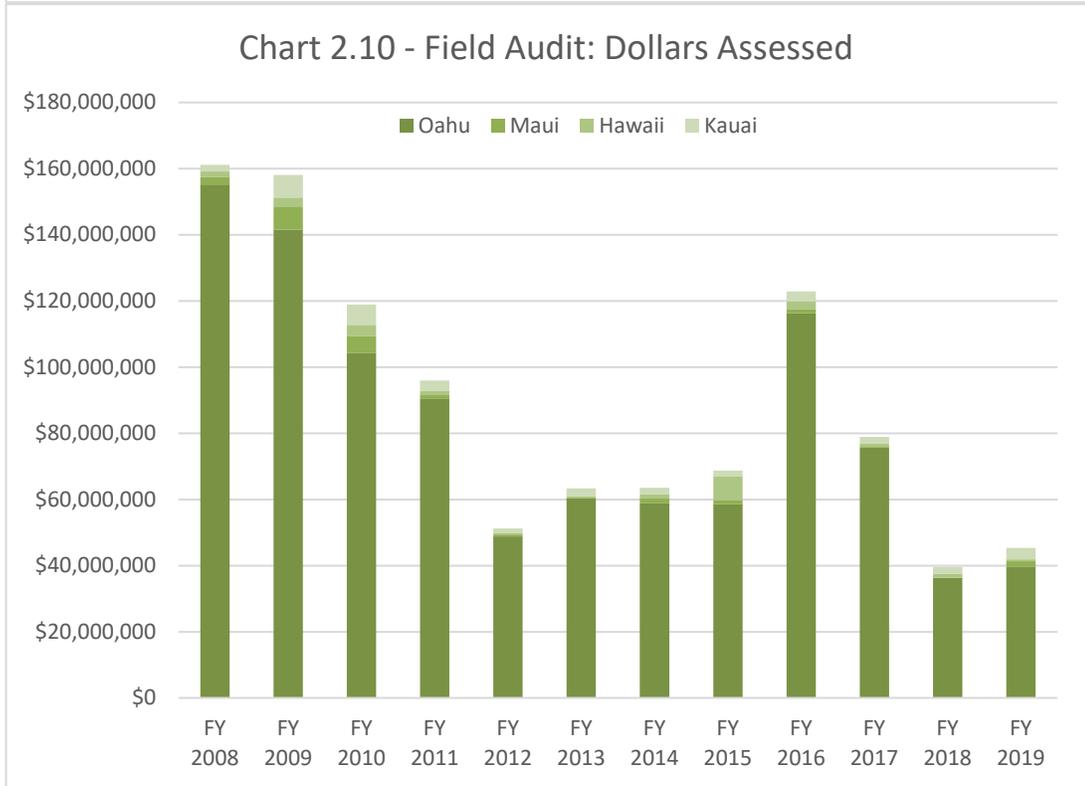
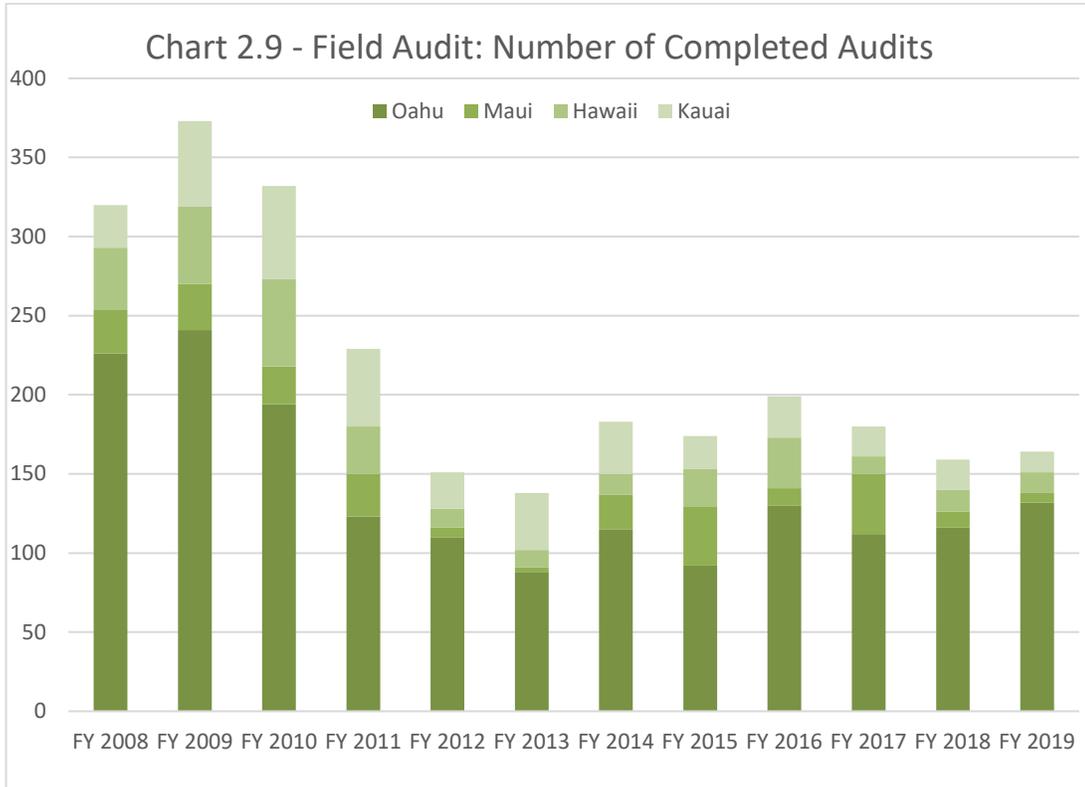


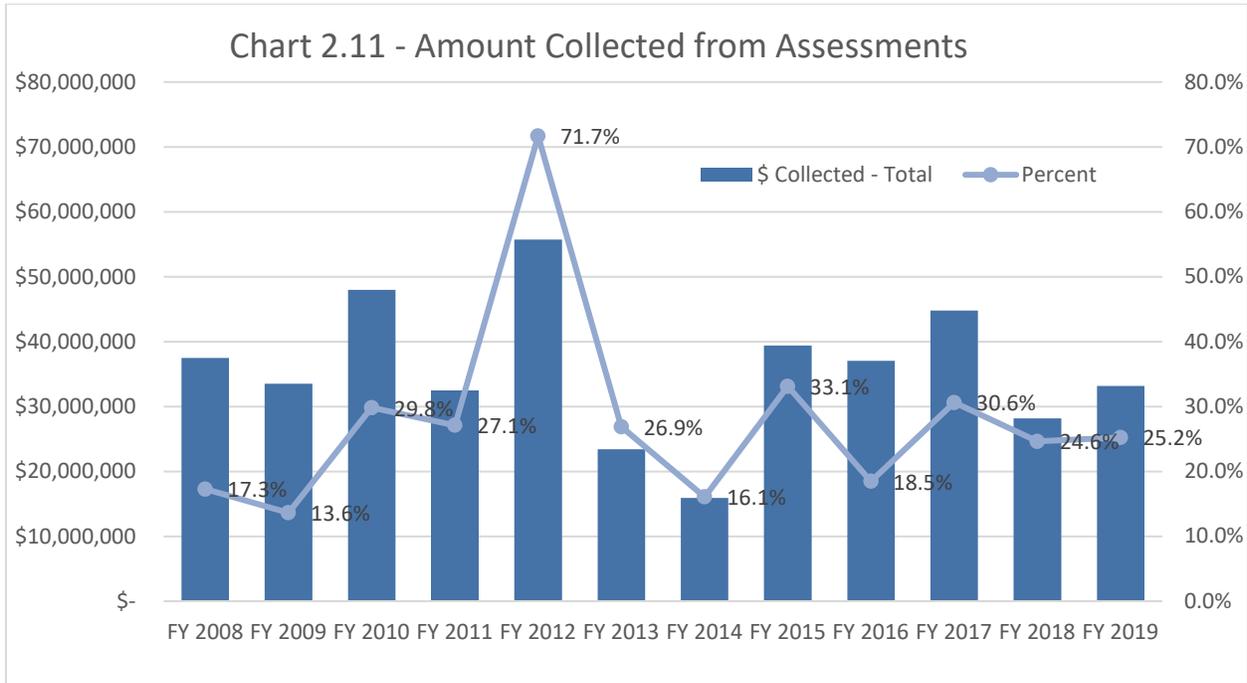
Chart 2.8 - Office Audit: Dollars Assessed





2.3.4 Revenue - Office and Field Audit Assessment Recoveries

The amount collected at the time the audits were closed and prior to the mailing of any billing notices increased from \$28.2 million in FY 2018 to **\$33.2 million in FY 2019**.⁵



⁵ The amounts assessed are the assessments generated during FY 2018. The amounts collected during FY 2018 may include assessments and settlements from prior fiscal years.

TABLE 2.1 - AMOUNTS ASSESSED FOR FY 2019

	OFFICE AUDIT		FIELD AUDIT	
	# of Audits	Dollars Assessed	# of Audits	Dollars Assessed
Oahu	16,980	\$61,271,630	132	\$39,530,051
Maui	3,440	\$18,727,070	**	\$1,766,263
Hawaii	2,496	\$5,130,311	13	\$545,962
Kauai	1,410	\$2,213,066	13	\$3,458,388
Total FY 2019	24,326	\$87,342,077	164	\$45,300,664
Total FY 2018	17,356	\$74,957,716	159	\$39,564,719

2.3.5 Special Projects

OAHU DISTRICT

Office Audit Branch conducted the following special projects during the fiscal year:

- Non-Filers: The examination of tax returns resulted in \$33.8 million in assessments and adjustments.
- Special Enforcement, Fraud, & Criminal Sections: The examination of tax accounts inclusive of correspondence, review of tax information and preparation of assessments resulted in \$6.7 million in assessments and adjustments.
- Supplemental Audit Scope: Examination of unreported and under-reported income pertaining to general income tax, net income taxes, reduction of Hawaii Real Property Tax Act (HARPTA) refunds claimed and transient accommodations taxes all of which amounted to \$5.4 million.

Field Audit Branch conducted the following special projects during the fiscal year:

- Federal Contractors Project: This project, which targets unlicensed contractors working on federal installations, was started in 1983 and is an ongoing activity. This fiscal year, one audit was completed and resulted in \$1,289,000 in assessments.
- Referral Cases from Criminal Investigation Unit: During this fiscal year, two cases that were either originally considered for possible criminal prosecution or arose pursuant to a criminal investigation were completed, resulting in \$14,000 in assessments.
- Renewable Energy Tax Credit: During this fiscal year, two audit cases involving the renewable energy tax credit were completed resulting in \$506,000 in assessments.
- Other Refund Projects: During this fiscal year, four audit cases involving other refunds were completed resulting in \$4,665,000 in assessments.
- Multistate Tax Commission audits: During this fiscal year, 15 audit cases examined by the MTC were followed through for Hawaii tax adjustments resulting in \$2,154,000 in assessments.

MAUI DISTRICT

Office Audit Section conducted the following special projects during the fiscal year:

- HARPTA Reviews: Maui Office Audit examined 792 HARPTA exemption claims with total selling prices of \$250,404,400, which resulted in 58 disapproved HARPTA exemption claims with total selling prices of \$1,724,000.
- Non-filers: The examinations in this area resulted in \$5.1 million in assessments and adjustments.

Field Audit Section conducted the following special project during the fiscal year:

- Renewable Energy Technologies Income Tax Credits: Maui Field Audit reviewed renewable energy income tax credits claimed in the amount of \$500,000 which resulted in the disallowance of credits in the amount of \$0.
- HARPTA Reviews: Maui Field Audit examined 2 HARPTA/capital gains case with a total selling price of \$9,525,000 which resulted in no assessment or adjustment.
- Selected General Excise Tax Exemptions: Maui Field Audit Section audited and disallowed \$5,195,500 in exemptions claimed.

HAWAII DISTRICT

Office Audit Section conducted the following special projects during the fiscal year:

- Enterprise Zone and Qualified High Technology Business Tax Credit: The examinations resulted in \$177,330 in assessments and adjustments.
- HARPTA Reviews: The examinations resulted in \$243,169 in assessments and adjustments of net income, general excise, and transient accommodations taxes.
- Non-Filers: The examinations in this area resulted in \$3.0 million in assessments and adjustments.

Field Audit Section conducted the following special projects during the fiscal year:

- Renewable Energy Technologies Income Tax Credit: The review of tax credits claimed resulted in \$122,650 in assessments and adjustments.
- HARPTA Reviews: Hawaii Field Audit reviewed HARPTA/capital gain cases, which resulted in assessments and adjustments of \$51,114.

KAUAI DISTRICT

Field Audit Section conducted the following special projects during the fiscal year:

- Renewable Energy Technologies Income Tax credits: Kauai Field Audit reviewed renewable energy income tax credits in the amount of \$5,894,105.
- HARPTA Reviews: Kauai Field Audit reviewed HARPTA cases resulting in an adjustment of \$23,417.

2.3.6 Taxpayer Assistance Provided

On neighbor islands, personnel helped taxpayers properly file numerous tax returns and other documents over the telephone, at the service counter, and by mail. The Oahu Office Audit, Field Audit, and Collection units also provided support services to the neighbor island district tax offices and to the Oahu Taxpayer Services Branch when requested. Table 2.2 summarizes the number of times that taxpayer assistance was provided by the Maui, Hawaii, and Kauai District Tax Offices.

TABLE 2.2 - TAXPAYER ASSISTANCE PROVIDED BY MAUI, HAWAII AND KAUAI DISTRICT OFFICE

	FY2019	FY2018	Difference	
			Number	Percentage
Counter	71,995	67,764	4,231	6.2%
Phone Services	46,712	46,504	208	0.4%
Tax Clearances	4,545	3,619	926	25.6%
Correspondence	16,264	21,189	(4,925)	(23.2%)

The taxpayer services sections in the districts provide telephone and counter services, supplementing the centralized customer services provided by the Oahu TSP Division. The districts continue to receive a steady flow of telephone inquiries and can use the statewide tax data system to assist with any tax inquiry.

Compliance Division’s continues to emphasize taxpayer education and problem resolution. The Compliance Division believes that it is important to maintain taxpayers’ willingness to accurately and voluntarily comply with the State’s tax laws.

In addition, the neighbor island districts participated in the following activities:

MAUI DISTRICT

- Met with the Department of Education, local farmers, and vendors regarding compliance information and tax clearance procedures.

HAWAII DISTRICT

- 2018 Puna Lava Disaster Relief program at Kea'au High School on June 15, 2018 through July 13, 2018 assisted taxpayers affected by the lava with their tax matters.
- Met with the Department of Education, local farmers, and vendors regarding compliance information and tax clearance procedures.

KAUAI DISTRICT

- 2018 Kauai Flood Disaster Relief program held at Hanalei School on July 1, 2018 through July 8, 2018 assisted taxpayers affected by the flood with their tax matters.
- Met with the Department of Education, local farmers, and vendors regarding compliance information and tax clearance procedures.

- Q&A with the Contractor's Board and a group of licensed Contractors regarding the new Kauai County Surcharge, the exemptions for contracts entered into before June 30, 2018, and instruction for the new GE forms.

2.3.7 Collection Branch

The Compliance Division’s Tax Collections program consists of the Oahu collection branch and the collection sections in the Maui, Hawaii, and Kauai District Tax Offices. There were 63,992 collection cases in FY 2019 compared to 59,831 cases in FY 2018. The Oahu collection branch accounted for 74% of the statewide delinquent tax collections in FY 2019.

Chart 2.12 shows delinquent collections for FY 2008 through FY 2019. For comparison, Table 2.3 shows major performance measures for FY 2019 and FY 2018, including penalty and interest on outstanding tax delinquencies.

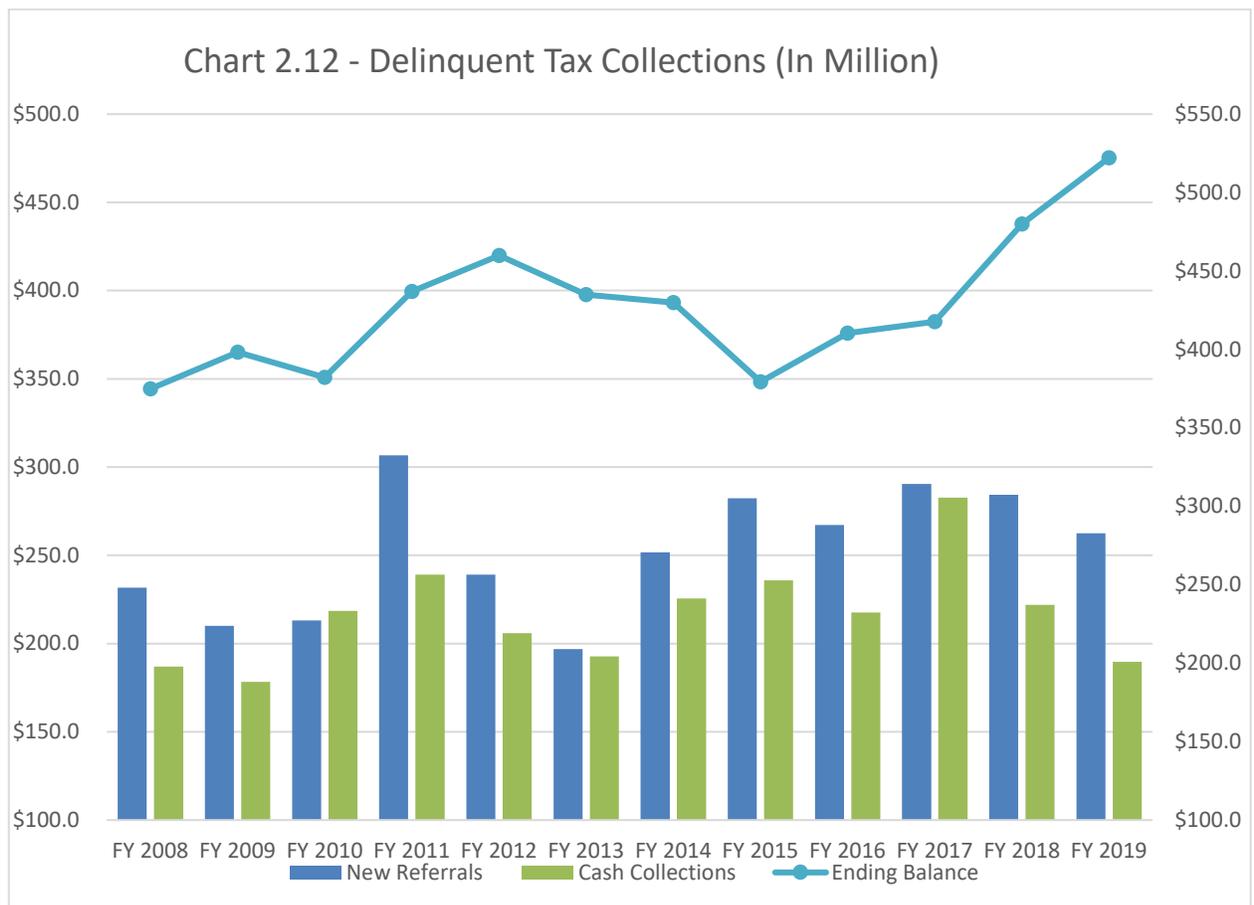


TABLE 2.3 - MAJOR PERFORMANCE MEASURES FOR FY 2019 AND FY 2018

Measure	FY 2019	FY 2018	Difference	
			Amount	Percentage
Starting Delinquent Balance	\$971.4	\$846.3	\$125.1	12.9%
Delinquent Taxes (\$ Millions)	\$ 516.1	\$ 480.0	\$ 36.1	7.5%
Delinquent Penalties, Interest, Other (\$	\$ 521.5	\$ 482.5	\$ 39.0	8.0%
Ending Delinquent Balance	\$1037.6	\$971.4	\$66.2	6.4%
Total New Delinquent Referrals (\$ Millions)	\$ 270.1	\$ 284.4	\$ (14.3)	(5.0%)
Total Cash Collected (\$ Millions)	\$ 191.3	\$ 222.0	\$ (30.7)	(13.8%)
Uncollectible Tax Write-Offs (\$ Millions)	\$ 21.8	\$ 0.2	\$ 21.6	10,800%
Payment Plan Initiated	19,822	20,997	(1,175)	(5.6%)
Tax Liens Filed	1,879	1,720	159	9.2%
Levies Served	15,596	14,769	827	5.6%

2.3.8 Criminal Investigation Section

During FY 2019, the Criminal Investigation Section (CIS) conducted forty-four (44) criminal tax investigations into entities with legitimate sources of income, as well into individuals and criminal groups involved in illegal activities, such as narcotics trafficking, gambling, prostitution, and other related financial frauds.

CIS continues to work with the U.S. Attorney's Office and the Federal Bureau of Investigation (FBI) for assistance, review and federal prosecutions of some of their investigations. During FY 2019, the State of Hawaii, Department of Attorney General prosecuted five (5) individuals and eight (8) businesses for felony and misdemeanor tax violations. The individuals involved were allowed to self-surrender and/or were arrested by CIS Special Agents. There are nine (9) business entities and three (3) individuals in process at the Department of Attorney General, with recommended felony and misdemeanor tax violations. The successful adjudication will yield an anticipated \$573,900 in restitution and \$1,004,325 in additional civil assessments for FY 2020.

Completed investigations not referred for criminal prosecution were turned over to the appropriate Oahu Office Audit Branch, Field Audit Branch or District Offices for further civil examination. In FY 2019, 273 referrals were made to the Oahu Office Audit Branch resulting in \$2,910,495 in additional assessments. The Maui, Hawaii and Kauai District Offices made \$19,455 in additional assessments for CIS.

These assessments were mutually exclusive to those made in prior years' adjudicated criminal cases. An additional \$1,813,796 in criminal collections and secured returns were made in FY 2019. It is estimated that CIS investigative efforts will have yielded approximately \$4.7 million in restitution, assessments, penalties and interest that would have otherwise not been realized by

the State of Hawaii.

2.3.9 Special Enforcement Section

The Special Enforcement Section (SES) was established in 2009, through the *Cash Economy Enforcement Act*. Its goal is to ensure that all sectors of Hawaii's economy, especially those that conduct a significant portion of business transactions in cash ("cash economy"), pay their fair share of taxes. In FY 2016, SES was given additional responsibilities for ensuring that short-term vacation rental operators comply with the state's transient accommodations tax laws.

The SES has broad legal authority to conduct civil investigations of suspected violations of tax laws. It conducts complex financial investigations to determine correct income subject to tax by securing and examining books, records and other corroborating evidence. It executes a wide range of activities, including investigating complaints, developing leads through various sources, obtaining evidence, securing delinquent and amended tax returns and payments from taxpayers, conducting site visits, inspections, surveys, and training sessions at various events, business locations and short-term rental sites throughout the state for the purpose of educating the public and business operators about their tax obligations and verifying tax compliance.

In FY 2019, SES pursued additional leads discovered through a 2018 project that utilized publicly available and confidential database sources that identified taxpayers who were potentially not compliant with transient accommodations and general excise tax laws. The project utilized new resources made available by TSM to evaluate large amounts of data. The project yielded about \$2.4 million in additional TAT and related GET collections during the year and is expected to continue providing substantial additional tax collections in FY 2020.

SES continues to bring positive change by educating and bringing taxpayers into compliance and in collecting tax revenues. SES measures its accomplishments by determining the actual tax collections that were remitted by taxpayers on delinquent returns secured by SES. In addition, as taxpayers brought into tax compliance by SES were largely non-filers, who would have likely remained non-compliant indefinitely, the potential impact on future tax revenues was substantial. The potential tax revenues were based on tax collections remitted by taxpayers for a post compliance period of 18 months after they were brought into tax compliance. Delinquent period tax collections and post compliance period collections aggregate to Impact Revenue. Accordingly, SES Total Impact Revenue grew to \$8,549,112 in FY 2019, as compared with \$7,973,436 in FY 2018, \$5,268,362 in FY 2017, and \$3,505,618 in FY 2016. Additional details of SES's accomplishments are as follows:

	FY 2019	FY 2018	FY 2017
Complaints Received	328	419	307
Businesses Educated on Compliance of Tax Laws	1,561	2,359	1,331
Number of Events Visited Throughout the State	147	46	25
GET Impact Revenue Collected	\$6,183,255	\$5,754,966	\$4,242,496
TAT Impact Revenue Collected	\$2,365,857	\$2,218,470	\$1,025,866
Total Impact Revenue Collected from Taxpayers	\$8,549,112	\$7,973,436	\$5,268,362
Total Tax Collected from Secured Delinquent Returns	\$4,255,748	\$3,867,116	\$2,528,814

2.3.10 Tax Fraud Unit (Ad Hoc)

The Tax Fraud Unit (TFU) was created in 2013 to combat abusive tax promotions resulting from identity theft and other related tax frauds. Tax fraud promoters and return preparers have grown increasingly bold and sophisticated, utilizing the internet to instantaneously gain access to a wide audience base, causing various tax schemes and scams to grow at a phenomenal rate.

The TFU researches, develops and identifies both investigative and audit leads for Criminal Investigation, Field and Office Audit Sections. Utilizing complex manual and advanced automated tools and compliance checks, including Tax System Modernization (TSM) data and the related Fraud Manager program, TFU is also responsible for detecting, investigating and stopping fraudulent refunds. With in-depth, technical analyses relating to Criminal and Fraud investigations, as well as Civil Audit operations TFU coordinates with the impacted sections.

In 2019, the TSM Fraud Manager **captured approximately 3,000 alleged fraudulent refund claims**, totaling in excess of \$4.7 million. Approximately 2,400 of these fraudulent refunds were associated with inflated Schedule C loss returns, where the alleged fraudulent business losses were used to off-set wages, leading to increased refund requests. The Schedule C fraudulent refund claims totaled in excess of \$3.5 million.

Other TFU focus areas include questionable tax return schemes, detected through communications from electronic return originators, financial institutions, return preparers and/or concerned citizens.

The following are the fraud unit results for fiscal year ending 2017, 2018 and 2019:

FY	Fraudulent	
	Returns Stopped	Amount
2017	277	\$1,304,420
2018	230	\$547,956
2019	651	\$1,871,519

2.3.13 Voluntary Disclosure Program

Pursuant to Tax Information Release No. 2016-02 Re: Voluntary Disclosure Practice, Compliance Division reviewed 86 cases which resulted in revenue of \$5.5 million through the program.

2.4 STAFF OFFICES

2.4.1 Administrative Services Office

The Administrative Services Office submitted the biennium budget for FY 2020 and FY 2021 to the 2019 Legislature. The Legislature appropriated \$36.7 million for FY 2020 for operating expenses. For FY 2019, \$31 million was appropriated for DOTAX. In discharging its duties and responsibilities, the incurred operating expenses of \$25.8 million for the year. The DOTAX collected \$7.87 billion in net tax revenues in FY 2019, so the cost to collect \$100.00 of taxes was \$0.33.

2.4.1.2 Personnel Management

In FY 2019 the Personnel Department's focused on filling vacancies, outside recruitment, internal promotions and retention programs. Personnel staff also participated in the development of the new payroll system, reviewing and organizing files to transition into the new payroll system. At the end of FY 19, 344 of the permanent positions were filled. During that fiscal year, DOTAX's total vacancy rate for permanent positions increased by 6 positions or 11%.

2.4.2 Rules Office

The Rules Office is comprised of the Rules staff and the Technical Section. The function of the Rules Office is to serve as a resource for complex policy recommendations and internal support. The Rules Office also assists in DOTAX's implementation of new legislation and in creating and maintaining the tax forms, form instructions, and publications.

2.4.2.1 Rules Staff

The Rules staff serves as DOTAX's internal advisory arm to the Director of Taxation on tax policy and advises the Director's Office and DOTAX on legislative and tax policy issues. The Rules staff provided training for personnel and did presentations at the DOTAX's annual workshops for tax practitioners. Litigation and other external legal matters are handled exclusively by the Tax & Charities Division of the Department of the Attorney General.

In addition, the Rules staff assists, counsels, and represents DOTAX's compliance personnel with tax disputes and other administrative tax controversies. The Rules staff also assisted the Tax & Charities Division of the Department of the Attorney General with the judicial tax appeals and provided support to the Department's Tax System Modernization project.

For the 2019 legislative session, the Rules staff drafted and submitted nine bills that were introduced as part of the Administration's legislative package. Prior to the start of the legislative

session, the Rules staff also reviewed and commented on proposed tax legislation submitted by other executive branch agencies.

After reviewing all bills introduced to the Legislature, the Rules staff determined that there were approximately 323 measures proposing tax law changes and analyzed them in depth. The measures were tracked throughout the legislative session and written testimonies were prepared each time a tax measure was heard by the Legislature. The Rules staff also drafted numerous responses to legislative committee chairs responding to specific questions raised during hearings or to address specific concerns of committee members.

The Rules staff also prepared Tax Announcements, Tax Information Releases, letter rulings, Administrative Directives, and other publications. During FY 2019, 13 Tax Announcements and three Tax Information Releases were issued. Since 2009, when it became DOTAX's policy to publicly release taxpayer letter rulings in redacted form, 60 redacted letter rulings have been released.

In FY 2019, DOTAX promulgated administrative rules relating to taxpayers' last known address, the definition of "substantial gainful employment," sourcing of gross receipts from intangible property, clarifying "persons with material interest" for general excise tax purposes, and Act 204, Sessions Laws of Hawaii 2015 (transient accommodations tax).

Finally, the Rules staff also reviewed and certified 34 requests for the credit for research activities pursuant to section 235-110.91, HRS.

2.4.2.2 Technical Section

The Technical Section is tasked with varying responsibilities to carry out DOTAX's projects, goals and initiatives, and to support its operational needs. Specifically, the Technical Section assists and advises all divisions within the DOTAX, as well as outside parties such as individual and corporate taxpayers and tax professionals, on complex areas of the state tax laws. For FY 2019, the Technical Section responded to 1,542 email inquiries and 4,055 telephone inquiries. They also responded to formal requests which includes requests for letter rulings or information letters, determinations of tax status (such as for eligibility for the general excise tax exemptions for air-pollution control facilities), and multi-level marketing agreements as well as tax surveys and questionnaires from other government agencies, educational institutions, and major tax service product providers.

The Technical Section also reviews, researches, analyzes, and provides comments and recommendations on the technical and procedural aspects of legislative bills, administrative rules, and tax information releases. The staff is responsible for revising or creating the State's tax forms and instructions, incorporating all applicable federal and state tax law changes. For FY 2019, the Technical Section reviewed 484 tax forms, 58 tax form instructions, 27 Tax Modernization System letter templates and 28 Tax Publications. The Technical Section also developed 4 new tax forms, and no tax forms were made obsolete.

Other duties of the Technical Section include analyzing and reviewing certain applications for tax

exemptions. In FY 2019, 181 applications for an exemption from the general excise tax were received, 164 applications were reviewed and approved, 76 applications are pending further action and 20 applications were cancelled due to lack of response to a request for additional information or the organization did not qualify as exempt under section 237-23(b), HRS. In addition, 2,601 applications for conveyance tax exemptions were reviewed and processed.

2.4.3 Tax Research and Planning Office

The main functions of the Tax Research and Planning (TRP) Office include: (1) prepare reports on data collected by DOTAX, including monthly reports on collections of the State's various taxes and annual reports on the income patterns of individual and business taxpayers, tax credits claimed by taxpayers, general excise and use tax exemptions claimed; (2) provide administrative and technical support to the Council on Revenues, assisting in the preparation of forecasts for General Fund tax revenues and Total Personal Income; (3) provide economic and statistical analyses to help the DOTAX execute its policies and programs; (4) prepare reports on the revenue consequences of proposed tax legislation for the Legislature, the Governor, and other State agencies; (5) conduct economic analysis and educate the Legislature, the Governor, and other State agencies regarding the state's tax system; and (6) provide administrative and technical support to the Tax Review Commission when in session.

The TRP Office prepares the following reports on a monthly, fiscal year, and calendar year basis: (1) State Tax Collections and Distributions; (2) General Excise and Use Tax Collections; (3) Liquid Fuel Tax Base and Collections; (4) Liquid Fuel Tax Allocations by Fund; (5) Liquor Tax Collections and Permits; (6) Tobacco Tax Collections and Licenses, (7) Preliminary Comparative Statement of General Fund Tax Revenues, (8) the General Excise and Use Tax Liability Report by District, (9) the Transient Accommodation Tax Liability by District, and (9) the Liquor report.

In FY 2019, the TRP Office worked on DOTAX's Annual Report: 2017–2018, which was completed and submitted in December of 2018. The Office published reports on Tax Credits Claimed by Hawaii taxpayers, Hawaii Individual Income Tax Statistics, Hawaii Business Income Tax Statistics, and the Hawaii General Excise and Use Tax Exemptions report.

For the 2019 Legislative session, TRP staff reviewed and tracked tax-related legislative bills and resolutions, and prepared more than 616 revenue estimates for various drafts of the bills. Revenue estimates were also prepared for various proposals in response to requests from the administration, legislators, and others. The Office also responds to requests from the general public regarding statistics and trends of the Hawaii tax system.

An important function of the TRP Office is to provide administrative and technical support to help the Council on Revenues produce its forecasts of tax revenues. The seven members of the Council are responsible for forecasting General Fund revenues and the State's Total Personal Income. The Council provides forecasts of State revenue for the current and six subsequent fiscal years. The forecasts are due on September 10, January 10, March 15, and June 1 of each year. The forecasts are used by the Governor and by the Legislature to develop and administer the State's budget. The Council also forecasts Total Personal Income (TPI) for the current and immediately following

calendar years. The TPI forecasts are due on August 5 and November 5 of each year. The growth in Hawaii Total Personal Income is used to set the ceiling for expenditures from the State's General Fund, as required by the State's Constitution.

TRP staff applied econometric modeling techniques to data on State tax collections and to data on other economic variables to help the Council produce its forecasts. The Council's last General Fund forecast for FY 2019 was produced on August 29, 2019. The forecast called for tax collections dedicated to the Fund to grow by 4.1% compared with FY 2018.

The TRP Office updated its econometric models that were developed to predict General Fund tax collections based on the Council's forecasts for economic variables, including its original model, the model that was developed under a contract with UCLA Anderson Forecast, and the single-equation model that the Office developed at the request of the Council on Revenues.

2.4.4 Technical Services Office

The Technical Services Office was created in March 1, 2018 and incorporated the Tax System Modernization (TSM) Program Management staff (positions were at the DAGS, Office of Enterprise Technology Services and returned to DOTAX by the 2018 Legislature, effective July 1, 2018).

In Fiscal Year 2019, the Tax System Modernization (TSM) project completed its fourth of five major deployments. The November 2018 deployment addressed Individual Income, Partnership, Fiduciary, and Estate/Transfer tax. Highlights include:

- **Form N-11 (Resident income tax form).** Form N-11 can be filed on HTO, MeF, and paper. For Tax Year 2018, 55,546 were filed using MeF and 1,701 were filed using HTO.
- **Individual Income tax refund offsets:** Act 97, SLH 2019 gave DOTAX legal authority to administer tax refund offsets with Department of Accounting and General Services (DAGS). For Tax Year 2018, DOTAX implemented tax refund offsets for IRS (SITLP) and CSEA, recovering more than \$4 million in debts owed.
- **Identity Theft Protection:** Taxpayers can enroll in an Identity Theft Protection program, through which a taxpayer would be notified when a return is filed using their name and Social Security Number. About 100 people enrolled in this program for this first filing season.
- **Cashiering:** In January 2019, year-end changes went live. This deployment required included changes made to the G-45 and G-49 that incorporated rate change for the County Surcharge administered by Hawaii and Kauai counties.

On September 3, 2019, the TSM project delivered its fifth and final functional deployment. This deployment addressed cigarette/tobacco, fuel, and liquor tax, enabling all tax types to be managed through GenTax and Hawaii Tax Online. Highlights include:

- **Mandatory e-filing:** DOTAX required mandatory e-filing for certain tax types for the first time. Beginning taxable periods from September 2019, cigarette/tobacco, fuel, and liquor taxpayers will be required to e-file. Rental vehicle taxpayers will be required to e-file beginning October 2019. Other e-filing requirements will follow over the coming year.

- **License management.** DOTAX manages 1,116,317 different tax licenses/accounts.
 - Revocation due to abandonment. About 400,000 tax licenses were revoked due to abandonment on September 30, 2019. This is the first time that DOTAX utilized this legal authority.
 - Suspension and Revocation. In order to prevent licenses from being abandoned, DOTAX has begun suspending licenses due to non-filing.
- **Tax clearance automation.** DOTAX processes approximately 47,389 tax clearances in a year. Tax clearances are required for government contracts and licenses. With all tax types now operational in GenTax, tax clearance processing has been automated.
- **ITIMS was decommissioned** September 30, 2019. Correspondence and returns were migrated into GenTax.

With the completion of Rollout 5, **all 597 contractual requirements are complete.** The five TSM functional rollouts were **completed on time and within budget.** In total 15.5 million returns and 4.24 million accounts were converted, and 44,800 test scenarios were written and executed.

Moving forward, the TSM project will be shifting its focus to **production support and warranty services.** During this phase, TSM will be focused on transitioning technical responsibilities from the vendor to DOTAX staff. There are two major releases anticipated annually: (1) Year End Changes in January and (2) Mid-Year Changes in July. Each of these major releases will provide additional features and functionality, including changes to the core software. In addition, weekly releases of bug fixes and enhancements will be delivered throughout the year.

Other major technical initiatives include:

- **Information Security Training and Certifications & Suitability Background Checks.** In order to comply with IRS security requirements, DOTAX developed and delivered Information Security training that was completed by all staff. In addition, all staff completed Suitability Background Checks, including fingerprint reviews. Additional work will be done to implement all policies and procedures required by the IRS.
- **DOTAX system replacement.** The aging server infrastructure to support DOTAX administrative functions was replaced.
- **Windows 10 deployment.** With the decommissioning of ITIMS, the desktop operating systems can be upgraded from Windows 7. Windows 10 will bring DOTAX to Microsoft 365 and Adobe.
- **Interactive Voice Recognition (IVR) expansion.** The contact center phone system was expanded to include Collections. Additional enhancements are being undertaken to improve the base configuration to enable additional staff in Honolulu to be added to the phone system.
- **Disaster Recovery.** Working with DAGS/ETS to reconfigure the network to enable neighbor island offices to be operational in the event that the Honolulu Punchbowl office is unavailable.

2.4.5 Information Technology Services Office (ITSO)

The Information Technology Services Office (ITSO) is responsible for providing technical support for the DOTAX's computerized tax systems and applications, local area network, and network-related components and infrastructures.

During FY 2019, ITSO continued to focus on managing, administering, and maintaining the Integrated Tax Information Management System (ITIMS) and supporting network-related components and infrastructures. The ITS Office also supported the multi-year Tax System Modernization (TSM) Program, which will eventually replace all the DOTAX's current information technology systems and applications.

Key initiatives in the fiscal year include:

1. Maintenance and operation of the legacy ITIMS systems, which was decommissioned in September 2019.
2. Development and deployment of system modifications to accommodate year end changes, which included modifications to implement mandated tax law changes for Act 174, SLH 2019 to increase the rental motor vehicle surcharge tax (RVST) from \$3 to \$5 per day effective July 1, 2019, configurations of a 0.25 percent county surcharge for Hawaii County and 0.50 percent surcharge for Kauai County on General Excise Taxes, and the modification of 21 forms.
3. Assisting vendors using the bulk filing process to file withholding taxes. A total of ten vendors are now using the bulk filing application.
4. Migration of 67,739,087 return images from ITIMS to GenTax systems.
5. Replacing 351 aging workstations and upgrading operating systems by the end of Calendar Year 2019.
6. Deployment of security tools to provide additional network and data security, vulnerability management, and compliance checks across the environment.
7. Replacement of aging servers with a Hyper Converted Infrastructure (HCI) stack in the off-site data center. The HCI server stack provides a highly available, redundant, expandable platform for daily operations, consolidated resources, and improves efficiency.
8. The expansion of the Pure Connect Customer Interaction Center telephony platform to the Collections Section and to improve the taxpayer services.

2.4.6 Taxpayer Advocate

The Taxpayer Advocacy Program assists taxpayers who do not have a resolution to their tax related issue after going through normal channels. This program provided assistance to 947 taxpayers during the Fiscal Year ending June 30, 2019.

The Taxpayer Advocate assisted taxpayers in working to resolve systemic problems within DOTAX. Examples of issues addressed include processing, inter-departmental and workflow problems which affect taxpayers.

Other accomplishments of this office included speaking, teaching, and participating in tax

workshops and educational outreaches to tax professionals and the general public.

2.4.7 Tax Practitioner Priority Office

The Practitioner Priority Specialist (PPS) office provides tax practitioners a separate and dedicated connection to DOTAX's Taxpayer Services functions.

The PPS office assisted verified tax practitioners via telephone, email, and fax to resolve tax account issues such as locating and applying payments, explaining notices and letters, providing procedural guidance, and assisting with other taxpayer account inquiries. Tax issues outside these parameters were referred for follow up to the appropriate functions within DOTAX.

The PPS also assisted verified tax practitioners by working within DOTAX to improve services (including online) and workflows based on their input.

Other accomplishments of this office included speaking, teaching, and participating in tax workshops and educational outreaches to tax professionals.

2.5 MANAGEMENT PERSONNEL

As of June 30, 2019

OFFICE OF THE DIRECTOR

Director of Taxation Linda Chu Takayama
Deputy Director of Taxation Damien Elefante

STAFF OFFICES

Public Information Officer Deborah Kwan
Rules Officer Ted Shiraishi
 Technical Section Supervisor Denise Inouye
Tax Research & Planning Officer Seth Colby
 Senior Economist Yvonne Chow
Senior Special Assistant & Technical Program Manager Rona Suzuki
Information Technology Services Officer Robert Su
Administrative Services Officer Dexter Suzuki
 Personnel Officer Jennifer Egami
Taxpayer Advocate Jaysen Morikami
Administrative Appeals Officer Adriane Aarona
Tax Practitioner Priority Specialist Rachael Raquino

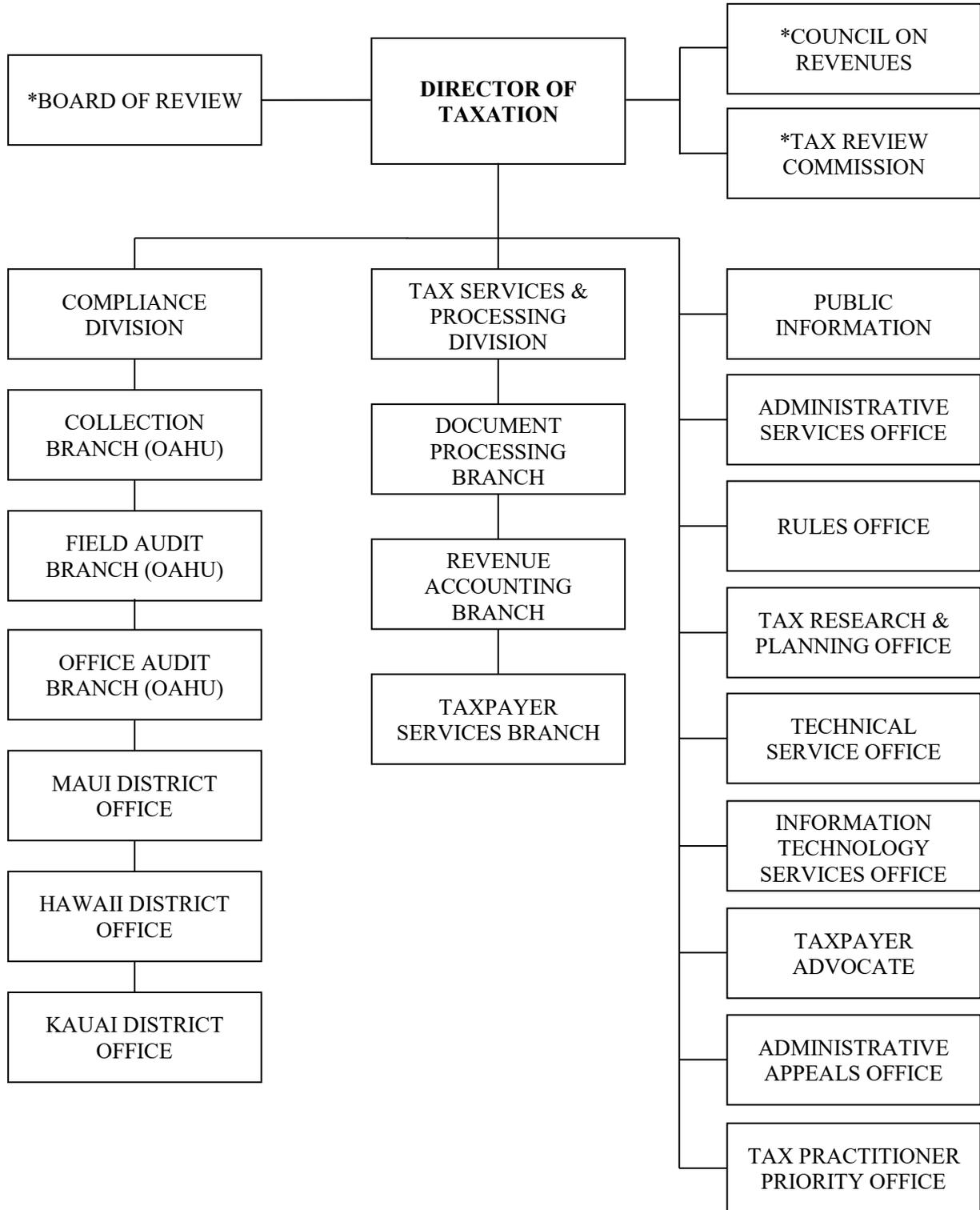
OPERATIONS STAFF

Taxation Compliance Administrator Kevin Wakayama
 Acting Tax Compliance Coordinator Regina Yuen
 Oahu Field Audit Branch Chief Madelaina Lai
 Oahu Office Audit Branch Chief Donald Kuriki
 Acting Oahu Collection Branch Chief Bryce Okamoto
 Maui District Tax Manager John Higgins
 Hawaii District Tax Manager Duquesne Hulihee
 Kauai District Tax Manager Ruth Jackson

Taxation Services Administrator Nicki Ann Thompsom
 Document Processing Operations Manager Todd Kuromoto
 Revenue Accounting Branch Chief Jennifer Oshiro
 Taxpayer Services Branch Chief John Pacheco

2.6 ORGANIZATION CHART

As of June 30, 2019



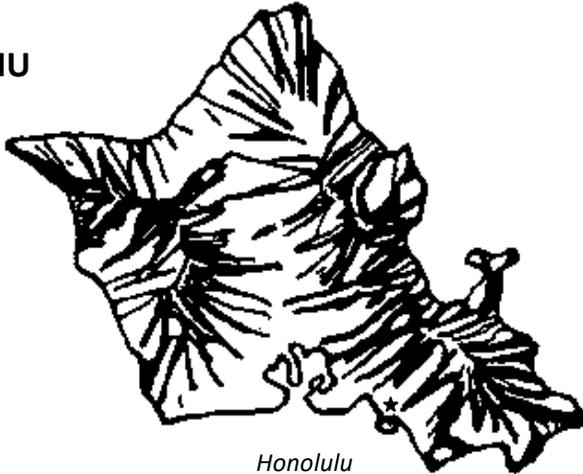
*For Administrative Purposes.

2.7 DISTRICT OFFICES

FIRST TAXATION DISTRICT

City & County of Honolulu

OAHU

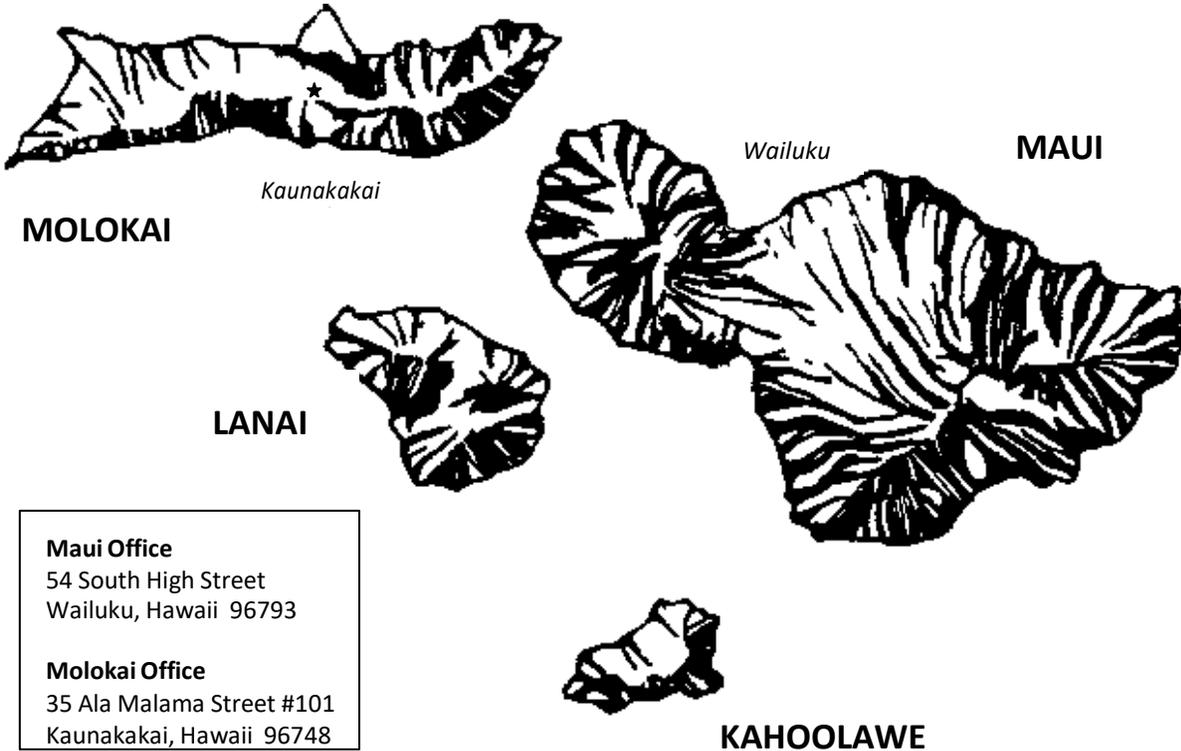


Honolulu

Oahu Office
830 Punchbowl Street
Honolulu, Hawaii 96813

SECOND TAXATION DISTRICT

Counties of Maui and Kalawao



Kaunakakai

Wailuku

MAUI

MOLOKAI

LANAI

Maui Office
54 South High Street
Wailuku, Hawaii 96793

Molokai Office
35 Ala Malama Street #101
Kaunakakai, Hawaii 96748

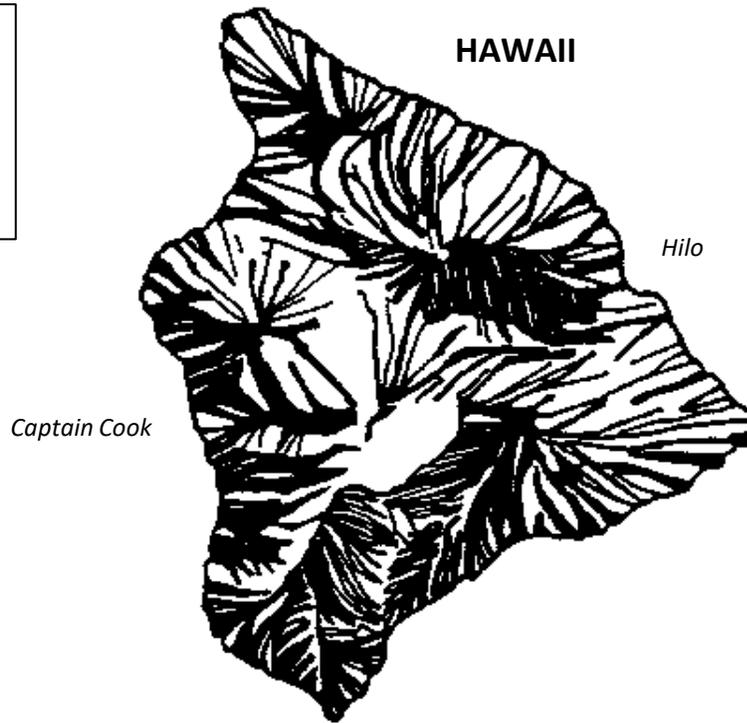
KAHOO LAWE

THIRD TAXATION DISTRICT

County of Hawaii

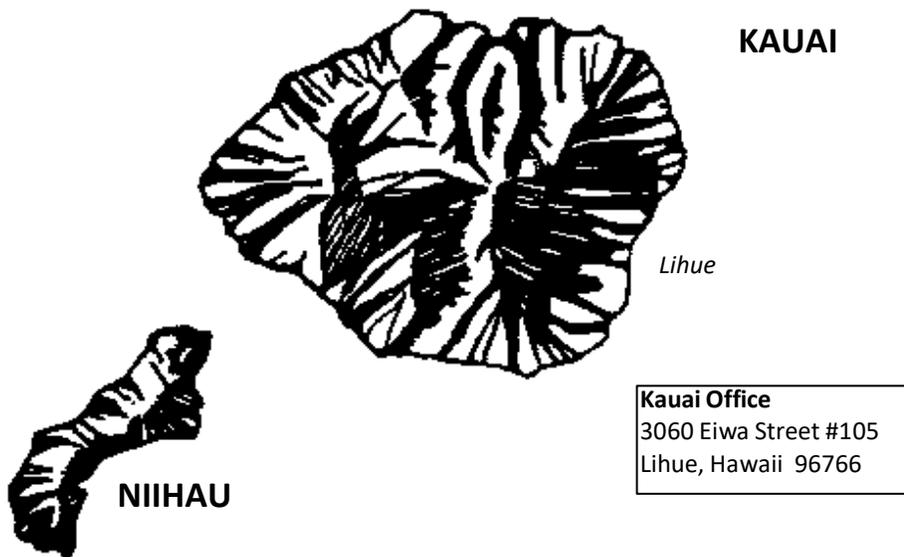
Hilo Office
75 Aupuni Street
Hilo, Hawaii 96720

Kona Office
82-6130 Mamalahoa Highway #8
Captain Cook, Hawaii 96704



FOURTH TAXATION DISTRICT

County of Kauai



3.0 APPEALS AND LITIGATION

3.1 ADMINISTRATIVE APPEALS OFFICE

The Administrative Appeals Office administers the Administrative Appeals and Dispute Resolution (AADR) program. AADR is a streamlined appeals process that assists taxpayers and return preparers in resolving their disputes involving proposed assessments, final assessments, and return preparer penalty assessments issued as a result of a DOTAX audit. Our mission is to help people resolve tax disputes fairly, expeditiously, and without litigation. The AAO is separate and independent of the DOTAX offices that conduct audits and issue assessments. For more information about the program, please visit our website at tax.hawaii.gov/appeals.

In FY 2019, 86 appeals were filed and 107 cases closed. There were 23 cases pending as of June 30, 2019. The AAO's caseload data is described in further detail in the table below. As part of the Tax System Modernization (TSM) project, taxpayers can now electronically file an appeal application to appeal proposed or final assessments for the following tax types: corporate income, general excise/use, transient accommodations, rental motor vehicle, franchise, withholding, and public service company taxes.

AAO Caseload for Fiscal Year 2019

Type of Case	Cases Received	Cases Closed ¹	Cases Pending (June 30, 2019)
General Excise/Use Tax	53	70	11
Income Tax	26	30	9
Other ²	7	7	3
Total Cases	86	107	23

¹Cases closed includes cases received in prior fiscal years.

²"Other" cases involve miscellaneous tax types such as franchise tax and transient accommodations tax and cases where multiple tax types were appealed.

3.2 BOARDS OF TAXATION REVIEW

Each taxation district has an administrative (i.e., non-judicial) Board of Taxation Review consisting of five members. Tax disputes that are not resolved at the district tax office level may be appealed to a Board of Taxation Review unless the dispute involves the Constitution or laws of the United States. Statewide, the boards began the fiscal year with 177 pending tax appeals. In FY 2019, 27 new appeals were filed, 11 appeals withdrawn, and 13 appeals settled; a total of 180 appeals to the Boards of Taxation Review were pending at the end of the fiscal year.

The following table details appeals to the Boards of Taxation Review by taxation district:

Taxation District	First					TOTAL
	Field	Office	Second	Third	Fourth	
Appeals Pending (Beginning)	85	36	37	9	10	182
New Appeals	10	11	0	3	3	28
Appeals Withdrawn	5	4	0	2	0	11
Appeals Settled	4	3	1	5	0	13
BOR Appeals Pending (Ending)	86	40	36	5	13	180

3.3 CIVIL DECISIONS, SETTLEMENTS AND OTHER LEGAL MATTERS

Matters Closed

During the last fiscal year, the Tax & Charities Division (“Division”) closed 799 Tax Department-related legal matters (excluding legislative matters in our case management system that DOTAX’s Legislative Division has not closed).

Tax Appeals	33
Bankruptcies	558
Contracts	10
Foreclosures	182
Legislation	Leg. Div has not closed any yet
Miscellaneous	7
Opinions	0
Quiet Title	2
Subpoenas	7
Admin Rules	1
Rule Review	1

Amounts Collected

Last fiscal year, the Division collected the following amounts:

Tax Appeals	\$301,731.42
Bankruptcies	\$1,229,621.48
Foreclosures	\$0.00
Miscellaneous	\$0.00
Trusts	\$0.00
Total	\$1,531,352.90

3.3.1 Resolved Tax Appeal Cases

In the Matter of Tax Appeal of James J. Richard & Rachael D. Richard, Case No. 1 T.X. 10-1-1805, Tax Appeal Court, State of Hawaii.

Taxpayers were assessed additional income and general excise taxes. Taxpayers challenged DOTAX 's reclassification and recalculation of their liabilities that were based on Taxpayers' IRC § 338(g) election on a sale of a business. The basis of Taxpayers' claim is that they made an election error on the Form 8023 and the parties to the sale intended a IRC § 338(h)(10) election instead of the IRC § 338(g) election. Taxpayers also challenged DOTAX's reclassification of income that changed the amount received as personal loans and/or advances from their business to wages. This case was settled.

In the Matter of the Tax Appeal of Avery B. Chumbley, Case No. 1 T.X. 14-1-0226, Tax Appeal Court, State of Hawaii.

Taxpayer was assessed general excise taxes and interest for underreported gross receipts of a non-profit organization's fund-raising activities. Taxpayer was assessed personally as the president of the organization at the time. Taxpayer claims he was entitled to deductions for certain expenses that were disallowed by DOTAX. This case was settled.

In the Matter of the Tax Appeal of Hawaiian Telcom Services Company, Inc., Case Nos. 1 T.X. 14-1-0231, 1 T.X. 15-1-0245, 1 T.X. 16-1-0321, and 1 T.X. 17-1-1386, Tax Appeal Court, State of Hawaii.

Taxpayer appealed the denial of use tax refund claims. Taxpayer claimed that Haw. Rev. Stat. §§ 238-2 and 238-2.3 impermissibly imposed use tax in violation of the commerce clause and the equal protection clause of the United States Constitution; the statutes discriminated against interstate commerce and were not fairly apportioned; and that Taxpayer erroneously paid use taxes with respect to services and/or contracting performed within the state by a licensed seller. These cases were dismissed by stipulation based on the decision in CompUSA Inc.

In the Matter of the Tax Appeal of Hawaiian Telcom, Inc., Case Nos. 1 T.X. 14-1-0232, 1 T.X. 15-1-0244, 1 T.X. 16-0322, and 1 T.X. 17-1-1385, Tax Appeal Court, State of Hawaii.

Taxpayer appealed the denial of use tax refund claims. Taxpayer claimed that Haw. Rev. Stat. §§ 238-2 and 238-2.3 impermissibly imposed use tax in violation of the commerce clause and the equal protection clause of the United States Constitution; the statutes discriminated against interstate commerce and were not fairly apportioned; and that Taxpayer erroneously paid use taxes with respect to services and/or contracting performed within the state by a licensed seller. These cases were dismissed by stipulation based on the decision in CompUSA Inc.

In the Matter of the Tax Appeal of Hawaiian Electric Company, Inc., Case Nos. 1 T.X. 14-1-0233, 1 T.X. 15-1-0296, 1 T.X. 16-1-0316, and 1 T.X. 17-1-1376, Tax Appeal Court, State of Hawaii.

Taxpayer appealed the denial of use tax refund claims. Taxpayer claimed that Haw. Rev. Stat. §§ 238-2 and 238-2.3 impermissibly imposed use tax in violation of the commerce clause and the equal protection clause of the United States Constitution and that the statutes discriminated against interstate commerce and were not fairly apportioned. These cases were dismissed by stipulation based on the decision in CompUSA Inc.

In re Tax Appeal of Longs Drug Stores Ca., LLC, Case Nos. 1 T.X. 14-1-0240, 1 T.X. 15-1-0237, and 1 T.X. 16-1-0314, Tax Appeal Court, State of Hawaii.

These cases were on hold pending the outcome of In the Matter of the Tax Appeal of CompUSA Inc., Case Nos. 12-1-0264, 12-1-0265, Tax Appeal Court, State of Hawaii and were dismissed by stipulation based on the decision in CompUSA Inc.

In the Matter of the Tax Appeal of Hawaii Electric Light Company, Inc., Case Nos. 1 T.X. 14-1-0259, 1 T.X. 15-1-0297, 1 T.X. 16-1-0317, and 1 T.X. 17-1-1377, Tax Appeal Court, State of Hawaii.

Taxpayer appealed the denial of use tax refund claims. Taxpayer claimed that Haw. Rev. Stat. §§ 238-2 and 238-2.3 impermissibly imposed use tax in violation of the commerce clause and the equal protection clause of the United States Constitution and that the statutes discriminated against interstate commerce and were not fairly apportioned. These cases were dismissed by stipulation based on the decision in CompUSA Inc.

In the Matter of the Tax Appeal of Maui Electric Company, Inc., Case Nos. 1 T.X. 14-1-260, 1 T.X. 15-1-0298, 1 T.X. 16-1-0315, and 1 T.X. 17-1-1378, Tax Appeal Court, State of Hawaii.

Taxpayer appealed the denial of use tax refund claims. Taxpayer claimed that Haw. Rev. Stat. §§ 238-2 and 238-2.3 impermissibly imposed use tax in violation of the commerce clause and the equal protection clause of the United States Constitution and that the statutes discriminated against interstate commerce and were not fairly apportioned. These cases were dismissed by stipulation based on the decision in CompUSA Inc.

In re Tax Appeal of Escal Institute of Advanced Technologies, Inc., Case No. 1 T.X. 15-1-0276, Tax Appeal Court, State of Hawaii.

In the Matter of the Tax Appeal of Escal Institute of Advanced Technologies, Inc., Case No. 1 T.X. 17-1-1374, Tax Appeal Court, State of Hawaii.

Taxpayer, for itself and its shareholders, appealed assessments on tax years 2008, 2010, 2012, and 2013 for income tax refunds denied; 2011 through 2013, inclusive, for income taxes assessed; and 2008, 2009, 2011 through 2013, inclusive, for general excise taxes assessed, alleging that refunds to shareholders were wrongly denied. Additionally, Taxpayer alleged that income taxes and general excise taxes were assessed on income from services performed outside Hawaii. This case was settled.

In re Tax Appeal of Pacific Isles Equipment Rental Inc., Case No. 1 T.X. 15-1-0315, Tax Appeal Court, State of Hawaii.

Taxpayer's President, a non-attorney, initially filed a Notice of Appeal of general excise taxes for tax years 2010, 2011, and 2012 and made payment "under protest." Taxpayer hired an attorney who filed a Complaint for Refund of Taxes in the tax appeal case. A motion to dismiss was granted in part and denied in part. Taxpayer claimed that pursuant to Haw. Rev. Stat. § 237-13, the 0.5 percent wholesale rate applied rather than the 4.5 percent contracting rate. This case was dismissed per Taxpayer's request.

In the Matter of the Tax Appeal of Hawaiian Telcom Communications, Inc., Case Nos. 1 T.X. 16-1-0323 and 1 T.X. 17-1-1384, Tax Appeal Court, State of Hawaii;

Taxpayer appealed the denial of use tax refund claims. Taxpayer claimed that Haw. Rev. Stat. §§ 238-2 and 238-2.3 impermissibly imposed use tax in violation of the commerce clause and the equal protection clause of the United States Constitution; the statutes discriminated against interstate commerce and were not fairly apportioned; and that Taxpayer erroneously paid use taxes with respect to services and/or contracting performed within the state by a licensed seller. These cases were dismissed by stipulation based on the decision in CompUSA Inc.

In the Matter of the Tax Appeal of Woodley L. Hunt; Gayle G. Hunt; Hunt ELP, Ltd.; Hunt Companies, Inc.; HB GP, LLC; Marion L. Hunt; and Norma H. Hunt, Case No. 1 T.X. 16-1-0340, Tax Appeal Court, State of Hawaii.

Taxpayers appealed income tax assessments for underreported taxable income due to understatement of a partnership's capital gains received from sale of real property in Hawaii. Taxpayers argued that the capital gains in question should be excluded from the Hawaii sales factor numerator and denominator for apportionment purposes. This case was settled.

In the Matter of the Tax Appeal of Wavecom Solutions Corporation, Case No. 1 T.X. 17-1-1390, Tax Appeal Court, State of Hawaii.

Taxpayer appealed the denial of use tax refund claims. Taxpayer claimed that Haw. Rev. Stat. §§ 238-2 and 238-2.3 impermissibly imposed use tax in violation of the commerce clause and the equal protection clause of the United States Constitution; the statutes discriminated against interstate commerce and were not fairly apportioned; and that Taxpayer erroneously paid use taxes with respect to services and/or contracting performed within the state by a licensed seller. This case was dismissed by stipulation based on the decision in CompUSA Inc.

In the Matter of the Tax Appeal of Perigon Partners, LLC, Case No. 1 T.X. 18-1-0317, Tax Appeal Court, State of Hawaii.

Taxpayer appealed final assessments for general excise taxes for tax year 2015. Taxpayer claimed that the assessed amounts are excessive because it improperly included taxes on amounts for services rendered out of the State. This case was settled.

3.2.2 Resolved Miscellaneous Tax Cases

Tax Foundation of the State of Hawaii, Inc. v. State of Hawaii, CAAP-16-0000462, Supreme Court, State of Hawaii.

In this case, the Tax Foundation of the State of Hawaii brought an action for injunctive and mandamus relief. At issue was the county surcharge on state tax, Haw. Rev. Stat. § 248-2.6, that requires the Department of Budget and Finance to transfer ten percent of the amount collected to the general fund to reimburse DOTAX's costs of assessment and collection of the surcharge. Plaintiff argued that amounts transferred to the general fund exceeded DOTAX of Taxation's actual costs and expenses. Under these facts, Plaintiff alleged that the statute violated the due process and equal protection clauses of the United States Constitution. The complaint sought refunds on Plaintiff's behalf and on behalf of the City and County of Honolulu. DOTAX moved to dismiss the complaint for lack of subject matter jurisdiction. The

complaint was dismissed and Plaintiff appealed to the Hawaii Supreme Court. The Hawaii Supreme Court ruled in favor of the State in an opinion dated March 21, 2019. No further appeal was taken and the case is now concluded.

3.2.3 Pending Tax Appeal Cases

In the Matter of the Tax Appeals of TMI Management, Inc., Case Nos. 1 T.X. 09-0071 and 1 T.X. 09-0072, Tax Appeal Court, State of Hawaii.

Taxpayer was assessed additional general excise taxes on amounts received for performing work for the federal government. Taxpayer argues, among other things, that the disputed income was exempt because Taxpayer was an employee leasing company and the disputed income was for salaries and expenses of leased employees. This case has been taken off the trial ready calendar.

In the Matter of the Tax Appeals of Bernard & Ellen Fuller and South Pacific Builders, Ltd., Case Nos. 1 T.X. 09-0087, 1 T.X. 09-0088, and 1 T.X. 09-0089, Tax Appeal Court, State of Hawaii.

Taxpayers were assessed additional general excise and net income taxes on amounts received for performing work within the State. Taxpayers argue, among other things, that the disputed income was exempt because Taxpayers paid certain amounts to other contractors. This case was taken off the trial ready calendar to give the parties time to work on settlement. Taxpayers' counsel withdrew from this case and Taxpayers are seeking new counsel.

In the Matter of the Tax Appeal of Patrick O'Brien, Case No. 1 T.X. 11-1-0013, Tax Appeal Court, State of Hawaii.

Taxpayer was assessed additional income taxes for unreported schedule C income from a single member LLC the Taxpayer owned. Taxpayer denies the income is taxable to him. Trial is not scheduled.

In the Matter of the Tax Appeal of Security Resources, LLC, Case No. 1 T.X. 11-1-0014; Tax Appeal Court, State of Hawaii.

Taxpayer was assessed additional general excise taxes for underreporting the amount of gross receipts it received. Taxpayer claims the assessments are overstated and that it is entitled to be taxed at the wholesale rate of .5 percent. Taxpayer also claims some of its sales are exempt because they were sales of tangible personal property to the federal government. Trial is not set.

In the Matter of the Tax Appeal of Julie A. Dunham, Case No. 1 T.X. 12-1-0390, Tax Appeal Court, State of Hawaii.

Taxpayer was assessed general excise and income taxes on non-filed returns for 1999 through 2010, inclusive. Taxpayer argues that DOTAX's income figures are incorrect. Trial is set for September 9, 2019.

In the Matter of the Tax Appeal of William A. Bartenstein, Case No. 1 T.X. 13-1-0228, Tax Appeal Court, State of Hawaii.

Taxpayer was assessed additional general excise and/or use taxes and penalties and interest on goods imported for resale. Taxpayer argues that DOTAX's income figures are incorrect and the stacking of the negligence and underpayment penalties is erroneous. Trial is set for March 9, 2020.

In the Matter of Priceline.com, Case Nos. 1 T.X. 13-1-0269, (and consolidated cases 1 T.X. 13-1-0261 through 1 T.X. 13-1-0270, 1 T.X. 14-1-0001 through 1 T.X. 14-1-0010, and 1 T.X. 14-1-0243 through 14-1-0251), Tax Appeal Court, State of Hawaii.

These consolidated tax appeals are by online travel companies Expedia, Inc., Hotwire, Inc., Orbitz, LLC., Trip Network, Inc. dba Cheaptickets.com, and Priceline.com ("OTCs") from assessments of general excise tax and penalties and interest for the OTCs' rental motor vehicle transactions in the State for tax years 2000 through 2013, inclusive. On cross motions for summary judgment, the Tax Appeal Court ruled that the OTCs owed general excise tax on their gross receipts on stand-alone rental car transactions, but where the car rental is part of a package transaction, then the OTCs are entitled to an apportionment and need to pay general excise tax only on the portion they retain from the gross amount collected. Both sides appealed to the Hawaii Supreme Court. The Hawaii Supreme Court heard oral arguments on April 5, 2018 and issued its ruling on March 4, 2019. The Hawaii Supreme Court ruled that the OTCs are entitled to a general excise tax apportionment on both stand-alone and package rental car transactions and remanded the matter back to the Tax Appeal Court for recalculation of the OTCs' general excise tax liability and associated penalties and interest.

In the Matter of the Tax Appeal of Skydiving School, Inc., Case Nos. 1 T.X. 14-1-0217 and 1 T.X. 14-1-0218, Tax Appeal Court, State of Hawaii.

Taxpayer appeals from the denial of a refund claim and assessments of general excise taxes related to its skydiving business. Taxpayer's major issue is that its gross receipts from skydiving activities is not subject to the general excise tax because of federal preemption under the Anti-Head Tax Act, P.L. 103-272, 108 Stat. 1111, as amended, and as codified in 49 U.S.C. § 40116. Trial briefs were submitted in lieu of a trial. The Tax Appeal Court has not ruled yet.

In the Matter of the Tax Appeal of Edward A. Alquero, M.D., Inc., Case No. 1 T.X. 14-1-0219, Tax Appeal Court, State of Hawaii.

Taxpayer was assessed additional income and general excise taxes, penalties, and interest for underreported income related to his medical practice. Taxpayer claims he is entitled to deductions for certain expenses that DOTAX disallowed. Trial is set for January 27, 2020.

In the Matter of the Tax Appeal of Darren Truitt, Case No. 1 T.X. 14-1-0228, Tax Appeal Court, State of Hawaii.

Taxpayer appeals DOTAX's assessment of additional income taxes, and penalties and interest for income attributed to his wholly owned LLC. Taxpayer's counsel withdrew from this case. The Tax Appeal Court took this case off the trial ready calendar to allow Taxpayer time to obtain new counsel.

In the Matter of the Tax Appeal of Construction Servs. & Management LLC, Case No. 1 T.X. 14-1-0229, Tax Appeal Court, State of Hawaii.

Taxpayer appeals DOTAX's assessment of general excise taxes, and penalties and interest for underreported gross receipts. Taxpayer's counsel withdrew from this case. The Tax Appeal Court took this case off the ready trial calendar to allow Taxpayer time to obtain new counsel.

In the Matter of the Tax Appeal of Hawaiian Airlines, Inc., Case No. 1 T.X. 14-1-0258, Tax Appeal Court, State of Hawaii.

Taxpayer claims a use tax refund alleging that it paid use tax on purchases of jet fuel from World Fuel Services for use and consumption during its inter-island flights. Trial is not set.

In the Matter of the Tax Appeal of Home Depot U.S.A., Inc., Case No. 1 T.X. 15-1-0218, Tax Appeal Court, State of Hawaii.

Taxpayer appeals DOTAX's disallowance of the wholesale rate on general excise taxes due on sales to customers at its retail stores as well as DOTAX's denial of the subcontractor deduction related to work performed for customers. Trial is set for October 7, 2019.

In the Matter of the Tax Appeal of Dan S. Tetsutani, Case No. 1 T.X. 15-1-0219, Tax Appeal Court, State of Hawaii.

Taxpayer appeals from a final assessment of additional general excise tax and/or use taxes stating the assessments were improper, or in the alternative, that Taxpayer should pay the wholesale rate. Trial is set for March 23, 2020.

Maria E. Zielinski v. Blake and Bianca Goodman, Case No. 1 T.X. 15-1-0221; Tax Appeal Court, State of Hawaii;

DOTAX denied Taxpayers' fully refundable Renewable Energy Technologies tax credits under Haw. Rev. Stat. § 235-12.5 because Taxpayers' adjusted gross income exceeded the statutory threshold entitling them to a fully refundable credit. The Board of Review ruled that Taxpayers could revoke their elections to receive refundable tax credits. Cross motions for summary judgment were heard on July 17, 2017; however, the Tax Appeal Court has not ruled yet. Trial was taken off the trial ready calendar.

In the Matter of the Tax Appeal of Polynesian Cultural Center, Case No. 1 T.X. 16-1-0290, Tax Appeal Court, State of Hawaii.

Taxpayer appeals DOTAX's assessment of additional general excise taxes based on the disallowance of the income splitting provisions under Haw. Rev. Stat. § 237-18(f). Trial is set for July 13, 2020.

In re Tax Appeal of Thomas Aki, Case No. 1 T.X. 16-1-0291, Tax Appeal Court, State of Hawaii.

Taxpayer appeals income tax assessments for tax years 2012, 2013, and 2014 in which DOTAX disallowed business expenses and deductions under Haw. Rev. Stat. chapter 235, disallowed the personal exemption deduction, and disallowed the application of losses from prior years. Trial is set for October 28, 2020.

In re Tax Appeal of Jeffrey Scott Lindner, Case No. 1 T.X. 16-1-0300, Tax Appeal Court, State of Hawaii.

Taxpayer appeals income taxes for tax years 2012 through 2014, inclusive. Taxpayer claims that he properly filed returns to qualify for High Technology Business Investment Tax Credits per Haw. Rev. Stat. § 235-110.9; however, DOTAX claims that it did not receive the returns. Trial is set for December 7, 2020.

In the Matter of the Tax Appeal of Gary Takahashi Sports Marketing Inc., Case No. 1 T.X. 16-1-0319, Tax Appeal Court, State of Hawaii.

Taxpayer appeals final assessments of general excise tax based on information obtained from the Internal Revenue Service. Taxpayer claims that assessments were improper because all sales occurred outside of Hawaii. Trial is set for December 16, 2019.

In the Matter of the Tax Appeal of Gary K. Takahashi, Case No. 1 T.X. 16-1-0320, Tax Appeal Court, State of Hawaii.

Taxpayer appeals final assessments of general excise tax based on information obtained from the Internal Revenue Service. Taxpayer claims that the assessments should have been made on Gary Takahashi Sports Marketing Inc. and not on him individually. Trial is set for December 16, 2019.

In the Matter of the Tax Appeal of Janice P.C. Hori, Case No. 1 T.X. 17-1-1340, Tax Appeal Court, State of Hawaii.

Taxpayer appeals final assessments of general excise taxes that were made based on information obtained from Taxpayer's income tax return. Taxpayer did not file general excise tax returns for the years listed on her income tax return. Trial set for October 19, 2020.

In the Matter of the Tax Appeal of Certified Erosion Control Hawaii LLC., Case No. 1 T.X. 17-1-1341, Tax Appeal Court, State of Hawaii.

Taxpayer appeals final assessments of general excise tax claiming it was entitled to the wholesale rate. Taxpayer was a non-filer and submitted unfiled returns with the auditor during the audit phase. Although Taxpayer qualified for the wholesale rate, the rate was disallowed because of Haw. Rev. Stat. § 237-41.5. Trial is set for December 16, 2019.

In the Matter of the Tax Appeal of Michelle Richardson, Case No. 1 T.X. 17-1-1349, Tax Appeal Court, State of Hawaii.

Taxpayer appeals final assessments of income and general excise taxes that were based on federal data because Taxpayer is a non-filer. Trial is set for October 29, 2019.

In the Matter of the Tax Appeal of Maui Fresh Fish Investors, LLC, Case No. 1 T.X. 17-1361, Tax Appeal Court, State of Hawaii.

Taxpayer appeals DOTAX's disallowance of QHTB credits for tax years 2010 through 2012. Taxpayer claims that funds set aside in a bank account were at risk as Haw. Rev. Stat. § 235-110.9 requires. Trial is set for February 3, 2020.

In the Matter of the Tax Appeal of Federal Business Council, Inc., Case No. 1 T.X. 18-1-0315, Tax Appeal Court, State of Hawaii.

Taxpayer appeals final assessments for general excise tax for tax years 2008 through 2013, inclusive. Taxpayer claims that much of its gross receipts are for services rendered outside of the State and should not be sourced to Hawaii for tax purposes. Trial is not set.

In the Matter of the Tax Appeal of Adrienne P. Sweeney, Case No. 1 T.X. 18-1-0316, Tax Appeal Court, State of Hawaii.

Taxpayer appeals the final assessment of income taxes after receiving notification that Taxpayer's administrative appeal had been closed. The final assessment disallows a deduction for repayment of trustee fees claimed on her 2014 Individual Income Tax Return. Trial is not set.

In the Matter of the Tax Appeal of Diamond Resorts Hawaii Collection Members Ass'n, Case Nos. 1 T.X. 18-1-0318, 1 T.X. 19-1-0180, 1 T.X. 19-1-0182, and 1 T.X. 19-1-0183.

These tax appeals involve the denial of Taxpayer's refund claim for general excise taxes for tax years 2014 through 2017, inclusive. Taxpayer claims that it operates timeshares in Hawaii and across the mainland United States and that for the tax years in question, it incorrectly included income from timeshares on the mainland that should not have been reported on its Hawaii return. Trial is not set.

In the Matter of the Tax Appeal of Richard A. and Leony C. Wheelock, Case No. 1 T.X. 18-1-0326.

Taxpayers appeal final assessments of income taxes for tax years 2008 through 2010, inclusive. Taxpayers contend that DOTAX improperly disallowed deductible expenses for mortgage interest in each of the tax years in issue. The parties have submitted a stipulation to the Tax Court to allow the case to be placed into DOTAX's Administrative Appeals and Dispute Resolution Program and are awaiting the court's approval of the same. Trial is not set.

In the Matter of the Tax Appeal of Colorado Personnel Resources, Inc., Case No. 1 T.X. 18-1-0334.

Taxpayer appeals from final assessments for general excise taxes for tax years 2004 through 2011, inclusive. Taxpayer challenges the assessments claiming that it lacks nexus with Hawaii. Trial is not set.

In the Matter of the Tax Appeal of EPRODS, LLC, Case No. 1 T.X. 18-1-0360.

Taxpayer appeals from final assessments for general excise taxes for tax years 2013 through 2016, inclusive. Taxpayer challenges the assessments on the basis that it exports the majority of its services and goods out-of-state and therefore is not subject to the general excise tax. Trial is not set.

In the Matter of the Tax Appeal of SP Cleaning Inc., Case No. 1 T.X. 18-1-0363.

Taxpayer appeals from final assessments for general excise taxes for tax years 2010 through 2011 and 2013 through 2016, inclusive. Taxpayer claims that the assessments overstate gross receipts. Trial is not set.

In the Matter of the Tax Appeal of Reliable Auto Movers Inc., Case No. 1 T.X. 18-1-0364.

Taxpayer appeals from final assessments for general excise taxes for tax years 2004 through

2017, inclusive. Taxpayer claims that the assessments incorrectly assess service income at the four percent rate instead of the wholesale rate and overstate gross receipts. Trial is not set.

In the Matter of the Tax Appeal of Scot Paiva, Case No. 1 T.X. 18-1-0365.

Taxpayer appeals from final assessments for income taxes for tax years 2010 through 2011 and 2013 through 2017, inclusive. Taxpayer claims that the assessments overstate flow-through income. Trial is not set.

In the Matter of the Tax Appeal of Masakazu Hirano, Case No. 1 T.X. 18-1-0366.

Taxpayer appeals from the denials of general excise tax refund claims for tax years 2013 and 2014 and general excise tax assessments for tax years 2015 and 2016. Taxpayer claims he erroneously paid general excise tax at the 4% rate when he should have been paying the wholesale rate. The Tax Appeal Court granted DOTAX's motion to dismiss on claims related to tax years 2013 and 2014. The claims relating to tax years 2015 and 2016 remain. Trial is not set.

In the Matter of the Tax Appeal of Rick YJ Cho, Case No. 1 T.X. 18-1-0412.

Taxpayer seeks a refund of taxes paid under protest in connection with final assessments for general excise and transient accommodations taxes for tax years 2008 and 2010 through 2016, inclusive. Taxpayer claims that the gross receipts are attributable to other entities and the related entities exemption applies. Trial is not set.

In the Matter of the Tax Appeal of HSI Honolulu Joint Venture Company, Case No. 1 T.X. 19-1-0166.

Taxpayer appeals from the denial of its refund claim for general excise taxes for tax year 2014 and the imposition of penalties for an erroneous claim for refund. Taxpayer claims that its gross receipts from sales at airport concessions are not subject to general excise tax due to preemption by the federal Anti-Head Tax Act. Trial is not set.

In the Matter of the Tax Appeal of HSI Kahului Joint Venture Company, Case No. 1 T.X. 19-1-0167.

Taxpayer appeals from the denial of its refund claim for general excise taxes for tax year 2014 and the imposition of penalties for an erroneous claim for refund. Taxpayer claims that its gross receipts from sales at airport concessions are not subject to general excise tax due to preemption by the federal Anti-Head Tax Act. Trial is not set.

In the Matter of the Tax Appeal of Host GRL LIH F&B, LLC, Case No. 1 T.X. 19-1-0168.

Taxpayer appeals from the denial of its refund claim for general excise taxes for for tax year 2014 and the imposition of penalties for an erroneous claim for refund. Taxpayer claims that its gross receipts from sales at airport concessions are not subject to general excise tax due to preemption by the federal Anti-Head Tax Act. Trial is not set.

In the Matter of the Tax Appeal of Gretchen Le Gre and GLG Holdings, LLC, Case No. 1 T.X. 19-1-0171.

Taxpayers filed a Notice of Appeal and a Complaint seeking: (1) a declaratory judgment that the conveyance tax is not applicable to the transfer of real property from a single-member LLC to the sole member; and (2) a refund of a \$443.15 conveyance tax purportedly paid

under protest for a transfer of a 10% interest in the property. The Director filed a motion to dismiss arguing: (1) declaratory relief is not available in any controversy with respect to taxes; and (2) Taxpayers failed to request an exemption for the subject transaction. The Tax Appeal Court granted the motion to dismiss, however, the order has not yet been entered.

In the Matter of the Tax Appeal of Kai Jacobsen, Case No. 1 T.X. 19-1-0184.

Taxpayer appeals from final assessments of general excise taxes for tax years 2009 through 2017, inclusive. Taxpayer claims, among other things, that the assessments improperly include tax on activities conducted and/or sales made outside the State of Hawaii. Trial is not set.

In the Matter of the Tax Appeal of Dolphin K. Pawn, Case No. 1 T.X. 19-1-0190.

Taxpayer appeals from final assessments of income taxes for tax years 2014 through 2017, inclusive. Taxpayer claims that he may be entitled to deductions and adjustments. Trial is not set.

In the Matter of the Tax Appeal of George Hochman, Case No. 1 T.X. 19-1-0197.

Taxpayer appeals from final assessments of general excise and withholding taxes for tax years 2003 and 2004 and 2008 through 2018, inclusive. Taxpayer claims, among other things, that the assessments improperly hold him personally liable for the general excise and withholding taxes of six corporations. Trial is not set.

In the Matter of the Tax Appeal of Guy C. Smith, Case No. 1 T.X. 19-1-0203.

Taxpayer appeals from final assessments of general excise and transient accommodations taxes for tax years 2008 through 2017, inclusive. Taxpayer claims that the assessments are incorrect. Trial is not set.

Other Civil Cases

Department of Taxation, State of Hawaii v. Airbnb, Inc., Special Proceeding No. 18-1-0315 JHA.

DOTAX petitioned the court to serve an administrative subpoena on Airbnb, Inc. for records of persons who booked accommodations in the State through Airbnb, Inc. from 2008 to the present. The court denied DOTAX's petition.

In re Office of Information Practices Opinion Letter No. F19-05, Special Proceeding No. 19-1-0191 DEO.

DOTAX appealed the Office of Information Practices' opinion letter finding that the assumptions, source data, and analysis used to create revenue estimates for legislative bills were not exempt from disclosure. DOTAX asserted that disclosure would frustrate a legitimate government function and the documents qualify as inchoate and draft working papers of legislative committees. The requester filed a counterclaim to compel disclosure of the documents. DOTAX's opening brief is due on September 30, 2019. No hearing is scheduled.

Booking.com v. Linda Chu Takayama, in her official capacity as Director of Taxation, and State of Hawaii Department of Taxation, Case No. 1 CC 19-1-0107-01 JHA.

Plaintiff Booking.com filed a complaint for declaratory relief alleging Hawaii Administrative Rules § 18-237-29.53-10(a)(3) is invalid and in violation of the Internet Tax Freedom Act, 47 U.S.C. § 151, by imposing tax in a discriminatory manner. Defendants filed a motion to dismiss the complaint, arguing: (1) the court does not have jurisdiction to grant declaratory relief in controversies with respect to taxes; and (2) Booking.com is not authorized to conduct business in Hawaii and therefore, cannot seek relief in state court. The court denied the motion to dismiss, but stayed the litigation "until it determines whether Plaintiff requires a certificate of authority." Trial is not set.

Department of Taxation, State of Hawaii v. Airbnb, Inc., Special Proceeding No. 19-1-0202 BIA.

DOTAX petitioned the court to serve an administrative subpoena on Airbnb, Inc. for records of persons who received payment from Airbnb, Inc. for accommodations in the State from 2016 to the present and persons who posted listings on Airbnb, Inc.'s website in April 2019 for accommodations in the State but who failed to list a Hawaii tax identification number. The hearing on the petition is scheduled for September 18, 2019.

4.0 ADMINISTRATIVELY ATTACHED ENTITIES

As of June 30, 2019

COUNCIL ON REVENUES

Kurt Kawafuchi, Chair

Marilyn M. Niwao, Vice-Chair

Carl S. Bonham

Christopher Grandy

Kristi L. Maynard

Jack P. Snyderhoud

Jessica E. Gluck

BOARDS OF TAXATION REVIEW

FIRST TAXATION DISTRICT

(OAHU)

Neil Hirasuna

Vacant

Vacant

Vacant

Vacant

THIRD TAXATION DISTRICT

(HAWAII)

Marilyn Gagen

Christopher Hannigan

Valerie Peralto

Richard Rovelstad

***SECOND TAXATION DISTRICT
(MAUI)***

William Curtis

Alan Bernaldo

Vacant

Vacant

***FOURTH TAXATION DISTRICT
(KAUAI)***

Vacant

Vacant

Vacant

Vacant

DEPARTMENT OF TAXATION

Goals and Objectives for Calendar Year 2020

The Department of Taxation (DOTAX) is required to submit goals and objectives to the Governor and Legislature (Act 100, Session Laws of Hawaii 1999). This section explains our strategic goals and objectives for Calendar Year 2020.

VISION

"The Department of Taxation efficiently and effectively collects the revenue needed to fund programs and services for the people of Hawaii."

MISSION

*"Our mission is to administer the tax laws for the State of Hawaii in a **fair, consistent, and efficient** manner."*

DOTAX recently made a small, but significant, modification to its mission statement by replacing "uniform" with "efficient" because (1) consistent and uniform were redundant and (2) "efficient" reflects our strategic priority. This updated mission statement reflects the following:

- **Fair** – All taxpayers need to pay their fair share of taxes. DOTAX ensures that we make it easy for taxpayers to voluntarily comply with Hawaii's tax laws and pursue non-filers and taxpayers with delinquencies to ensure that they pay their fair share.
- **Consistent** – DOTAX leverages our investment in technology to deploy consistent, uniform processes across the State to ensure that all taxpayers are treated equally.
- **Efficient** - DOTAX minimizes the cost of tax administration, minimizing operational costs per dollar collected. Presently, our cost of collecting each \$100 of taxes is 33 cents. Operationally, DOTAX will process payments and returns with improved accuracy and timeliness and addressing taxpayers concerns in a timely, professional manner.

GOALS

1. **Increase voluntary compliance.** DOTAX depends on voluntary compliance by the majority of our taxpayers. In order to support this, we are committed to making it easy for taxpayers to comply with our tax laws.

Objectives:

- Improving forms and instructions (paper and online) to make it easy for taxpayers to file and pay taxes.
- Enhancing web-based capabilities to provide information and enable taxpayers to self-service and file/pay electronically.

2. **Ensure all taxpayers pay their fair share.** While most taxpayers voluntarily comply with Hawaii's tax laws, DOTAX ensures that taxpayers who do not comply and/or attempt to commit fraud are brought into compliance.

Objectives:

- Aggressively pursuing non-filers and bad actors.

- Increasing collections activities to collect on outstanding tax liabilities.
3. **Provide consistent, efficient, secure service to all stakeholders.** DOTAX provides taxpayers service in person, in writing, and online through our staff located in offices across the state. Because of the sensitivity of the information in our care, it is important to maintain information security procedures to maintain taxpayer trust. In addition, operational procedures are needed so that taxpayers are treated consistently and efficiently by staff throughout the Department.
- Objectives:
- Leveraging our technologies and data to improve operational efficiency and data-driven decision making and process improvements.
 - Increasing transparency by making more information available to policy makers and other stakeholders.
 - Continuing to improve information security.
4. **Foster and empower staff.** The post-TSM DOTAX needs to adjust to our new technologies. The requirements for staff continue to evolve as we find opportunities to streamline and standardize processes and maximize the utilization of technologies. This is requiring continuous learning for DOTAX team members.
- Objectives:
- Evolving the organization structure and staff to adapt to the new organizational requirements.
 - Providing additional training to staff to enable utilization of our enhanced technologies, policies, and procedures.