

TAX REVIEW COMMISSION

**MINUTES OF THE FIRST MEETING OF THE
TAX REVIEW COMMISSION
HELD AT 830 PUNCHBOWL STREET
DEPARTMENT OF LABOR & INDUSTRIAL RELATIONS ROOMS 310-313
IN THE CITY AND COUNTY OF HONOLULU
STATE OF HAWAII, ON FRIDAY, JULY 15, 2011 AT 9AM**

The Commissioners of the Tax Review Commission (TRC) met at the Department of Labor & Industrial Relations Conference Rooms, in the City and County of Honolulu, State of Hawaii, on Friday, July 15, 2011.

Members Present: Randall Y. Iwase, Chair
Mitchell A. Imanaka, Vice-Chair
Roy K. Amemiya, Jr.
Peter S. Ho
Michael T. McEnerney
Darryl K. Nitta
Gregg M. Taketa

Staff: Donald Rousslang, Johnnel Nakamura, Titin Sakata and,
Jacquelyn Guitguiten

Others: Frederick Pablo, Director of Taxation
Suzanne Efhan, Department of Taxation
Randall S. Nishiyama, Dept. of the Attorney General
Mallory Fujitani, Department of Taxation
Ross Tsukenjo, State Senate
Ky Kano, Department of Taxation
Joshua Fujino, Department of Taxation
Lowell Kalapa, Hawaii Tax Foundation
Peter Fritz
Nandana Kalupahana, House Finance

CALL TO ORDER

Director Frederick Pablo called the meeting to order at 9a.m. with a quorum present.

INTRODUCE THE DEPARTMENT OF TAXATION (DOTAX) TAX REVIEW COMMISSION (TRC) STAFF AND THE MEMBERS OF THE TRC

Director Pablo mentioned that this is the first meeting for the TRC for 2010 to 2012. Director Pablo introduced himself and, said that he would preside over the meeting until a Chair and

Vice-Chair were selected, which would occur later in the meeting. He started off the meeting by introducing the DOTAX staff with whom the Members of the TRC would be working with: Johnnel Nakamura, TRC Co-Executive Director (Rules Officer); Donald Rousslang, TRC Executive Director (Acting Tax Research & Planning Officer); Titin Sakata, TRC Technical Coordinator; and, Jacquelyn Guitguiten, TRC Secretary.

Next, Director Pablo said DOTAX would make a series of presentations, providing background on the work it would perform to help the TRC carry out its mandate.

He said that after roll call, (since everybody was present and there was a quorum to start), he would cover communications to the TRC from the Legislature, the Sunshine Law (for which a representative from the Attorney General's Office, Mr. Randall Nishiyama, was present) the statutory provisions (to be explained by Ms. Johnnel Nakamura), the recommendations from the last TRC 2005-2007 (to be covered by Dr. Donald Rousslang) and, finally the election of the Chair and Vice-Chair for the 2010-2012 TRC. The nominations for the Chair would be taken from members (the nominations need not be seconded) and then voted on. A simple majority of the 7 members is needed. Nominees would be taken in which order they were nominated and voted on in that order.

After the Chair is selected, the Chair will take over the meeting and the Vice-Chair can be selected using the same procedures. After the selection of the Chair and the Vice-Chair there would be an Executive Meeting and everyone who is not with the TRC and its supporting staff would be asked to vacate the room. The Members of the TRC would discuss with Mr. Nishiyama during the Executive Meeting. Thereafter, the meeting would reconvene and the Chair would schedule the next meeting for the TRC.

Director Pablo asked the Members of the TRC to introduce themselves and to explain their views, objectives and visions for the work of the TRC to help the members select the Chair and Vice-Chair.

Statement of Mitchell A. Imanaka

"I'm a real estate lawyer. I have a law firm that focuses on real estate and labor law in the State of Hawaii. I've been practicing for 32 years. I feel very privileged and honored to be able to serve from this body and, I look forward to working toward the betterment of our state. Thank you and, I look forward to working with each of you."

Statement of Randall Y. Iwase

"I'm retired. I commend all of you for coming into town early--I forgot what it takes to come into town this early hour of the morning. I was formerly a Deputy Attorney General, Council Budget Chair; a State Senator; and the Chairman of the Labor Appeals Board. As I said, I'm happily retired and was asked to serve on this Commission to review the tax code at a time when the State is facing important issues, and to bring a fresh look at the code in light of the present needs and hopefully to make recommendations for the future of the State as we proceed. And so,

I look forward very much to working with this Commission and to producing a report which may be somewhat different in scope and vision from the reports of the previous two Tax Review Commissions."

Statement of Darryl K. Nitta

"I'm a CPA and, I work at Accuity, LLP, formerly, PricewaterhouseCoopers. I'm a Senior Tax Manager and I definitely look forward to working with everybody here as a team to come up with a report that the people of Hawaii and the Senators and Representatives can use to make decisions for our future."

Statement of Roy K. Amemiya, Jr.

"I'm President and CEO of 'Olelo Community Television; before that my career was in banking. I spent 20 years at Peter's Bank (Bank of Hawaii); 10 years at a competitive bank and I've spent 4 years as a City Budget Director. My vision for this Commission is that we look at taxes as not just a revenue-generating source for the State, but more broadly. Taxes should be fair, simple, and broad-based. They can help stimulate the economy of our State and perhaps help us with some of the social changes that we need to make in our community. As such, I really encourage us not just to look at what previous tax commissions have done but, to also look at what is being done elsewhere in the country as well as in some other countries around the World."

Statement of Michael T. McEnerney

"I'm a CPA with McEnerney, Shimabukuro, Okazaki & Fujita, CPAs, AAC, a local firm that has been around as an outgrowth of Alexander Grant and, now the Grant Thornton Company. I'm also an Attorney, Business Appraiser, Litigation Consultant and I taught taxation at the University of Hawaii, Chaminade University and to professionals, both CPAs and attorneys. I was very active in the Child Guidelines Committees for the State of Hawaii. I believe the Commission's statutory charge is to review the tax law for equity and efficiency and I have some very strong opinions about how taxes should be equal to all people -- with the same tax situation being taxed the same way. I'll give you two examples: if you have two people making \$160,000, in retirement income one of which is entirely social security and employer-funded retirement plans and the other is from employee-contributed savings, both of which pay the same federal tax, but the first individual pays zero state income tax even though both people live in Hawaii. Another example is the gross excise tax. To give you an example there, if I'm an insurance salesman and I sell an investment wrapped in an insurance policy, I pay less than half a percent excise tax on my commission. If I'm an investment advisor and I sell that investment directly, I pay 4.5% tax on my income. I have problems with that and I am concerned. Those are just two examples. In the area of efficiency, I will tell you that in over 30 years in dealing with the State Department of Taxation, they have gotten much, much better and, that's a lot of hard work on the part of the people here. But if you haven't done it before, I suggest you spend 15 or 20 minutes down on the 1st floor watching people go through the process in dealing with general excise, that would be very informative. If you don't prepare your own income tax returns for the State of Hawaii or the federal government, I wonder how you can really deal with the

issue of simplicity and efficiency. We pay people lots of money to do it. The average individual in Hawaii does their own tax returns. For a good example of efficiency, consider the federal government: if you have a domestic employee, you can use schedule H to pay withholding and unemployment tax as part of your quarterly estimated tax payments. However, for the State of Hawaii, you have to get a withholding tax license, you have to get a State unemployment tax license, and you have to get a TDI and a workman's comp, I'm not even considering the medical plan here. Streamlining to make things efficient--that's important to me. I'd also say that if you look at past Tax Review Commissions, a CPA has been the Chair and an Attorney has been the Vice-Chair. Whether you think that's good or that's bad, I think it simply reflects the fact that CPA's and Tax Attorney's spend a lot of time on detail of the tax laws. So, if you want to go in a completely different direction than in prior years, don't let a CPA be in charge."

Gregg M. Taketa

"I'm a partner in a CPA firm in Hilo, Hawaii. Taketa, Iwata, Hara & Associates, LLC. We've been a firm since 1983 and prior to that we were the Hilo Office of Peat Marwick Mitchell now known as KPMG. I am the past State President of the Hawaii Association of Public Accountants. I kind of share Mike's philosophy as far as horizontal equity--I think people in the same economic situation should be paying the same taxes. I'm in favor of trying to broaden the tax base while keeping the tax rates the same instead of increasing the rates. And, I'm looking at efficiency also but, there're certain challenges to that as well. That's basically my philosophy."

Peter S. Ho

"I am the Chairman, President and CEO at Bank of Hawaii. And, it's my privilege and honor to be working with all of you on this Commission. I'm probably the least versed in taxation so I will be doing a lot of listening and lending support. I happen to think that our community (not just economically but, in a lot of different areas), is deeply challenged. We find ourselves at a pivot point and taxation is an awfully important issue from a social standpoint; obviously also from an economic standpoint. My hope is that our work can help produce a better environment and outcome for the State."

Director Pablo thanked the Members of the Commission and said that they had a lot of great ideas and he could see that they were going to be a very productive TRC. He started by providing information for the TRC's consideration. The first item was House Resolution 218 entitled, "Requesting that the TRC conduct a study on the projected net loss to Hawaii residents in their federal tax liability that is attributable to the manner in which the state and county governments are currently funded".

The Resolution was a public document of which copies were provided. The members were told further information on the Resolution could be obtained from the Legislature.

The second item covered was the Sunshine Law. Director Pablo asked Mr. Nishiyama if he could provide the Members of the TRC an overview of the Sunshine Law.

Mr. Nishiyama referred to the Summary of Hawaii's Public Meeting Law, which said that absent any specific statutory exception all board business must be conducted in public. That means that the group cannot go into private and discuss things unless they have some exception, and a record must be taken of their actions. There are certain exceptions to public meeting requirement and one of them is that two board members can discuss board business outside of a meeting as long as no commitment is made or sought. Board members cannot discuss the same business with other board members in a series of meetings. TRC matters should be discussed at a properly noticed meeting. It makes things easier and avoids any challenges regarding whether they have conducted business in private. Finally, as board members they are allowed to discuss board business with non-board members. He said the hand-out was a good summary of their responsibilities. He suggested they take a couple of minutes to go through the hand-out and said he would be happy to answer any questions. He reminded everyone that board business should be conducted in public and that a written record of their deliberations be kept.

Director Pablo thanked Mr. Nishiyama.

Next, Ms. Nakamura covered some of the statutory provisions that govern the Tax Review Commission. Ms. Nakamura told the Members of the TRC that the Rules Office drafts the Administrative Rules, Tax Information Releases and the private letter rulings for DOTAX and that the Rules Office is also in charge of drafting and modifying all the tax forms. She said the duties of the Commission are to conduct a systematic review of the state's tax structure, using standards as equity and efficiency. She said they are tasked with providing a report to the Legislature 30 days prior to the convening of the Legislature that evaluates in the state's tax structure and makes recommendations regarding revenue and tax policies.

Director Pablo then turned to providing the Commission with information on its budget that was approved by the Legislature. Ms. Sakata notified the Members of the TRC that the Legislature has appropriated \$200,000 for fiscal year 2012 (which ends in June of 2012). She explained that in the past, the Commission spent the money on studies like outside consultants, travel, printing and, miscellaneous expenses. She said the Administrative Services Officer, Suzanne Eghan, would answer any questions they had on procurement and that when they enter into the Executive Session, Mr. Randall Nishiyama will provide them with the mechanics on how to request an extension. The report to the Legislature is due 30 days prior to the 2012 Legislative Session, which begins in 5 months. The decision whether to extend the deadline would affect the methods chosen to do the studies.

Mr. McEnerney asked Director Pablo whether the Members could get copies of the expenditures of prior Commissions. Director Pablo promised to provide the information.

Mr. Taketa asked if the Commission asked the Tax Office to do internal studies, would there be a charge for that--whether it would be charged against the \$200,000 budget.

Director Pablo responded that yes it would. If it's something that the Department could do with available staffing during its normal work hours, it would be charged to the Department's budget. Anything beyond that would be charged against the budget of the TRC.

Director Pablo thanked Ms. Sakata and moved to the recommendations from the 2005-2007 -- TRC that was convened, Dr. Rousslang said he would informally summarize the recommendations of the 2005-2007 TRC and gave a brief statement of actions taken in response to the recommendations.

The recommendations were as follows:

- 1) Streamlined Sales Tax Project -- Hawaii should support the exercise, but the TRC judged that it was premature to make a formal commitment. (There is no formal commitment yet.)
- 2) The high technology business investment tax credit should be changed to a grant program administered by a state agency. The Legislature should require data reporting by the hi-tech companies, including items such as their sales, employment and number of patents. (The credit has been allowed to expire. The data reporting was required by Act 206, SLH 2007.)
- 3) Tax credits should be minimized and subject to sunset dates.
- 4) Eliminate GET exemptions for nonprofit organizations. If not, require those organizations to obtain GET licenses. (A licensing requirement for taxpayers claiming GET exemptions was included in Act 155, SLH 2010.)
- 5) Hawaii should consider eliminating the individual income tax and should eliminate the corporate income tax.
- 6) The standard deduction and personal exemption should be indexed for inflation.
- 7) Hawaii should require withholding for nonresidents involved in pass-through entities, such as partnerships, S-corporations or LLCs.
- 8) Hawaii should raise the HARPTA withholding for real estate sales made by nonresidents.

Dr. Rousslang mentioned that recommendations of all past TRC's are summarized in Appendix I of the report of the 2005-2007 TRC. The Appendix shows which recommendations were repeated by successive Commissions and what actions were taken in response to the recommendations.

Dr. Rousslang said that the Office of Tax Research & Planning had an economist devoted full-time to producing economic studies for the 2005-2007 TRC. It also had four research statisticians with at least some time to devote to the TRC's work. He said the Office now has none of those resources. However, he said they would try to produce an updated report on tax adequacy, which has been a staple of previous TRC reports.

He said that fortunately he was able to get an unpaid intern from the University of Hawaii to help with that--but that otherwise the office's resources were very limited.

Mr. Iwase asked what the budget was for the previous TRC 2005-2007. Dr. Rousslang said the budget was for \$250,000. Mr. Iwase asked if the TRC was charged for the 9 studies that are in the Appendix of its report. Ms. Sakata stated that there was some overtime charged. Dr. Rousslang added that he was involved in some of the studies but, he wasn't involved in any of the budget matters.

Mr. Iwase asked whether that meant the current TRC had money and personnel resources than the previous TRC.

Director Pablo told the Commission Members that the Department can actually get that information for them from the prior Commission.

Mr. Ho asked if the Commission were able to secure pro-bono support from various service providers, would that have to go through the procurement process.

Ms. Ephan responded that volunteers do not. Volunteers sign up to a volunteer package including a non-disclosure agreement.

Director Pablo noted that what the TRC decides to study, is their decision.

He then moved on to the election of the Chair. After a Chair is elected, he will move to the selection of a Vice-Chair. Then, the Commission will go into the Executive Meeting and other items on the Agenda.

Mr. Nitta asked if it would be possible to talk about the extension of the report deadline prior to selecting the new Chair. Director Pablo said the report deadline would be covered in the Executive Meeting. He then opened the floor for nominations and noted that the nominations do not have to be seconded. He said the list of nominees would be voted on in the order they were presented.

Peter Ho nominated Randall Iwase for Chair.

Gregg Taketa nominated Michael McEnerney for Chair.

Director Pablo asked for a vote by showing of hands. The showing of hands for Randall Iwase was 5:

Mitchell Imanaka
Randall Iwase
Roy Amemiya, Jr.
Darryl Nitta
Peter Ho

Mr. Iwase was therefore elected as Chair.

Director Pablo passed the meeting to Mr. Iwase to conduct the selection for the Vice-Chair. Mr. Iwase thanked the members for the honor and privilege of serving as Chair and thanked Mr. Ho for the nomination.

Chair Iwase then moved to the nomination of the Vice-Chair.

Roy Amemiya, Jr. nominated Mitchell Imanaka for Vice-Chair

Gregg Taketa nominated Michael McEnerney for Vice-Chair

Chair Iwase asked for a vote by showing of hands. The showing of hands for Mitchell Imanaka were:

Randall Iwase
Mitchell Imanaka
Roy Amemiya, Jr.
Peter Ho

The showing of hands for Michael McEnerney were:

Gregg Taketa
Darryl Nitta
Michael McEnerney

Mitchell Imanaka was therefore elected as Vice-Chair.

Chair Iwase announced that the TRC would now go into the Executive Session.

Director Pablo said the Executive Session was for the TRC Members and the supporting staff (the 4 persons that he had previously indicated). Everybody else, including himself, left until the Executive Session ended.

EXECUTIVE SESSION MEETING, PURSUANT TO SECTION 92-5(a)(8), HAWAII REVISED STATUTES

At this time, the Chair adjourned to go into an Executive Session at 9:32 a.m.

The TRC meeting reconvened at 9:54 a.m.

CALL TO ORDER - Reconvene

Chair Iwase called the meeting to order at 9:54 a.m. Chair Iwase asked for a motion to amend the agenda, which required two-thirds vote in the affirmative, to request the Director of Taxation

to submit legislation at the next Legislative Session to extend the deadline to submit the report by the Commission to the year 2012 and to request additional funds.

It was moved by Mr. Imanaka and seconded by Mr. Ho to amend the agenda to request the Director of Taxation to submit legislation at the next Legislative Session. The motion was carried unanimously.

Mr. Imanaka then moved to request the Director of Taxation to submit legislation at the next Legislative Session to extend the deadline to submit the Commission's report from 2011 to 2012 and to request additional funding. Mr. Ho seconded the motion. The motion carried unanimously.

Chair Iwase asked the members to submit their agenda requests the week of July 18th.

ADJOURNMENT

The meeting was adjourned at 10:06 a.m. The next meeting was scheduled for Thursday, August 4, 2011 from 8:30 a.m. to 10 a.m. Ms. Sakata was asked to secure Rooms 310-313 for the next meeting and to send out an email to notify TRC members and TRC staff.