

SB22

Measure Title: RELATING TO TAXATION.

Report Title: Conveyance Tax; Sale of Stock

Description: Clarifies that the sale, transfer, or exchange of a legal entity's stock, whose assets include realty located in Hawaii, shall be deemed to be a transfer or conveyance of realty that is subject to the conveyance tax when the sale, transfer, or exchange of stock is executed with an unrelated entity or individual.

Companion:

Package: None

Current Referral: CPN, WAM

Introducer(s): GABBARD, Ige, Ihara

<u>Sort by Date</u>		Status Text
1/17/2013	S	Introduced.
1/17/2013	S	Passed First Reading.
1/17/2013	S	Referred to CPN, WAM.
1/24/2013	S	The committee(s) on CPN has scheduled a public hearing on 01-30-13 8:30AM in conference room 229.



**Testimony to the Senate Committee on Commerce and Consumer Protection
Wednesday, January 30, 2013
8:30 a.m.
State Capitol - Conference Room 229**

RE: SENATE BILL NO. 22, RELATING TO TAXATION

Chair Baker and Vice Chair Galuteria, and members of the committee:

The Chamber of Commerce of Hawaii **opposes** S.B. No. 22. The bill proposes to clarify that the selling, transfer, or exchange of a legal entity's stock, whose assets include realty located in Hawaii, shall be deemed to be a transfer or conveyance of realty that is subject to the conveyance tax when the sale, transfer, or exchange of the stock is executed with an unrelated entity or individual.

The Chamber is the largest business organization in Hawaii, representing more than 1,000 businesses. Approximately 80% of our members are small businesses with less than 20 employees. As the "Voice of Business" in Hawaii, the organization works on behalf of its members, which employ more than 200,000 individuals, to improve the state's economic climate and to foster positive action on issues of common concern.

This bill would amend HRS § 247-1 to specify that the sale or transfer of stock by a legal entity or individual that owns or leases realty in the State or has a controlling interest in the realty to an unrelated entity or individual, to the extent that the sale or transfer of stock reflects changes in ownership or control of the realty, shall be deemed a transfer or conveyance of an interest in the realty for purposes of subsection (a) and taxed accordingly.

We are deeply concerned by the manner in which the Conveyance Tax has been and is being applied. There is no rational nexus between the real estate transactions that are being taxed at conveyance, and the uses identified in HRS 247 as the beneficiaries of the tax. It appears that the legislation is targeting transactions involving the sale of interests in entities that have ownership over real property in the state due to the recent sales or changes of ownership of private holdings.

The Conveyance Tax was created to cover the administrative costs of recording the real estate transactions, such as those performed by the Bureau of Conveyance. With the recent amendments to the statutes, the conveyance tax is deposited into the general fund with the following allocations:

1. Ten per cent shall be paid into the land conservation fund established pursuant to section 173A-5;

2. Twenty-five per cent from July 1, 2009, until June 30, 2012, and thirty per cent in each fiscal year thereafter shall be paid into the rental housing trust fund established by section 201H-202; and
3. Twenty per cent from July 1, 2009, until June 30, 2012, and twenty-five per cent in each fiscal year thereafter shall be paid into the natural area reserve fund established by section 195-9; provided that the funds paid into the natural area reserve fund shall be annually disbursed by the department of land and natural resources in the following priority:
 - a. To natural area partnership and forest stewardship programs after joint consultation with the forest stewardship committee and the natural area reserves system commission;
 - b. Projects undertaken in accordance with watershed management plans pursuant to section 171-58 or watershed management plans negotiated with private landowners, and management of the natural area reserves system pursuant to section 195-3; and
 - c. The youth conservation corps established under chapter 193.

We do not believe that the conveyance tax is being used in an appropriate manner. The proposed bill only exacerbates the current problem. We suggest that these beneficiaries be funded from other means more closely related to their purposes

Thank you for the opportunity to express our views on this matter.

**Testimony Before The Senate Committee On
Commerce and Consumer Protection**

Senate Bill No. 22

January 30, 2013

By
Lon Okada
Manager, Corporate Taxes
Hawaiian Electric Industries, Inc.

Chair Baker, Vice Chair Galuteria and Members of the Committee:

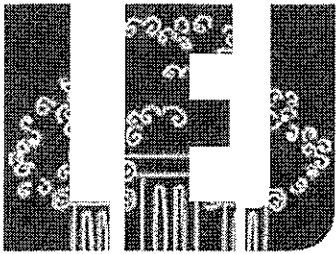
Hawaiian Electric Industries, Inc., Hawaiian Electric Company, Inc., Maui Electric Company, Limited and Hawaii Electric Light Company, Inc. are opposed to Senate Bill No. 22 ("SB 22"). This bill imposes the conveyance tax on the sale or transfer of a legal entity's or individual's stock (where the entity or individual owns, leases or has a controlling interest in realty in the state of Hawaii) to an unrelated entity or individual, to the extent that the sale or transfer of stock reflects changes in ownership or control of the realty.

SB 22, as currently worded, appears ambiguous and over-broad. At the extreme, the bill could be interpreted to impose a conveyance tax on: 1) an individual's sale or transfer of 1 share of common stock to another unrelated individual or 2) a company's sale of common stock to underwriters in a public offering of common stock.

The bill casts a wide net since the law defines the taxpayer population to which the conveyance tax would apply but does not appear to limit or provide a threshold for the amount of value sold or transferred. In the bill, §274-1(b) defines the stock transaction subject to the tax by providing "...to the extent that the sale or transfer of stock reflects changes in ownership or control of the realty." As pointed out in the above examples, the conveyance tax could apply to any share transfer which represents a change in the ownership interest in the underlying realty, however small. The broad scope creates a compliance nightmare, which we do not believe was intended.

SB 22 also provides that if the value of the realty transferred or conveyed cannot be determined from the value of the stock, then the conveyance tax will be based on the greater of 1) the appraised value of the realty or 2) the consideration paid for the stock. The latter alternative may not be indicative of the realty value and place an unfair tax burden on the transaction, especially in cases where the company whose shares are sold may own realty representing a very small portion of its total assets. In this case, the base on which the tax would be imposed would bear no relationship to realty value and would be inconsistent with the intent and methodology of the statute.

Thank you for the opportunity to testify in opposition to SB 22.



David Derauf, M.D.
Marc Fleischaker, Esq.
Naomi C. Fujimoto, Esq.
Patrick Gardner, Esq.
Francis T. O'Brien, Esq.
David J. Reber, Esq.

Victor Geminiani, Esq.

Testimony of Hawai'i Appleseed Center for Law and Economic Justice
Supporting SB 22 Relating to Taxation
Senate Committee on Commerce and Consumer Protection
Wednesday, January 30, 2013, 8:30 AM, Room 229

Thank you for an opportunity to testify on SB 22, which would subject to the conveyance tax any real property included in transfers of controlling interests in an entity. We strongly support this bill although we also urge an amendment that provides an exemption for affordable housing developments.

Hawai'i Appleseed Center for Law and Economic Justice is a nonprofit, 501(c)(3) law firm created to advocate on behalf of low income individuals and families in Hawai'i on civil legal issues of statewide importance. Our core mission is to help our clients gain access to the resources, services, and fair treatment that they need to realize their opportunities for self-achievement and economic security.

Ensuring that any controlling interest transfers involving real property are subject to the conveyance tax like any other sale of property is a matter of fairness. Our land is particularly precious in Hawai'i, and all transfers of real property should be recognized as such. We lost six million dollars in conveyance tax revenue when Lanai was sold because of what is essentially a loophole in the conveyance tax. In addition, it is possible that some transfers of real estate are structured as transfers of controlling interests in businesses avoid paying the conveyance tax.

The conveyance tax funds both affordable housing through the Rental Housing Trust Fund and important state initiatives that protect our environment. Conveyance tax revenues are the only dedicated source of funding for the Rental Housing Trust Fund, a critical tool in the creation of affordable housing. In the next four years, Hawai'i will need 13,000 more units to meet the need for affordable rentals. As a result of this shortfall, families struggle to keep themselves housed, and may even find themselves homeless. The Rental Housing Trust Fund has helped to create over 4,250 units, significant progress in addressing our need for housing. Increasing conveyance tax revenues by equitably taxing all real property transfers will help increase the availability of funds to this program.

We also wish to emphasize that calculating the appropriate amount of conveyance tax will not be unduly burdensome. Neither the stock transfer nor the value of the business is being assessed, but simply the value of the property that is being transferred within the larger sale. The bill provides two clear methods of assessment should it not be possible to determine the value of the realty based on the value of the stock or interest transferred: either the "most recent assessed appraised value" or the "amount of consideration paid for the stock transfer," whichever is greater.

The committee may wish to consider another option, basing the value of the realty on the lesser of a recent qualified appraisal, if available, or the current county real property tax assessed value. The valuation has three main advantages: 1) it focuses on the realty itself, which is the subject of the tax, not on the overall value of the stock or the business; 2) it gives the seller the option of having the realty appraised or relying on the county's assessed value; and 3) it offers the Department of Taxation a clear and fair external means of determining the property's value.

To ensure that this bill does not disincentivize the creation of affordable housing, we strongly urge an amendment stating that this chapter shall not apply to "any transfer from a limited partner to a general partner of a limited partnership that owns an affordable rental housing project for which low-income housing tax credits have been issued under section 235-110.8 or 241-4.7 or section 42 of the Internal Revenue Code of 1986 as amended." The funding structure used to develop affordable housing may require transactions that would be subject to the conveyance tax under this bill if no exemption is established. To tax these affordable housing conveyances may well have the unintended effect of discouraging affordable housing development, a consequence that runs counter to our state's housing priorities.

THE TRUST *for* PUBLIC LAND

CONSERVING LAND FOR PEOPLE

**THE TRUST FOR PUBLIC LAND'S TESTIMONY
IN SUPPORT OF AN AMENDMENT OF SB 22 RELATING TO TAXATION**

Senate Committee on Commerce & Consumer Protection

Wednesday, January 30, 2013, 8:30 AM, Room 229

The Trust for Public Land supports SB 22, with suggested amendments exempting affordable housing rental projects included in The Nature Conservancy's testimony. We believe this bill appropriately closes a major loophole to the conveyance tax on transfers of real estate – real estate transferred via a majority stock transfer.

Only sophisticated and wealthy individuals can afford to take advantage of the current loophole by forming corporations or limited liability companies that “own” real estate, and then transferring the stock ownership of the company to transfer ownership of the real estate. For example, although real estate worth hundreds of millions of dollars on Lana'i was sold last year to billionaire Larry Ellison, no real estate conveyance taxes were collected because of this stock transfer loophole.

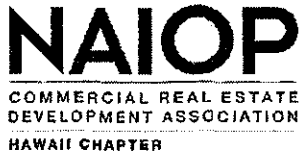
Under HRS §247-7, a portion of conveyance tax revenue has been appropriately used for land preservation and forested watershed conservation via the Land Conservation Fund and the Natural Area Reserve Fund (another portions is directed to the Affordable Housing Rental Trust Fund). Since the development and sale of real estate puts pressure on our natural resources like fresh water and our watersheds, it makes sense to spend a portion of conveyance tax revenue on protecting those natural resources.

Although the Trust for Public Land supports this bill, I will not be able to appear in person to testify due to a scheduling conflict.

Mahalo for this opportunity to testify -



Lea Hong
Hawaiian Islands State Director
1136 Union Mall, Suite 202
524-8563 (office), 783-3653 (cell)



January 28, 2012

The Hon. David Y. Rosalyn H. Baker, Chair, and
Members of the Senate Committee on
Commerce and Consumer Protection

Re: Testimony in **Opposition** to S.B. Bill No. 22, Relating to Taxation
Hearing Date and Time: 8:30 a.m., January 30, 2013
Conference Room 229, Hawaii State Capitol

Dear Chair Baker and Members of the Committee:

I am submitting this testimony on behalf of NAIOP Hawaii in **strong opposition** to S.B. No. 22. We are the Hawaii chapter of NAIOP, the Commercial Real Estate Development Association, which is the leading national organization for developers, owners and related professionals in office, industrial and mixed-use real estate. The local chapter comprises property owners, managers, developers, financial institutions and real estate related professionals who are involved in the areas of commercial and industrial real estate in the State of Hawaii.

NAIOP Hawaii has submitted testimony to the Legislature since the 1990s, voicing its concerns regarding the potential misuse of the conveyance tax. Unfortunately, the concerns voiced by NAIOP over the years have largely come to fruition, through radical increases in rates of the tax, diversion of tax revenues into areas totally unrelated to the conveyance tax, and now, attempts to expand the tax beyond real estate transfers.

The purpose of the conveyance tax was to cover the costs of running the Bureau of Conveyances. (Long-timers in the Legislature may remember that, years ago, the debate every year was whether there should be an increase in the tax to cover a "new computer system" and "automation" for the Bureau.) It was never intended to be a revenue-generating tax. However, over time various non-conveyance uses for the conveyance tax revenue have been proposed and implemented by the Legislature. All of these causes might be worthy, such as protection of the NARS system or facilitating affordable housing, but as NAIOP consistently testified, were never intended to be supported by the conveyance tax.

The rates of the tax have also been increased dramatically. At this point it has become a punitive surtax on many real estate transactions. It is no longer a conveyance tax but a type of capital gains tax surcharge. However, it is more onerous than a true capital gains tax, because not just the gain on the transfer is taxed, but instead the entire face value of the transaction. And it is a hidden tax, because it only shows up as a expense line item on a closing statement.

Now, S.B. No. 22 and a number of similar bills introduced into the Legislature would tax not only transfers of real estate, but also the transfers of stock of entities that own real estate in

The Hon. Rosalyn H. Baker and Members of the Senate Commerce and Consumer Protection
Committee
January 28, 2013
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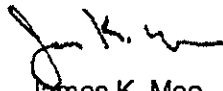
Hawaii. This is clearly beyond the scope of what the conveyance tax was ever intended to cover. And since an income tax is likely already being imposed on the stock sale, there is now double-taxation being levied by the State on the same money.

If the Legislature wants to impose a new surcharge tax on transfers of stock, it should do so by enacting a new tax. But it is not honest to claim it is just taxing a "conveyance," because a stock transfer is not a conveyance and was never intended to be covered by this tax.

If these measures become law, they will reinforce the negative image Hawaii has as a place to do business.

Thank you for the opportunity to testify on this measure. We would urge that it be held in committee.

Respectfully,



James K. Mee
Chair, Legislative Affairs Committee

BIA-HAWAII

BUILDING INDUSTRY ASSOCIATION

"Building Better Communities"

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JW, Inc.

Ryan Engle
Bays Lung Rose & Holma

Scotty Anderson
Pacific Rim Partners

W. Bruce Barrett
Castle & Cooke Homes Hawaii, Inc.

Testimony to the Senate Committee on Commerce and Consumer Protection

Wednesday, January 30, 2013

8:30 a.m.

State Capitol - Conference Room 229

RE: SENATE BILL NO. 22, RELATING TO TAXATION

Dear Chair Baker, Vice-Chair Galuteria, and members of the committee:

My name is Gladys Marrone, Director of Government Relations for the Building Industry Association of Hawaii (BIA-Hawaii), the voice of the construction industry. BIA-Hawaii promotes its members through advocacy and education, and provides community outreach programs to enhance the quality of life for the people of Hawaii. BIA-Hawaii is a not-for-profit professional trade organization, chartered in 1955, and affiliated with the National Association of Home Builders.

BIA-Hawaii is **opposed** to S.B. 22, Relating to Taxation. The bill proposes to clarify that the selling, transfer, or exchange of a legal entity's stock, whose assets include realty located in Hawaii, shall be deemed to be a transfer, or conveyance of realty, that is subject to the conveyance tax when the sale, transfer, or exchange of the stock is executed with an unrelated entity or individual.

This bill would amend HRS §247-1 to specify that the sale or transfer of stock by a legal entity or individual that owns or leases realty in the State or has a controlling interest in the realty to an unrelated entity or individual, to the extent that the sale or transfer of stock reflects changes in ownership or control of the realty, shall be deemed a transfer or conveyance of an interest in the realty for purposes of subsection (a) and taxed accordingly.

We are deeply troubled by the manner in which the conveyance tax has been, and is, being applied. There is no rational nexus between the real estate transactions that are being taxed at conveyance, and the uses identified in HRS §247 as the beneficiaries of the tax.

The conveyance tax was created to cover the administrative costs of recording real estate transactions, such as those performed by the Bureau of Conveyance. With the recent amendments to the statutes, the conveyance tax is deposited into the general fund with the following allocations:

1. Ten per cent shall be paid into the land conservation fund established pursuant to section 173A-5;

Mailing address: P.O. Box 970967, Waipahu, HI 96797 Street address: 94-487 Akoki St., Waipahu, HI 96797-0967;
Telephone: (808) 847-4666 Fax: (808) 440-1198 E-mail: info@biahawaii.org; www.biahawaii.org

1. Twenty-five per cent from July 1, 2009, until June 30, 2012, and thirty per cent in each fiscal year thereafter shall be paid into the rental housing trust fund established by section 201H-202; and
2. Twenty per cent from July 1, 2009, until June 30, 2012, and twenty-five per cent in each fiscal year thereafter shall be paid into the natural area reserve fund established by section 195-9; provided that the funds paid into the natural area reserve fund shall be annually disbursed by the department of land and natural resources in the following priority:
 - a. To natural area partnership and forest stewardship programs after joint consultation with the forest stewardship committee and the natural area reserves system commission;
 - b. Projects undertaken in accordance with watershed management plans pursuant to section 171-58 or watershed management plans negotiated with private landowners, and management of the natural area reserves system pursuant to section 195-3; and
 - c. The youth conservation corps established under chapter 193.

We do not believe that S.B 22 proposed to utilize the conveyance tax in an appropriate manner. The proposed bill only exacerbates the current problem. BIA-Hawaii is **opposed** to this measure.

Thank you for the opportunity to express our views on this matter.



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**SB 22
RELATING TO TAXATION**

**PAUL T. OSHIRO
MANAGER – GOVERNMENT RELATIONS
ALEXANDER & BALDWIN, INC.**

JANUARY 30, 2013

Chair Baker and Members of the Senate Committee on Commerce & Consumer Protection:

I am Paul Oshiro, testifying on behalf of Alexander & Baldwin, Inc. (A&B) on SB 22, "A BILL FOR AN ACT RELATING TO TAXATION."

On July 1, 2012, Alexander & Baldwin completed the implementation of a plan to separate itself into two independent, publicly traded companies. One company consists of A&B's real estate and agriculture businesses, and retained the Alexander & Baldwin name and the other company consists of A&B's ocean transportation and logistics businesses, which operates under the Matson name. The A&B corporate separation resulted in two financially strong public companies for Hawaii, each with more than a billion dollars in assets and over a thousand employees. And each A&B shareholder received a share of stock in each of the two companies. Both A&B and Matson remain fully committed to meeting the needs of Hawaii for many generations to come.

In order to complete the separation of the two A&B companies in a manner that was most efficient (i.e. least amount of time, administrative burden, costs), we utilized a process that consisted of transfers and mergers involving companies that may be considered "unrelated" for the purposes of this bill. Should the provisions in this bill be

enacted and implemented retroactive to June 1, 2012, we believe that the transfers and mergers that we utilized to effectuate our company separation may be subject to the provisions of this bill and may be required to pay the conveyance tax on these transactions.

Should your Committee decide to pass this bill, we respectfully request that the provisions of this bill be implemented prospectively.

Thank you for the opportunity to testify.



Housing Hawaii

Advocating Creating Maintaining Affordable Housing

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Director – Gregg

Robertson, Robertson
& Company, LLC


Testimony of Housing Hawaii
Supporting SB 22 Relating to Taxation
Senate Committee on Commerce and Consumer Protection
Wednesday, January 30, 2013, 8:30 AM, Room 229

Chair Baker, Vice Chair Galuteria and Members of the Senate Committee on Commerce and Consumer Protection, thank you for an opportunity to testify in support on SB 22, which would subject to the conveyance tax any real property included in transfers of controlling interests in an entity. Housing Hawaii strongly supports this bill although we also urge an amendment that provides an exemption for affordable housing developments.

The conveyance tax funds both affordable housing through the Rental Housing Trust Fund and important state initiatives that protect our environment. Conveyance tax revenues are the only dedicated source of funding for the Rental Housing Trust Fund, a critical tool in the creation of affordable housing. In the next four years, Hawai'i will need 13,000 more units to meet the need for affordable rentals. As a result of this shortfall, families struggle to keep themselves housed, and may even find themselves homeless. The Rental Housing Trust Fund has helped to create over 4,250 units, significant progress in addressing our need for housing. Increasing conveyance tax revenues by equitably taxing all real property transfers will help increase the availability of funds to this program.

To ensure that this bill does not have a negative impact on the creation of affordable housing, we strongly urge an amendment stating that this chapter shall not apply to "any transfer from a limited partner to a general partner of a limited partnership that owns an affordable rental housing project for which low-income housing tax credits have been issued under section 235-110.8 or 241-4.7 or section 42 of the Internal Revenue Code of 1986 as amended." The funding structure used to develop affordable housing may require transactions that would be subject to the conveyance tax under this bill if no exemption is established. To tax these affordable housing conveyances may well have the unintended effect of discouraging affordable housing development; a consequence that runs counter to our state's housing priorities.

Sincerely,



Kevin R. Carney, NAHP-c
President

Housing Hawaii, 841 Bishop Street, Suite 2208, Honolulu, HI 96813

Phone: 808-523-8826

www.housinghawaii.org

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Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: CONVEYANCE, Clarify imposition on sale, transfer or exchange of stock

BILL NUMBER: SB 22

INTRODUCED BY: Gabbard and 2 Democrats

BRIEF SUMMARY: Amends HRS section 247-1 to provide that the sale or transfer of stock by a legal entity or individual that owns or leases realty in the state or has a controlling interest in the realty to an unrelated entity or individual, that reflects changes in ownership or control of the realty, shall be deemed a transfer or conveyance and subject to the conveyance tax. If the value of the realty transferred or conveyed cannot be determined from the value of the stock transferred, then the conveyance tax shall be based upon the most recent assessed appraised value of the realty or the amount of consideration paid for the stock transfer, whichever is greater.

Defines “controlling interest” and “unrelated entity or individual” for purposes of the measure.

EFFECTIVE DATE: Retroactively to sales or transfers of stock occurring after June 1, 2012

STAFF COMMENTS: It appears that the proposed measure would clarify that any sale, transfer or exchange of a legal entity’s stock that involves a change in ownership of any realty included in the sale, transfer, or exchange of such stock, whichever is greater, would be subject to the conveyance tax.

It should be noted that the current conveyance tax was never established to be a source of revenue. Only in recent years as lawmakers sought to fund their favorite programs did the conveyance tax come under fire as a way to raise new sources of revenue to fund favored programs. Rather than reining in spending, lawmakers keep searching for new revenue streams and now attempt to subject transfers of real property included in the transfer of stock to the conveyance tax.

While it appears that the value of the realty associated with the transfer of stock could not be determined at the time of the transfer, the measure states that the conveyance tax shall be based on whichever is greater - the amount of the most recent appraised value of the realty or the amount of consideration of the stock transfer. If the conveyance tax is then imposed on the value of realty transferred since the value of the realty is in excess of the value of the stock transfer, then under the proposed measure the transfer of stock will not be subject to the conveyance tax. In addition, the imposition of the conveyance tax on these “incidental” transfers of realty may add another nail in the economic coffin of Hawaii as it is just one more cost that an investor must weigh in deciding whether or not the return on an investment in Hawaii is attractive or reasonable.

It should be remembered that the conveyance tax was initially enacted by the 1966 legislature after the repeal of the federal law requiring stamps for transfers of real property. It was enacted for the sole purpose of providing the department of taxation with additional data for the determination of market value of properties transferred. This information was also to assist the department in establishing real

SB 22 - Continued

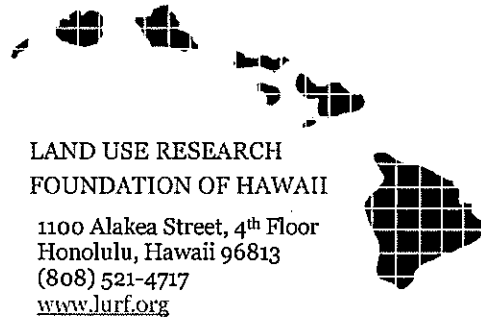
property assessed values and at that time the department stated that the conveyance tax was not intended to be a revenue raising device. The conveyance tax is imposed each time property changes title or ownership. However, over the years the tax has been increased and conveyance tax revenues have been tapped to provide revenue for the land conservation fund, rental housing trust fund, and the natural area reserve fund.

The issue that this proposal attempts to address is a problem of lawmakers' own making. When the conveyance tax was last increased, lawmakers attempted to "milk" owners of luxury properties of a million dollars or more, imposing the highest rates of the conveyance tax on those transfers and in particular the transfer of residential property that was not going to be owner occupied. Perhaps unintended but indeed caught in the crossfire are commercial properties and residential rental properties of any substantial value such as an apartment complex. The highest rates of the conveyance tax are imposed on these transfers which can amount to hundreds of thousands if not millions of dollars.

As a result of several major commercial transactions, one of which this measure attempts to capture with its retroactive effective date, companies that owned real property were sold as the corporate entity and therefore avoided a conveyance of the real property that would have been subject to the conveyance tax. But again, a proposal like this also ignores the reality that a sale of a business does not always mean an attempt at avoiding the conveyance tax but, if adopted, this proposal would impose the tax on the sale of the company that was purchased for its good will or products and not its realty. For example, the sale of a longtime producer of baked goods included the plant where the bread was made. However, the value of the company was really its products and the good reputation it had in the community. Would this proposal be imposed because the sale of the company included taking over the facility where the production of the bread was done? Care should be exercised in this rush of avarice on the part of state lawmakers.

Inasmuch as it appears that this measure is proposed as another "cash grab" so that lawmakers will not have to deal with the bleeding state checkbook, its adoption cannot be justified.

Digested 1/25/12



January 28, 2013

Senator Rosalyn H. Baker, Chair
Senator Brickwood Galuteria, Vice Chair
Senate Committee on Commerce and Consumer Protection

Testimony in Strong Opposition to SB 22 Relating to Conveyance Tax (Sale of Stock).

Wednesday, January 30, 2013, 8:30 a.m., in CR 229

The Land Use Research Foundation of Hawaii (LURF) is a private, non-profit research and trade association whose members include major Hawaii landowners, developers and a utility company. LURF's mission is to advocate for reasonable, rational and equitable land use planning, legislation and regulations that encourage well-planned economic growth and development, while safeguarding Hawaii's significant natural and cultural resources, and public health and safety.

SB 22. This bill proposes to impose the conveyance tax on the transfer of a controlling interest of an entity with an interest in real property, however, stipulates that the imposition of the conveyance tax on transfers of entity ownership shall not apply to any transfer of interest or acquisition between entities wholly owned by the same common ownership that results in no change in beneficial ownership.

LURF's Position. LURF recognizes the stated intent of this bill, which is to clarify that the selling, transfer, or exchange of a legal entity's stock, whose assets include Hawaii realty, shall be deemed to be a transfer of realty that is subject to the conveyance tax when the sale or transfer of stock is executed with an unrelated entity or individual. However, based on the following reasons and considerations, LURF opposes SB 22, and must request that this bill be held in Committee.

The proposed imposition of the conveyance tax on transfers of controlling interests in entities is inappropriate and improper given that:

- 1. The proposed bill applies retroactively, thereby raising significant constitutional issues.** Through its retroactive application, SB 22 would arguably violate the Contract Clause of the United States Constitution by altering the terms of existing sale, transfer or conveyance agreements which may have already been negotiated between the parties to the conveyance, and attempting to change contractual obligations, to their detriment.

Such changes are unconstitutional and illegal as they may result in substantial and severe impairment of contracts by depriving the parties of important rights and opportunities afforded under those prior contracts, and destroying their contractual expectations and relationships without significant and legitimate public purpose.

- 2. The Hawaii Conveyance Tax was never intended as a revenue-generating tax.** Hawaii Revised Statutes (“HRS”), Chapter 247 (Conveyance Tax), was purposefully enacted in 1966 to provide the State Department of Taxation (“DoTax”) with informational data for the determination of market value of properties transferred, and to assist the DoTax in establishing real property assessed values. In short, the sole intent of the conveyance tax was originally to cover the administrative costs of collecting and assessing said informational data, which necessarily entails the recording of real estate transactions, as performed by the Bureau of Conveyances.

Since the enactment of HRS Chapter 247, however, the State Legislature has proposed, and has successfully implemented changes to the law 1) to allow application of conveyance tax revenue to a number of non-conveyance type uses (land conservation fund; rental housing trust fund; and natural area reserve fund) to the point where there is no longer any clear nexus between the benefits sought by the original Act and the charges now proposed to be levied upon property-holding entities transferring ownership; and 2) also to increase the tax rates to the point where said revenues now appear to far exceed the initially stated purpose of the Act.

These expansions and deviations which go beyond the scope of the original intent of the conveyance tax law are concerning since the proposed bills, particularly if unlawfully targeting recent transactions involving the sale of interests in private entities which own real property in the State, could be characterized as imposing an improper penalty, hidden tax, or surcharge, which may be subject to legal challenge.

- 3. Transfers of stock are not “conveyances” of real property, and rightfully should not be made subject to the conveyance tax law.** The proposed bill would inappropriately subject sales of controlling interests in an entity regardless of whether real estate may be the primary or largest asset owned by the entity. Given that transfers of stock are not conveyances of real property, and given the clear intent underlying HRS Chapter 247, the methods sought to be used to impose a tax on transfers of stock (i.e., amendment or expansion of the existing conveyance tax law) is improper.
- 4. This bill may have unintended consequences,** especially to our island families who own large properties and may want to transfer property within their family. The measures will also have major negative consequences for many of Hawaii’s large *kama`aina* landowners who may be transferring large properties for agricultural farms, housing developments, environmental programs, or other developments which would serve the community and create needed employment.
- 5. This proposed measure creates a significant disincentive for business in Hawaii.** At a time where Hawaii is attempting to encourage business expansion in, and attract business operations to Hawaii, HB 386 and HB 680 actually create a disincentive, and will have a substantial negative impact on persuading new and existing businesses to open or expand in Hawaii, or to relocate their operations to this State. The proposed additional cost of doing business in Hawaii as a result of these bills would certainly

appear to negatively outweigh any positive revenue impact resulting from the imposition of conveyance taxes pursuant to the measures.

6. The imposition of conveyance tax as proposed by this bill will drive up the cost of lands for agricultural production, affordable and market homes, and commercial development.

- The proposed imposition of the conveyance tax on transfers which affect **agricultural lands** will be passed on to farmers and other agricultural operators, making it even harder for agriculture to survive in Hawaii.
- The proposed imposition of the conveyance tax on transfers which affect **land intended for housing developments** will be passed on to home buyers, will increase the price of homes, and will exacerbate the affordable housing problem in Hawaii.
- The proposed imposition of the conveyance tax onto transfers which affect **commercial properties** will also be passed on to small businesses, creating yet another substantial financial burden on them.

7. Proper and effective implementation of the proposed bill would involve complex, time-consuming, and subjective determinations. As a practical matter, in order that the proposed measure be properly and effectively administered and enforced, a number of determinations must be made pursuant to rules adopted by the DoTax director. These determinations may necessarily include the value of the realty being transferred as a result of the transfer (which would be difficult to ascertain in the case of a stock transfer as other assets in addition to real estate may be conveyed as part of the sale), and whether persons may be acting in concert for the purpose of effectuating the transfer. These types of determinations may involve complex inquiries, involving assessments of subjective issues and value which entail significant time and expense.

For the reasons stated above, LURF respectfully recommends that **SB 22 be held in this Committee.**

Thank you for the opportunity to provide testimony strongly opposing this proposed measure.

Testimony of The Nature Conservancy of Hawai'i
Supporting with Amendments S.B. 22 Relating to Taxation
Senate Committee on Commerce and Consumer Protection
Wednesday, January 30, 2013, 8:30AM, Room 229

The Nature Conservancy of Hawai'i is a private non-profit conservation organization dedicated to the preservation of the lands and waters upon which life in these islands depends. The Conservancy has helped to protect nearly 200,000 acres of natural lands in Hawai'i. Today, we actively manage more than 32,000 acres in 10 nature preserves on Maui, Hawai'i, Moloka'i, Lāna'i, and Kaua'i. We also work closely with government agencies, private parties and communities on cooperative land and marine management projects.

The Nature Conservancy supports S.B. 22. We think it is reasonable that, like direct transfers of real estate via purchase and sale agreements, transfers of real estate via majority stock transfers should also be subject to the State's real estate conveyance tax. We do, however, support amendments that would provide exemptions for real estate transfers between subsidiaries of the same parent entity, and between partners in qualified affordable rental housing developments.

We also think it is important to be clear in this measure that it is neither the value of stock nor the value of the business that is being assessed the conveyance tax, but the value of the realty that is a component of the stock transfer. We note that this bill includes a proposed provision (§247-1(b)) detailing options for valuing the real property based on the county tax assessed value or the amount paid for the stock. **We think a preferred option would be to base the real estate valuation on the lesser of the county tax assessed value or a recent qualified appraisal, e.g.:**

"The conveyance tax shall be based upon the lesser of the most recent county real property tax assessed value of the realty or, if available, a current qualified appraisal by a licensed real estate appraiser in the State of Hawaii."

In this way, the valuation (1) focuses on the subject of the tax—the realty itself—not on the overall value of the stock or the business; (2) provides the seller the option of getting an appraisal on the realty or relying on the county tax assessed value; and (3) offers the tax department an appropriate external means of determining valuation.

Also, we believe it may be helpful to specifically note a reporting requirement for stock transfers that affect realty, and we recommend an amendment to HRS §247-6 like the following:

"§247-6 Certificate of conveyance required. (a) Any party, with the exception of governmental bodies, agencies, or officers, to a document or instrument subject to this chapter, or the party's authorized representative, shall file, in the manner and place which the director of taxation shall prescribe, a certificate of conveyance setting forth the actual and full consideration of the property transferred, or the value of the property transferred by way of the transfer of a controlling interest as that term is used in section 247-A, including any lien or encumbrance on the property, and any other facts as the director may by rules prescribe. The certificate of conveyance shall be verified by a written declaration thereon that the statements made therein are subject to the penalties in section 231-36. The certificate shall be appended to the document or instrument made subject to this chapter and shall be filed with the director simultaneously with the aforementioned document or instrument for the imprinting of the required seal or seals.

Under HRS §247-7, a portion of conveyance tax revenue has been appropriately used for land preservation and forested watershed conservation via the Land Conservation Fund and the Natural Area Reserve Fund, respectively. The development and sale of real estate helps drive Hawaii's economy and is helping lift us out of the recent recession, but it also puts pressure on our natural resources like fresh water resources. It makes sense to spend a portion of conveyance tax revenue on protecting those natural resources.

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CATHOLIC CHARITIES HAWAII

TESTIMONY IN SUPPORT OF SB 22: RELATING TO TAXATION

TO: Senator Rosalyn H. Baker, Chair, and Senator Brickwood Galuteria, Vice Chair, and Members, Committee on Commerce and Consumer Protection

FROM: Betty Lou Larson, Legislative Liaison, Catholic Charities Hawaii

Hearing: **Wednesday, January 30, 2013; 8:30 am; CR 229**

Chair Baker, Vice Chair Galuteria, and Members, Committee on Commerce and Consumer Protection:

Thank you for the opportunity to testify on SB 22, regarding applying the conveyance tax to sale, transfer or exchange of stock, whose assets include realty located in Hawaii. I am Betty Lou Larson, Legislative Liaison for Catholic Charities Hawaii. Catholic Charities Hawaii supports this bill. We also urge you to include amendments to this bill that would provide exemptions for real estate transfers between subsidiaries of the same parent entity, and between partners engaged in qualified affordable rental housing developments. We support the language in a similar bill, SB 97 to avoid any negative impact on affordable rental housing development.

When the island of Lanai was sold, no conveyance tax was paid. Yet if a house or a business is sold, the conveyance tax is paid. This bill would close a loophole in the conveyance tax law and provide additional needed funds for critical state needs, such as affordable housing, land preservation and watershed protection which receive appropriations from the conveyance tax proceeds.

Catholic Charities Hawaii receives hundreds of calls each month from families that need affordable housing. The Hawaii Housing Planning Study of 2011 found that an estimated 13,000 rental units need to be built by 2016. To build these 13,000 affordable units, additional resources are required for the Rental Housing Trust Fund, which receives conveyance tax proceeds. The Trust Fund has created **4,250 rental units**. **In FY 12, it received \$37 million in project requests, yet was only able to commit funds to 4 out of the 9 project applications due to limited resources.**

We note that this bill includes various options for valuing the real property. Another option would be to base the real estate valuation on a recent qualified appraisal (if available) or the most current county real property tax assessed value, whichever is less. In this way, the valuation (1) focuses on the subject of the tax—the realty itself—not on the overall value of the stock or the business; (2) provides the seller the option of getting an appraisal on the realty or relying on the county tax assessed value; and (3) offers the tax department an external means of determining valuation.

We urge your support to close this tax loophole and tax the value of the real estate. Thank you for your consideration of SB22 and its impact on housing and land protection

