March 28, 2018

The Honorable Donovan M. Dela Cruz
Chair, Hawaii Senate Committee on Ways and Means
Hawaii State Capitol, Room 208
Honolulu, HI 96813

RE: SIFMA Letter in Opposition to H.B. 2702 H.D.1, on Real Estate Investment Trusts (REITs).

Dear Chair Dela Cruz and Members of the Senate Committee on Ways and Means:

The Securities Industry and Financial Markets Association ('SIFMA")[1] is a national trade association which represents hundreds of large, medium and small broker-dealers, banks and assets managers, many of whom have a presence in Hawaii. We appreciate the opportunity to comment on H.B. 2702 H.D. 1, which recently passed the House and has been sent to your committee for consideration.

H.B. 2702 H.D.1 is similar to S.B. 3067 S.D. 1, which was recommitted to Senate Ways and Means by the full Senate on March 6. The bill would require real estate investment trusts (REITs) to:

1. Prepare annual tax returns which include detailed personal information on each shareholder, the number of shares each shareholder owns, and a shareholder by shareholder breakdown of what REIT income is attributable to the State;

2. Secure, and subsequently file with the Department of Taxation, the agreement of each nonresident shareholder to file a Hawaii return with respect to the investment income and to be subject to liability for unpaid taxes; and

3. Where agreements are not filed, withhold an amount equal to the shareholder's pro rata share of the income attributable to the state multiplied by the highest marginal tax rate.

We are writing to express our strong opposition to H.B. 2702 H.D. 1. While broker-dealers are not expressly referenced, both they and their clients would be adversely affected by the bill. Specifically, we urge you to consider the following:

[1] SIFMA is the voice of the U.S. securities industry. We represent the broker-dealers, banks and asset managers whose nearly 1 million employees provide access to the capital markets, raising over $2.5 trillion for businesses and municipalities in the U.S., serving clients with over $18.5 trillion in assets and managing more than $67 trillion in assets for individual and institutional clients including mutual funds and retirement plans. For more information, visit http://www.sifma.org.

- Requiring Broker-Dealers and REITs to Compile and Disclose Information on Individual Investors Would Be Unduly Burdensome.

  For both proprietary and confidentiality reasons, REIT shares are typically registered in the name of the financial intermediary (e.g., broker) holding the shares for its customers in a "street name" or nominee account. REITs therefore often do not have the information requested by the bill and would be forced to go to broker-dealers to obtain it.

  This, of course, undercuts the premise behind registering the shares in a street name or nominee account. It also would be a tremendous amount of work both for brokers to provide this information and for REITs to take it and process it.

  In 2017, more than 48 billion REIT transactions were made through the New York Stock Exchange. The daily volume often exceeds 200 million transactions and can reach 400 million. It would be extremely costly and time consuming for our members to sort, track and securely report sensitive personally identifiable information (PII) on all the investors who might own REIT shares at some point during the year. It would be nearly impossible for broker-dealers to obtain and share with REITs agreements to file a HI tax return from each nonresident beneficial owner, keeping in mind that such shares are often held indirectly through mutual funds or in a retirement account. REITs would then have the additional burdens of breaking REIT investments down by state and shareholder, seeking HI nonresident agreements to file a tax return, and calculating the pro rata share of income attributable to the state multiplied by the highest marginal tax rate. To our knowledge, no other state has contemplated such a requirement.

- Additional Requirements Could Make Investments in Hawaii Real Estate Less Attractive. Imposing novel tax reporting, withholding, and investor tax return filing requirements on REITs with Hawaii investments inevitably will make REITs with a Hawaii presence less attractive to investors, and this could reduce the level of investment in Hawaii real property. U.S. equity market participants have other investment options that do not require them to commit to filing an individual tax return or to share sensitive PII with multiple intermediaries.

- Disclosing PII Could Place Clients at Risk.

  H.B. 2702 H.D. 1 requires detailed information on each individual investor, including name, address and social security number, as well as additional filings with the Department of Taxation. Broker-dealers implement and maintain strict security procedures and practices to protect the client's PII. These measures are generally appropriate to the nature of the personal information owned or licensed and the nature and size of the entity or operation.[2] Limiting the collection and disclosure of sensitive data to that which is directly relevant and

[2] H.R. 4028, the "Promoting Responsible Oversight of Transactions and Examinations of Credit Technology Act of 2017."

necessary to accomplish a specified purpose is one of the best practices to protect client information.[3] Requiring broker-dealers to disclose PII to REITs runs counter to protecting the client's private information. This is true even if similar information is already reported elsewhere.

- Over-Withholding Would Further Reduce the Appeal of Hawaii REIT Investments

  If the difficult to obtain shareholder consents are not filed with the Department of Taxation, H.B. 2702 H.D. 1 would require REITs to withhold at the highest marginal tax rate on distributions to their shareholders with income attributable to Hawaiian properties. In order to avoid penalties, REITs might be required to withhold on the full amount of a distribution, even if only a small portion of the overall investment is Hawaii-related. This could occur if such REITs are not able to calculate the portion of a REIT dividend attributable to HI at the time of the distribution. Over-withholding is not in the investors' best-interest even if there is a process for recovering the over-withholding down the road. Such over-withholding would further reduce the appeal of HI-based REITs for equity investors.

- Resident and Non-Resident Hawaii REIT Shareholders Would be Subject to Double Taxation.

  Whether or not over-withholding occurs, both resident and non-resident shareholders would be subject to double taxation. Non-Hawaiian shareholders would be taxed first in Hawaii and then in their own country or state of residence with respect to the same REIT dividend. It is unlikely that any other state or foreign jurisdiction would allow a credit for tax imposed by Hawaii under the proposed legislation.

  In the absence of a Hawaii credit, which the legislation does not seem to provide, Hawaii resident shareholders also appear to be subject to a double-tax when REITs pay dividends to shareholders already subject to tax or withholding under the legislation.

In short, for a variety of reasons we believe that H.B. 2701 H.D. 1 is not good for brokers, investors or the State of Hawaii, and we urge you to oppose the legislation. We appreciate the opportunity to provide feedback. If you have any questions, or if there is any further information we can provide, please contact me at 212-313-1311.

Sincerely,

Kim Chamberlain
Managing Director & Associate General Counsel
SIFMA

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[3] NIST Cybersecurity Framework, p. 16.