
A BILL FOR AN ACT

RELATING TO TAXATION.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF HAWAII:

SECTION 1. The purpose of this Act is to conform Hawaii income tax laws to the Internal Revenue Code, except as provided by this Act.

SECTION 2. Section 235-2.3, Hawaii Revised Statutes, is amended to read as follows:

"§235-2.3 Conformance to the federal Internal Revenue Code; general application. (a) For all taxable years beginning after December 31, ~~[2017,]~~ 2018, as used in this chapter, except as provided in section 235-2.35, "Internal Revenue Code" means subtitle A, chapter 1, of the federal Internal Revenue Code of 1986, as amended as of ~~[February 9, 2018,]~~ December 31, 2018, as it applies to the determination of gross income, adjusted gross income, ordinary income and loss, and taxable income, except those provisions of the Internal Revenue Code and federal public laws which, pursuant to this chapter, do not apply or are otherwise limited in application and except for the provisions of Public Law 109-001 which apply to section 170 of the Internal Revenue Code. The provisions of Public Law 109-001 to accelerate the deduction for charitable cash contributions for the relief of victims of the 2004 Indian Ocean tsunami are applicable for the calendar year that ended December 31, 2004, and the calendar year ending December 31, 2005.

Prior law shall continue to be used to determine:

- (1) The basis of property, if a taxpayer first determined the basis of property in a taxable year to which prior law applies; and
- (2) Gross income, adjusted gross income, ordinary income and loss, and taxable income for a taxable year to which prior law applies.

(b) The following Internal Revenue Code subchapters, parts of subchapters, sections, subsections, and parts of subsections shall not be operative for the purposes of this chapter, unless otherwise provided:

- (1) Subchapter A (sections 1 to 59A) (with respect to determination of tax liability), except section 1(h)(2) (relating to net capital gain reduced by the amount taken into account as investment income), except sections 2(a), 2(b), and 2(c) (with respect to the definition of "surviving spouse" and "head of household"), except section 41 (with respect to the credit for increasing research activities), except section 42 (with respect to low-income housing credit), except sections 47 and 48, as amended, as of December 31, 1984 (with respect to certain depreciable tangible personal property), and except section 48(d)(3), as amended, as of February 17, 2009 (with respect to the treatment of United States Department of Treasury grants made under section 1603 of the American Recovery and Reinvestment Tax Act of 2009). For treatment, see sections 235-110.91, 235-110.7, and 235-110.8;
- (2) Section 78 (with respect to dividends received from certain foreign corporations by domestic corporations choosing foreign tax credit);
- (3) Section 86 (with respect to social security and tier 1 railroad retirement benefits);
- (4) Section 91 (with respect to certain foreign branch losses transferred to specified 10-percent owned foreign corporations);
- (5) Section 103 (with respect to interest on state and local bonds). For treatment, see section 235-7(b);
- (6) Section 114 (with respect to extraterritorial income). For treatment, any transaction as specified in the transitional rule for 2005 and 2006 as specified in the American Jobs Creation Act of 2004 section 101(d) and any transaction that has occurred pursuant to a binding contract as specified in the American Jobs Creation Act of 2004 section 101(f) are inoperative;

- (7) Section 120 (with respect to amounts received under qualified group legal services plans). For treatment, see section 235-7(a)(9) to (11);
- (8) Section 122 (with respect to certain reduced uniformed services retirement pay). For treatment, see section 235-7(a)(3);
- (9) Section 135 (with respect to income from United States savings bonds used to pay higher education tuition and fees). For treatment, see section 235-7(a)(1);
- (10) Section 139C (with respect to COBRA premium assistance);
- (11) Subchapter B (sections 141 to 150) (with respect to tax exemption requirements for state and local bonds);
- (12) Section 151 (with respect to allowance of deductions for personal exemptions). For treatment, see section 235-54;
- (13) Section 179B (with respect to expensing of capital costs incurred in complying with Environmental Protection Agency sulphur regulations);
- (14) Section 181 (with respect to special rules for certain film and television productions);
- (15) Section 196 (with respect to deduction for certain unused investment credits);
- (16) Section 199 (with respect to the U.S. production activities deduction);
- (17) Section 199A (with respect to qualified business income);
- (18) Section 222 (with respect to qualified tuition and related expenses);
- (19) Sections 241 to 247 (with respect to special deductions for corporations). For treatment, see section 235-7(c);
- (20) Section 250 (with respect to foreign-derived intangible income and global intangible low-taxed income);
- (21) Section 267A (with respect to certain related party amounts paid or accrued in hybrid transactions or with hybrid entities);

- (22) Section 280C (with respect to certain expenses for which credits are allowable). For treatment, see section 235-110.91;
- (23) Section 291 (with respect to special rules relating to corporate preference items);
- (24) Section 367 (with respect to foreign corporations);
- (25) Section 501(c)(12), (15), (16) (with respect to exempt organizations); except that section 501(c)(12) shall be operative for companies that provide potable water to residential communities that lack any access to public utility water services;
- (26) Section 515 (with respect to taxes of foreign countries and possessions of the United States);
- (27) Subchapter G (sections 531 to 565) (with respect to corporations used to avoid income tax on shareholders);
- (28) Subchapter H (sections 581 to 597) (with respect to banking institutions), except section 584 (with respect to common trust funds). For treatment, see chapter 241;
- (29) Section 642(a) and (b) (with respect to special rules for credits and deductions applicable to trusts). For treatment, see sections 235-54(b) and 235-55;
- (30) Section 646 (with respect to tax treatment of electing Alaska Native settlement trusts);
- (31) Section 668 (with respect to interest charge on accumulation distributions from foreign trusts);
- (32) Subchapter L (sections 801 to 848) (with respect to insurance companies). For treatment, see sections 431:7-202 and 431:7-204;
- (33) Section 853 (with respect to foreign tax credit allowed to shareholders). For treatment, see section 235-55;
- (34) Section 853A (with respect to credits from tax credit bonds allowed to shareholders);
- (35) Subchapter N (sections 861 to 999) (with respect to tax based on income from sources within or without the United States), except sections 985 to 989 (with respect to foreign currency transactions). For treatment, see sections 235-4, 235-5, and 235-7(b), and 235-55;

- (36) Section 1042(g) (with respect to sales of stock in agricultural refiners and processors to eligible farm cooperatives);
- (37) Section 1055 (with respect to redeemable ground rents);
- (38) Section 1057 (with respect to election to treat transfer to foreign trust, etc., as taxable exchange);
- (39) Sections 1291 to 1298 (with respect to treatment of passive foreign investment companies);
- (40) Subchapter Q (sections 1311 to 1351) (with respect to readjustment of tax between years and special limitations);
- (41) Subchapter R (sections 1352 to 1359) (with respect to election to determine corporate tax on certain international shipping activities using per ton rate);
- (42) Subchapter U (sections 1391 to 1379F) (with respect to designation and treatment of empowerment zones, enterprise communities, and rural development investment areas). For treatment, see chapter 209E;
- (43) Subchapter W (sections 1400 to 1400C) (with respect to District of Columbia enterprise zone);
- (44) Section 1400O (with respect to education tax benefits);
- (45) Section 1400P (with respect to housing tax benefits);
- (46) Section 1400R (with respect to employment relief);
- (47) Section 1400T (with respect to special rules for mortgage revenue bonds);
- (48) Section 1400U-1 (with respect to allocation of recovery zone bonds);
- (49) Section 1400U-2 (with respect to recovery zone economic development bonds); and
- (50) Section 1400U-3 (with respect to recovery zone facility bonds); ~~and~~
- (51) Subchapter Z (sections 1400Z-1 to 1400Z-2) (with respect to opportunity zones)]."

SECTION 3. Section 235-2.4, Hawaii Revised Statutes, is amended by amending subsection (ee) to read as follows:

"(ee) Sections 512 to 514 (with respect to taxation of business income of certain exempt organizations) of the Internal Revenue Code shall be operative for the purposes of this chapter as provided in this subsection.

"Unrelated business taxable income" means the same as in the Internal Revenue Code, except that ~~[iñ]~~:

(1) In the computation ~~[thereof sections]~~ of unrelated business taxable income:

(A) Sections 235-3 to 235-5, and 235-7 (except subsection (c)), shall apply~~[r]~~; and ~~[iñ]~~

(B) Section 512(a)(7) shall not apply;

(2) In the determination of the net operating loss deduction there shall not be taken into account any amount of income or deduction that is excluded in computing the unrelated business taxable income~~[r]~~; and

(3) Unrelated business taxable income shall not include any income from a legal service plan.

For a person described in section 401 or 501 of the Internal Revenue Code, as modified by section 235-2.3, the tax imposed by section 235-51 or 235-71 shall be imposed upon the person's unrelated business taxable income."

SECTION 4. Section 235-2.45, Hawaii Revised Statutes, is amended to read as follows:

"§235-2.45 Operation of certain Internal Revenue Code provisions; sections 641 to 7518. (a) Section 641 (with respect to imposition of tax) of the Internal Revenue Code shall be operative for the purposes of this chapter subject to the following:

(1) The deduction for exemptions shall be allowed as provided in section 235-54(b);

(2) The deduction for contributions and gifts in determining taxable income shall be limited to the amount allowed in the case of an individual, unless the contributions and gifts are to be used exclusively in the State; and

(3) The tax imposed by section 1(e) of the Internal Revenue Code as applied by section 641 of the Internal Revenue Code is hereby imposed by this chapter at the rate and amount as determined under section 235-51 on estates and trusts.

(b) Section 667 (with respect to treatment of amounts deemed distributed by trusts in preceding years) of the Internal Revenue Code shall be operative for the purposes of this chapter and the tax imposed therein is hereby imposed by this chapter at the rate determined under this chapter; except that the reference to tax-exempt interest to which section 103 of the Internal Revenue Code applies in section 667(a) of the Internal Revenue Code shall instead be a reference to tax-exempt interest to which section 235-7(b) applies.

(c) Section 685 (with respect to treatment of qualified funeral trusts) of the Internal Revenue Code shall be operative for purposes of this chapter, except that the tax imposed under this chapter shall be computed at the tax rates provided under section 235-51, and no deduction for the exemption amount provided in section 235-54(b) shall be allowed. The cost-of-living adjustment determined under section 1(f)(3) of the Internal Revenue Code shall be operative for the purpose of applying section 685(c)(3) under this chapter.

(d) Section 704 of the Internal Revenue Code (with respect to a partner's distributive share) shall be operative for purposes of this chapter; except that section 704(b)(2) shall not apply to:

- (1) Allocations of the high technology business investment tax credit allowed by section 235-110.9 for investments made before May 1, 2009;
- (2) Allocations of net operating loss pursuant to section 235-111.5; or
- (3) Allocations of low-income housing tax credits among partners under section 235-110.8.

(e) Section 1202 (with respect to partial exclusion for gain from certain small business stock) of the Internal Revenue Code shall be

operative for purposes of this chapter, except that section 1202(a)(3) and (4) shall not be operative for purposes of this chapter.

(f) Section 1212 (with respect to capital loss carrybacks and carryforwards) of the Internal Revenue Code shall be operative for the purposes of this chapter; except that for the purposes of this chapter, the capital loss carryback provisions of section 1212 shall not be operative and the capital loss carryforward allowed by section 1212(a) shall be limited to five years; except for a qualified high technology business as defined in section 235-7.3, which shall be limited to fifteen years.

(g) Section 1221 (with respect to the definition of capital assets) is operative; provided that the provisions of section 301 of Public Law 110-343, which provide that gain or loss from the sale or exchange of any applicable preferred stock by any applicable financial institution (such terms being defined by Public Law 110-343) shall be treated as ordinary income or loss, shall not be operative. A sale or exchange of any applicable preferred stock by any applicable financial institution (as those terms are defined by section 301 of Public Law 110-343) shall be treated as a sale of a capital asset and taxed accordingly.

(h) Subchapter S (sections 1361 to 1379) (with respect to tax treatment of S corporations and their shareholders) of chapter 1 of the Internal Revenue Code shall be operative for the purposes of this chapter as provided in part VII.

(i) Section 1400N (with respect to tax benefits for Gulf Opportunity Zone) of the Internal Revenue Code shall be operative for the purposes of this chapter, except that sections 1400N(a) (with respect to tax-exempt bond financing); 1400N(b) (with respect to advance refundings of certain tax-exempt bonds); 1400N(c) (with respect to the low income housing credit); 1400N(d) (with respect to special allowance for certain property acquired on or after August 28, 2005); 1400N(e) (with respect to increase in expensing under section 179); 1400N(h) (with respect to increase in

rehabilitation credit); 1400N(l) (with respect to credit to holders of Gulf tax credit bonds); 1400N(m) (with respect to application of new markets tax credit to investments in community development entities serving Gulf Opportunity Zone); 1400N(n) (with respect to treatment of representations regarding income eligibility for purposes of qualified residential rental project requirements) shall not be operative for purposes of this chapter.

(j) Section 1400S (with respect to additional tax relief provisions) of the Internal Revenue Code shall be operative for the purposes of this chapter, except that section 1400S(d) (with respect to the special rule for determining earned income) shall be operative for the purposes of this chapter.

(k) Subchapter Z (sections 1400Z-1 to 1400Z-2) (with respect to opportunity zones) shall be operative for purposes of this chapter; except that for purposes of this chapter, subchapter Z shall only apply to qualified opportunity zones, as defined in section 1400Z-1, that are designated as such by the chief executive officer of this State.

~~(l)~~ (l) Section 6015 (with respect to relief from joint and several liability on joint return) of the Internal Revenue Code is operative for purposes of this chapter.

~~(m)~~ (m) Sections 6103(i) (3) (C) and 6103(i) (7) (with respect to disclosures of information to the United States Justice Department or appropriate federal or state law enforcement agency for purposes of investigating terrorist incidents, threats, or activities, and for analyzing intelligence concerning investigating terrorist incidents, threats, or activities) of the Internal Revenue Code shall be operative for the purposes of this chapter.

~~(n)~~ (n) Sections 6221, 6222, 6223, 6225, and 6226 (with respect to partnership audits) of subchapter C of chapter 63 of the Internal Revenue Code shall be operative for the purposes of this chapter; provided that if a taxpayer makes the election under section 6221(b) for federal income tax

purposes, that taxpayer shall also make the same election for Hawaii income tax purposes.

~~[(n)]~~ [(o)] Section 6241 (with respect to definitions and special rules regarding partnerships) of the Internal Revenue Code shall be operative for the purposes of this chapter, except that the definitions that appear in items numbered (1), (3), and (5) shall not be operative for purposes of this chapter.

~~[(e)]~~ [(p)] Section 6501(e) (with respect to limitation on assessment and collection where there is a substantial omission of items) of the Internal Revenue Code shall be operative for purposes of this chapter.

~~[(f)]~~ [(q)] Section 6511(h) (with respect to running of periods of limitation suspended while taxpayer is unable to manage financial affairs due to disability) of the Internal Revenue Code shall be operative for purposes of this chapter, with due regard to section 235-111 relating to the limitation period for assessment, levy, collection, or credit.

~~[(g)]~~ [(r)] Section 7518 (with respect to capital construction fund for commercial fishers) of the Internal Revenue Code shall be operative for the purposes of this chapter. Qualified withdrawals for the acquisition, construction, or reconstruction of any qualified asset that is attributable to deposits made before the effective date of this section shall not reduce the basis of the asset when withdrawn. Qualified withdrawals shall be treated on a first-in-first-out basis."

SECTION 5. Section 236E-3, Hawaii Revised Statutes, is amended to read as follows:

"§236E-3 Conformance to the Internal Revenue Code; general application. For all decedents dying, or transfers occurring, after December 31, ~~[2017,]~~ 2018, as used in this chapter, "Internal Revenue Code" means subtitle B of the federal Internal Revenue Code of 1986, as amended as of December 31, ~~[2017,]~~ 2018, as it applies to the determination of gross estate, adjusted gross estate, federal taxable estate, and

generation-skipping transfers, except those provisions of the Internal Revenue Code and federal public laws that, pursuant to this chapter, do not apply or are otherwise limited in application."

SECTION 6. Section 236E-6, Hawaii Revised Statutes, is amended by amending subsection (a) to read as follows:

"(a) An exclusion from a Hawaii taxable estate shall be allowed to the estate of every decedent against the tax imposed by section 236E-8. For the purpose of this section, the applicable exclusion amount is equal to:

(1) The federal applicable exclusion amount;

(2) The exemption equivalent of the unified credit reduced by the amount of taxable gifts made by the decedent that reduces the amount of the federal applicable exclusion amount; or

(3) The exemption equivalent of the unified credit on the decedent's federal estate tax return,

as set forth for the decedent in chapter 11 of the Internal Revenue Code as amended as of December 21, 2017, as if the decedent died on December 31, 2017, and as further adjusted pursuant to subsection (b)."

SECTION 7. Statutory material to be repealed is bracketed and stricken. New statutory material is underscored.

SECTION 8. This Act shall take effect upon its approval; provided that:

(1) Sections 2, 3, and 4 shall apply to taxable years beginning after December 31, 2018; and

(2) Sections 5 and 6 shall apply to decedents dying or taxable transfers occurring after December 31, 2018.

Report Title:

Taxation; Internal Revenue Code; Income Tax; Estate and Generation-skipping Transfer Tax

Description:

Specifies that the Internal Revenue Code section 512(a)(7), with respect to increases in unrelated business taxable income by disallowed fringe, is not

operative in Hawaii income tax law. Conforms Hawaii income and estate and generation-skipping transfer tax laws to the Internal Revenue Code of 1986, as amended as of December 31, 2018. Clarifies wording regarding the Hawaii applicable exclusion amount. (SD1)

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