
A BILL FOR AN ACT

RELATING TO PASS-THROUGH ENTITY TAXATION.

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

1 SECTION 1. The purpose of this Act is to establish a state
2 tax law to permit certain entities to elect to pay Hawaii income
3 tax at the entity level. This Act will help Hawaii's small
4 businesses by allowing taxpayers to deduct Hawaii state income
5 taxes paid on their federal income tax returns. These
6 deductions from federal taxable income were eliminated through
7 changes to the federal tax code in 2017, which deprived Hawaii
8 taxpayers of significant federal tax benefits. This Act will
9 bring Hawaii into conformity with the majority of other states
10 that already permit similar elections by so-called "pass-through
11 entities" to pay state income taxes.

12 SECTION 2. Chapter 235, Hawaii Revised Statutes, is
13 amended by adding a new section to part III to be appropriately
14 designated and to read as follows:

15 "§235- Pass-through entity taxation election. (a) A
16 partnership or S corporation may elect to become an electing
17 pass-through entity in any tax year; provided that a separate



1 election shall be made for each taxable year. An election made
2 pursuant to this subsection shall be filed in the form and
3 manner prescribed by the director and signed by:

4 (1) Each member of the entity who is a member at the time
5 the election is filed; or

6 (2) Any officer, manager, or member of the entity who is
7 authorized to make the election and who attests to
8 having such authorization under penalty of perjury.

9 (b) Notwithstanding any provision of law to the contrary,
10 the following tax is imposed on each electing pass-through
11 entity: the sum of each member's distributive share of Hawaii
12 taxable income as calculated under this chapter, multiplied by
13 the highest rate of tax applicable to the individual under
14 section 235-51. If the income calculated pursuant to this
15 subsection reflects a net loss for the electing pass-through
16 entity, the net loss may be carried forward to subsequent tax
17 years for as long as the electing pass-through entity elects to
18 be subject to the tax pursuant to this section until exhausted.

19 (c) A nonresident individual who is a member of an
20 electing pass-through entity shall not be required to file an
21 income tax return pursuant to this chapter for a tax year if the



1 member's only source of Hawaii income is from electing pass-
2 through entities and the electing pass-through entity or
3 entities file and pay the tax due under this section.

4 (d) Each electing pass-through entity shall report to each
5 of its members, for each tax year, the member's pro rata share
6 of the tax imposed pursuant to this section.

7 (e) Each member of an electing pass-through entity shall
8 be entitled to a credit equal to the member's share of the tax
9 paid pursuant to this section. If the amount of the credit
10 authorized by this subsection exceeds the member's tax liability
11 imposed pursuant to this chapter, the excess amount shall not be
12 refundable to the member. Any member claiming a credit shall
13 not be entitled to deduct from their Hawaii state taxable income
14 those amounts of Hawaii state income taxes paid by the member on
15 their distributive share of income from the electing pass-
16 through entity.

17 (f) Each member that is subject to the tax imposed by this
18 chapter as a resident or part-year resident of the State shall
19 be entitled to a credit for the direct member's or indirect
20 member's pro rata share of taxes paid to another state or to the
21 District of Columbia, on income of any partnership or S



1 corporation, of which the person is a member; provided that the
2 taxes paid to another state or to the District of Columbia
3 result from a tax that the director of taxation determines is
4 substantially similar to the tax imposed pursuant to this
5 section. Any credit shall be calculated in a form and manner
6 prescribed by the director; provided that the calculation is
7 consistent with the provisions of this section. If the amount
8 of the credit authorized by this subsection exceeds the member's
9 tax liability for the tax imposed pursuant to this chapter, the
10 excess amount shall not be refundable and shall not carry
11 forward.

12 (g) The department of taxation may establish rules to
13 implement this section.

14 (h) For purposes of this section:

15 "Direct member" means a member that holds an interest
16 directly in an electing pass-through entity.

17 "Electing pass-through entity" means any eligible
18 partnership or S corporation that elects to be subject to tax
19 pursuant to subsection (a).

20 "Indirect member" means a member that itself holds an
21 interest, through a direct or indirect member that is a



1 partnership or S corporation, in an electing pass-through
2 entity.

3 "Member" means:

4 (1) A shareholder of an S corporation;

5 (2) A partner in a general partnership, a limited
6 partnership, or a limited liability partnership; or

7 (3) A member of a limited liability company that is
8 treated as a partnership or S corporation for federal
9 income tax purposes.

10 "Partnership" means the same as in the Internal Revenue
11 Code. "Partnership" includes a limited liability company that
12 is treated as a partnership for federal income tax purposes but
13 does not include any publicly traded partnership within the
14 meaning of section 7704 of the Internal Revenue Code.

15 "S corporation" means a corporation for which a valid
16 election under section 1362(a) of the Internal Revenue Code is
17 in effect."

18 SECTION 3. This Act, upon its approval, shall apply to
19 taxable years beginning after December 31, 2022.

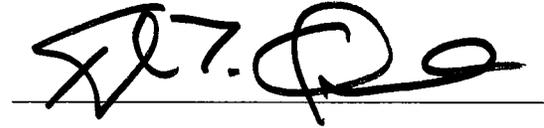
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H.B. NO. 1362

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INTRODUCED BY:

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JAN 25 2023



H.B. NO. 1362

Report Title:

Taxation; Pass-through Entity; S Corporations; Partnerships

Description:

Authorizes certain entities to elect to pay Hawaii income tax at the entity level through pass-through entities.

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