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# A BILL FOR AN ACT

RELATING TO TAXATION.

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

1       SECTION 1. The legislature finds that the majority of  
2 income received from real estate investment trusts by corporate  
3 entities doing business in Hawaii is not taxed at the state  
4 level. They enjoy a preference that exempts them from paying  
5 taxes on dividends paid on revenues generated in Hawaii.  
6 According to the department of taxation, the estimated amount of  
7 income tax revenues that will be foregone in the 2026 taxable  
8 year may be as much as \$26,800,000.

9       The legislature also finds that, in September 2016, the  
10 department of business, economic development, and tourism,  
11 through its research and economic analysis division,  
12 commissioned a report to evaluate the recovery of income tax  
13 revenues from real estate investment trusts within the State.  
14 The findings revealed that Hawaii received only \$954,842 from  
15 in-state residents paying taxes on dividend income associated  
16 with Hawaii real estate investment trusts. In contrast, the  
17 majority of the real estate investment trust income taxes were



1 paid to other states by out-of-state shareholders receiving  
2 dividends, meaning that Hawaii did not benefit from the bulk of  
3 the income generated by real estate investment trusts operating  
4 within its borders. The legislature further finds that real  
5 estate investment trust income generated through the use of  
6 state resources should be taxed in Hawaii to benefit the State.

7 Accordingly, the purpose of this Act is to disallow the  
8 dividends paid deduction for most real estate investment trusts.

9 SECTION 2. Section 235-2.3, Hawaii Revised Statutes, is  
10 amended by amending subsection (b) to read as follows:

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

- 15 (1) Subchapter A (sections 1 to 59A) (with respect to  
16 determination of tax liability), except section  
17 1(h)(2) (relating to net capital gain reduced by the  
18 amount taken into account as investment income),  
19 except sections 2(a), 2(b), and 2(c) (with respect to  
20 the definition of "surviving spouse" and "head of  
21 household"), except section 41 (with respect to the



1 credit for increasing research activities), except  
2 section 42 (with respect to low-income housing  
3 credit), except sections 47 and 48, as amended, as of  
4 December 31, 1984 (with respect to certain depreciable  
5 tangible personal property), and except section  
6 48(d)(3), as amended, as of February 17, 2009 (with  
7 respect to the treatment of United States Department  
8 of Treasury grants made under section 1603 of the  
9 American Recovery and Reinvestment Tax Act of 2009).

10 For treatment, see sections 235-110.91, 235-110.7, and  
11 235-110.8;

12 (2) Section 78 (with respect to dividends received from  
13 certain foreign corporations by domestic corporations  
14 choosing foreign tax credit);

15 (3) Section 86 (with respect to social security and tier 1  
16 railroad retirement benefits);

17 (4) Section 91 (with respect to certain foreign branch  
18 losses transferred to specified 10-percent owned  
19 foreign corporations);

20 (5) Section 103 (with respect to interest on state and  
21 local bonds). For treatment, see section 235-7(b);



1 (6) Section 114 (with respect to extraterritorial income).

2 For treatment, any transaction as specified in the  
3 transitional rule for 2005 and 2006 as specified in  
4 the American Jobs Creation Act of 2004 section 101(d)  
5 and any transaction that has occurred pursuant to a  
6 binding contract as specified in the American Jobs  
7 Creation Act of 2004 section 101(f) are inoperative;

8 (7) Section 120 (with respect to amounts received under  
9 qualified group legal services plans). For treatment,  
10 see section 235-7(a)(9) to (11);

11 (8) Section 122 (with respect to certain reduced uniformed  
12 services retirement pay). For treatment, see section  
13 235-7(a)(3);

14 (9) Section 135 (with respect to income from United States  
15 savings bonds used to pay higher education tuition and  
16 fees). For treatment, see section 235-7(a)(1);

17 (10) Section 139C (with respect to COBRA premium  
18 assistance);

19 (11) Subchapter B (sections 141 to 150) (with respect to  
20 tax exemption requirements for state and local bonds);



- 1       (12)   Section 151 (with respect to allowance of deductions  
2           for personal exemptions). For treatment, see section  
3           235-54;
- 4       (13)   Section 179B (with respect to expensing of capital  
5           costs incurred in complying with Environmental  
6           Protection Agency sulphur regulations);
- 7       (14)   Section 181 (with respect to special rules for certain  
8           film and television productions);
- 9       (15)   Section 196 (with respect to deduction for certain  
10          unused investment credits);
- 11      (16)   Section 199 (with respect to the U.S. production  
12          activities deduction);
- 13      (17)   Section 199A (with respect to qualified business  
14          income);
- 15      (18)   Section 222 (with respect to qualified tuition and  
16          related expenses);
- 17      (19)   Sections 241 to 247 (with respect to special  
18          deductions for corporations). For treatment, see  
19          section 235-7(c);



- 1       (20) Section 250 (with respect to foreign-derived  
2       intangible income and global intangible low-taxed  
3       income);
- 4       (21) Section 267A (with respect to certain related party  
5       amounts paid or accrued in hybrid transactions or with  
6       hybrid entities);
- 7       (22) Section 280C (with respect to certain expenses for  
8       which credits are allowable). For treatment, see  
9       section 235-110.91;
- 10      (23) Section 291 (with respect to special rules relating to  
11      corporate preference items);
- 12      (24) Section 367 (with respect to foreign corporations);
- 13      (25) Section 501(c)(12), (15), (16) (with respect to exempt  
14      organizations); except that section 501(c)(12) shall  
15      be operative for companies that provide potable water  
16      to residential communities that lack any access to  
17      public utility water services;
- 18      (26) Section 515 (with respect to taxes of foreign  
19      countries and possessions of the United States);



- 1       (27) Subchapter G (sections 531 to 565) (with respect to  
2       corporations used to avoid income tax on  
3       shareholders);
- 4       (28) Subchapter H (sections 581 to 597) (with respect to  
5       banking institutions), except section 584 (with  
6       respect to common trust funds). For treatment, see  
7       chapter 241;
- 8       (29) Section 642(a) and (b) (with respect to special rules  
9       for credits and deductions applicable to trusts). For  
10      treatment, see sections 235-54(b) and 235-55;
- 11      (30) Section 646 (with respect to tax treatment of electing  
12      Alaska Native settlement trusts);
- 13      (31) Section 668 (with respect to interest charge on  
14      accumulation distributions from foreign trusts);
- 15      (32) Subchapter L (sections 801 to 848) (with respect to  
16      insurance companies). For treatment, see sections  
17      431:7-202 and 431:7-204;
- 18      (33) Section 853 (with respect to foreign tax credit  
19      allowed to shareholders). For treatment, see section  
20      235-55;



(34) Section 853A (with respect to credits from tax credit bonds allowed to shareholders);

(35) Section 857(b)(2)(B) (with respect to the dividends paid deduction for real estate investment trusts); provided that any real estate investment trust that has investments or is a community development financial institution shall be exempt from this paragraph. For purposes of this paragraph, "community development financial institution" shall have the same meaning as in section 103 of the Community Development Banking and Financial Institutions Act of 1994 (12 U.S.C. §4702);

~~[(35)]~~ (36) 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)]~~ (37) Section 1042(g) (with respect to sales of stock in agricultural refiners and processors to eligible farm cooperatives);



1        [~~+37+~~] (38) Section 1055 (with respect to redeemable ground  
2                    rents);

3        [~~+38+~~] (39) Section 1057 (with respect to election to treat  
4                    transfer to foreign trust, etc., as taxable exchange);

5        [~~+39+~~] (40) Sections 1291 to 1298 (with respect to treatment  
6                    of passive foreign investment companies);

7        [~~+40+~~] (41) Subchapter Q (sections 1311 to 1351) (with  
8                    respect to readjustment of tax between years and  
9                    special limitations), except for section 1341 (with  
10                   respect to computation of tax where taxpayer restores  
11                   substantial amount held under claim of right);

12        [~~+41+~~] (42) Subchapter R (sections 1352 to 1359) (with  
13                   respect to election to determine corporate tax on  
14                   certain international shipping activities using per  
15                   ton rate);

16        [~~+42+~~] (43) Subchapter U (sections 1391 to 1397F) (with  
17                   respect to designation and treatment of empowerment  
18                   zones, enterprise communities, and rural development  
19                   investment areas). For treatment, see chapter 209E;

20        [~~+43+~~] (44) Subchapter W (sections 1400 to 1400C) (with  
21                   respect to District of Columbia enterprise zone);



1       ~~[(44)]~~ (45) Section 14000 (with respect to education tax  
2                   benefits);

3       ~~[(45)]~~ (46) Section 1400P (with respect to housing tax  
4                   benefits);

5       ~~[(46)]~~ (47) Section 1400R (with respect to employment  
6                   relief);

7       ~~[(47)]~~ (48) Section 1400T (with respect to special rules for  
8                   mortgage revenue bonds);

9       ~~[(48)]~~ (49) Section 1400U-1 (with respect to allocation of  
10                  recovery zone bonds);

11       ~~[(49)]~~ (50) Section 1400U-2 (with respect to recovery zone  
12                  economic development bonds); and

13       ~~[(50)]~~ (51) Section 1400U-3 (with respect to recovery zone  
14                  facility bonds)."

15       SECTION 3. Section 235-71, Hawaii Revised Statutes, is  
16       amended by amending subsection (d) to read as follows:

17       "(d) In the case of a real estate investment trust there  
18       is imposed on the taxable income, computed as provided in  
19       sections 857 and 858 of the Internal Revenue Code but with the  
20       changes and adjustments made by this chapter (without prejudice  
21       to the generality of the foregoing, for the taxable years



1 beginning before January 1, 2026, the deduction for dividends  
2 paid is limited to ~~[such]~~ the amount of dividends as is  
3 attributable to income taxable under this chapter~~[+r]~~ and, for  
4 taxable years beginning after December 31, 2025, no deductions  
5 for dividends paid shall be allowed), a tax consisting in the  
6 sum of the following: 4.4 per cent if the taxable income is not  
7 over \$25,000, 5.4 per cent if over \$25,000 but not over  
8 \$100,000, and on all over \$100,000, 6.4 per cent. In addition  
9 to any other penalty provided by law any real estate investment  
10 trust whose tax liability for any taxable year is deemed to be  
11 increased pursuant to section 859(b)(2)(A) or 860(c)(1)(A) after  
12 December 31, 1978, (relating to interest and additions to tax  
13 determined with respect to the amount of the deduction for  
14 deficiency dividends allowed) of the Internal Revenue Code shall  
15 pay a penalty in an amount equal to the amount of interest for  
16 which the trust is liable that is attributable solely to the  
17 increase. The penalty payable under this subsection with  
18 respect to any determination shall not exceed one-half of the  
19 amount of the deduction allowed by section 859(a), or 860(a)  
20 after December 31, 1978, of the Internal Revenue Code for the  
21 taxable year.



1       Notwithstanding the foregoing, beginning January 1, 2022,  
2       the department shall require a real estate investment trust  
3       subject to this chapter to:

4       (1)   Notify the department, in the manner prescribed by the  
5             department, of its operation as a real estate  
6             investment trust in the State no later than fifteen  
7             days from the first day of operation in the State;  
8             provided that, for real estate investment trusts  
9             operating in the State as of July 1, 2021, the  
10            department shall be notified no later than January 15,  
11            2022;

12       (2)   Properly designate on its tax return that it is a real  
13             estate investment trust, as required by the  
14             department;

15       (3)   Complete its tax return in the specific manner  
16             required by the department, including following  
17             line-by-line instructions; and

18       (4)   Submit a copy of the real estate investment trust's  
19             federal tax return covering the same period with each  
20             state tax return that the real estate investment trust  
21             files with the department under this chapter.



1 Any real estate investment trust that fails to comply with these  
2 requirements shall be assessed a penalty of \$50 per day."

3 SECTION 4. Statutory material to be repealed is bracketed  
4 and stricken. New statutory material is underscored.

5 SECTION 5. This Act, upon its approval, shall apply to  
6 taxable years beginning after December 31, 2025.



**Report Title:**

Income Tax; REIT; Dividends Paid Deduction

**Description:**

Disallows the dividends paid deduction for real estate investment trusts, except those having investments or that are community development financial institutions. (SD1)

*The summary description of legislation appearing on this page is for informational purposes only and is not legislation or evidence of legislative intent.*

