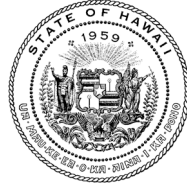


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**TESTIMONY OF  
GARY S. SUGANUMA, DIRECTOR OF TAXATION**

**TESTIMONY ON THE FOLLOWING MEASURE:**

S.B. No. 2881, S.D.1, Relating to State Income Tax

**BEFORE THE:**

House Committee on Finance

**DATE:** Tuesday, April 7, 2026  
**TIME:** 2:00 p.m.  
**LOCATION:** State Capitol, Room 308

Chair Todd, Vice-Chair Takenouchi, and Members of the Committee:

The Department of Taxation (DOTAX) offers the following comments regarding S.B. 2881, S.D.1, for your consideration.

S.B. 2881, S.D.1, amends chapter 235, Hawaii Revised Statutes (HRS), by adding a new section that would allow a taxpayer to have taxable income from retirement-related accounts (i.e., pensions, annuities, Individual Retirement accounts, etc.) that are reported on federal Internal Revenue Service Form 1099-R be subject to withholding at an applicable rate under chapter 235, HRS.

The bill provides that, for distributions subject to tax under this chapter, a taxpayer may provide written notice to the entity making a distribution on the account of the taxpayer's election for withholding. Upon election, the entity is required to withhold and remit the tax amount designated by the taxpayer to, and in the form and manner to be prescribed by, DOTAX.

Any withholding would be reported on the taxpayer's return as a credit against their tax liability owed, and if excess of liability, refunded as per current procedure under section 235-110, HRS.

This bill is effective upon approval and applies to taxable years beginning after December 31, 2026.

DOTAX notes that it can administer a withholding option for taxable years beginning after December 31, 2026.

Thank you for the opportunity to provide comments on this measure.

# TAX FOUNDATION OF HAWAII

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SUBJECT: DOTAX; INCOME. Voluntary Withholding on Form 1099-R Distributions

BILL NUMBER: SB 2881 SD1

INTRODUCED BY: WAM

EXECUTIVE SUMMARY: Provides that taxable income subject to reporting as distribution on Internal Revenue Service Form 1099-R may be subject to withholding at the taxpayer's election. Requires the Department of Taxation to adopt rules and prescribe forms. Applicable to taxable years beginning after 12/31/2026. (SD1)

SYNOPSIS: Adds a new section to chapter 235, HRS, providing that a taxpayer may elect to have any taxable income received by the taxpayer that is subject to reporting as a distribution on Internal Revenue Service Form 1099-R be subject to withholding.

The taxpayer must give written notice to the distributing entity for withholding to apply.

EFFECTIVE DATE: Taxable years beginning after December 31, 2026.

STAFF COMMENTS: Section 3405 of the Internal Revenue Code establishes federal income tax withholding rules for most retirement-type distributions reported on Form 1099-R. It divides distributions into periodic payments, nonperiodic distributions, and eligible rollover distributions, each with different withholding requirements.

For periodic payments, the payer must withhold federal tax as if the payment were wages, using payroll withholding tables; however, the payee may opt out of withholding by filing the appropriate form (e.g., Form W-4P). This election remains in effect until revoked.

For nonperiodic distributions, which are irregular or lump-sum payments that are not part of a series lasting more than one year, the payer must withhold 10% of the distribution; however, the payee may opt out of withholding in this situation as well.

For eligible rollover distributions, the mandatory withholding is 20%, unless the taxpayer chooses a direct rollover to another eligible retirement plan, in which case the withholding requirement does not apply.

This bill proposes to allow the payee to voluntarily withhold Hawaii income tax.

The bill in its current form does not prescribe consequences would need to be prescribed for a payor that, although properly and timely notified of a withholding election, does not in fact pay over the withheld tax to the State. To remedy this problem, we suggest the following, which would take advantage of existing payroll withholding mechanisms and fix a technical issue that now exists regarding withholding under section 235-69:

**§235-66 Further withholdings at source; crediting of withheld taxes.** (a) The department of taxation by regulation, may require the deduction and withholding of tax from any gross income or adjusted gross income of a nonresident, in order to collect the tax imposed by this chapter on the nonresident.

(b) A taxpayer may elect to have any taxable income received by the taxpayer that is subject to federal withholding under Internal Revenue Code section 3405 be subject to withholding under this chapter at an applicable rate pursuant to this chapter. An entity making a distribution, upon receiving written notice from a taxpayer of an election under this section, shall deduct and withhold the amount designated by the taxpayer and remit the amount withheld to the department of taxation in the form and manner prescribed by the department; provided that this section shall not apply to an entity if the distributions are not subject to tax under this chapter.

~~[(b)]~~ (c) Income upon which any tax has been withheld at the source under sections 235-61 to ~~[235-64.2, or under regulations adopted pursuant to subsection (a),]~~ 235-69 shall be included in the return of the recipient of such income, but any amount of tax so withheld shall be credited against the amount of income tax as computed in the return, and if in excess of the tax due for the taxable year shall be refunded as provided in section 235-110.