

TAX FOUNDATION OF HAWAII

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

BILL NUMBER: SB 2881

INTRODUCED BY: KIM, CHANG, LAMOSAO, MCKELVEY

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.

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.

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.

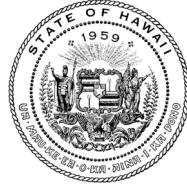
This bill proposes to allow the payee to voluntarily withhold tax.

Perhaps the Committee would consider an arrangement where default consequences apply, similar to IRC section 3405. In addition, 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.

Digested: 2/28/2026

JOSH GREEN M.D.
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TESTIMONY OF
GARY S. SUGANUMA, DIRECTOR OF TAXATION

TESTIMONY ON THE FOLLOWING MEASURE:

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

BEFORE THE:

Senate Committee on Ways and Means

DATE: Monday, March 2, 2026
TIME: 10:00 a.m.
LOCATION: State Capitol, Room 211

Chair Dela Cruz, Vice-Chair Moriwaki, and Members of the Committee:

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

S.B. 2881 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.

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 although this bill would allow a taxpayer to elect to have income tax withheld, there is no provision that would require the administrator of the retirement account to withhold and remit the tax. DOTAX therefore recommends that the bill be amended to require that a taxpayer make an election by providing written notice of their election to the administrator of the account, and further requiring that the administrator withhold and remit the tax to DOTAX upon receiving written notice from the taxpayer.

DOTAX further 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.