

ACT 91

H.B. NO. 1089

A Bill for an Act Relating to Conformity of the Hawaii Income Tax Law to the Internal Revenue Code.

*Be It Enacted by the Legislature of the State of Hawaii:*

SECTION 1. The purpose of this Act is to conform Hawaii income tax law to the Internal Revenue Code.

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

“(a) For all taxable years beginning after December 31, [2009,] 2010, 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 December 31, [2009,] 2010, 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.

Sections 235-2, 235-2.1, and 235-2.2 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 such sections apply, and if such determination was made before January 1, 1978; and

- (2) Gross income, adjusted gross income, ordinary income and loss, and taxable income for a taxable year to which such sections apply where such taxable year begins before January 1, 1978.”

SECTION 3. Section 235-2.35, Hawaii Revised Statutes, is amended to read as follows:

**“[H§235-2.35] Operation of certain Internal Revenue Code provisions not operative under section 235-2.3.** [Notwithstanding the meaning of “Internal Revenue Code” as that term is used in section [235-2.3], beginning April 1, 2010, the] The following sections of the federal Internal Revenue Code of 1986, as amended [as of April 1, 2010], shall be operative for purposes of this chapter:

- (1) Section 6041 as applicable to persons under section 6041(h) (with respect to information returns at the source for certain corporations);
- (2) Section 6038D (with respect to information with respect to foreign financial assets). With respect to persons required to report information under this section, section 6662(j) (with respect to imposition of accuracy-related penalties on underpayments) and section 6501(e)(1)(A)(ii) (with respect to limitations on assessment and collection) shall also be operative for purposes of this chapter and shall be applied consistently with the correlating provisions of [H sections] 231-36.6 and 235-111;
- (3) Section 6045B (with respect to returns relating to actions affecting basis in securities); and
- (4) Section 6050W (with respect to returns relating to payments made in settlement of payment card and third party network transactions).”

SECTION 4. Section 235-2.4, Hawaii Revised Statutes, is amended to read as follows:

**“§235-2.4 Operation of certain Internal Revenue Code provisions; sections 63 to 530.** (a) Section 63 (with respect to taxable income defined) of the Internal Revenue Code shall be operative for the purposes of this chapter, subject to the following:

- (1) Sections 63(c)(1)(B) (relating to the additional standard deduction), 63(c)(1)(C) (relating to the real property tax deduction), 63(c)(1)(D) (relating to the disaster loss deduction), 63(c)(1)(E) (relating to the motor vehicle sales tax deduction), 63(c)(4) (relating to inflation adjustments), 63(c)(7) (defining the real property tax deduction), 63(c)(8) (defining the disaster loss deduction), 63(c)(9) (defining the motor vehicle sales tax deduction), and 63(f) (relating to additional amounts for the aged or blind) of the Internal Revenue Code shall not be operative for purposes of this chapter;
- (2) Section 63(c)(2) (relating to the basic standard deduction) of the Internal Revenue Code shall be operative, except that the standard deduction amounts provided therein shall instead mean:
  - (A) \$4,400 in the case of:
    - (i) A joint return as provided by section 235-93; or
    - (ii) A surviving spouse (as defined in section 2(a) of the Internal Revenue Code);
  - (B) \$3,212 in the case of a head of household (as defined in section 2(b) of the Internal Revenue Code);

- (C) \$2,200 in the case of an individual who is not married and who is not a surviving spouse or head of household; or
- (D) \$2,200 in the case of a married individual filing a separate return;
- (3) Section 63(c)(5) (limiting the basic standard deduction in the case of certain dependents) of the Internal Revenue Code shall be operative, except that the limitation shall be the greater of \$500 or such individual's earned income; and
- (4) The standard deduction amount for nonresidents shall be calculated pursuant to section 235-5.
- (b) Section 68 (with respect to the overall limitation on itemized deductions) of the Internal Revenue Code shall be operative, except that sections 68(f) and 68(g) shall not be operative; provided that the thresholds shall be those that were operative for federal tax year 2009.
- ~~[(b)]~~ (c) Section 72 (with respect to annuities; certain proceeds of endowment and life insurance contracts) of the Internal Revenue Code shall be operative for purposes of this chapter and be interpreted with due regard to section 235-7(a), except that the ten per cent additional tax on early distributions from retirement plans in section 72(t) shall not be operative for purposes of this chapter.
- ~~[(e)]~~ (d) Section 85 (with respect to unemployment compensation) of the Internal Revenue Code shall be operative for purposes of this chapter, except that section 85(c) shall not be operative for purposes of this chapter.
- ~~[(d)]~~ (e) Section 108 (with respect to income from discharge of indebtedness) of the Internal Revenue Code shall be operative for purposes of this chapter, except that section 108(i) (relating to deferral and ratable inclusion of income arising from business indebtedness discharged by the reacquisition of a debt instrument) shall not be operative for purposes of this chapter.
- ~~[(e)]~~ (f) Section 121 (with respect to exclusion of gain from sale of principal residence) of the Internal Revenue Code shall be operative for purposes of this chapter, except that for the election under section 121(f), a reference to section 1034 treatment means a reference to section 235-2.4(s) in effect for taxable year 1997.
- ~~[(f)]~~ (g) Section 132 (with respect to certain fringe benefits) of the Internal Revenue Code shall be operative for purposes of this chapter, except that the provision in section 132(f)(2) that equalizes the dollar amounts for sections 132(f)(2)(A) and (B) after February 17, 2009, until January 1, 2011, shall not be operative and except that section 132(n) shall not apply to United States Department of Defense Homeowners Assistance Program payments authorized by the American Recovery and Reinvestment Act of 2009.
- ~~[(g)]~~ (h) Section 163 (with respect to interest) of the Internal Revenue Code shall be operative for the purposes of this chapter, except that provisions in section 163(d)(4)(B) (defining net investment income to exclude dividends), section 163(e)(5)(F) (suspension of applicable high-yield discount obligation (AHYDO) rules) and section 163(i)(1) as it applies to debt instruments issued after January 1, 2010, (defining AHYDO) shall not be operative for the purposes of this chapter.
- ~~[(h)]~~ (i) Section 164 (with respect to taxes) of the Internal Revenue Code shall be operative for the purposes of this chapter, except that sections 164(a)(6), 164(b)(5), and 164(b)(6) shall not be operative for the purposes of this chapter.
- ~~[(i)]~~ (j) Section 165 (with respect to losses) of the Internal Revenue Code shall be operative for purposes of this chapter, except that the amount prescribed by sections 165(h)(1) (relating to the limitation per casualty) of the Internal Revenue Code shall be a \$100 limitation per casualty, and sections 165(h)(3)(A) and

165(h)(3)(B) (both of which relate to special rules for personal casualty gains and losses in federally declared disasters) of the Internal Revenue Code shall not be operative for the purposes of this chapter. Section 165 as operative for this chapter shall also apply to losses sustained from the sale of stocks or other interests issued through the exercise of the stock options or warrants granted by a qualified high technology business as defined in section 235-7.3.

~~[(f)]~~ (k) Section 168 (with respect to the accelerated cost recovery system) of the Internal Revenue Code shall be operative for purposes of this chapter, except that sections 168(j) (relating to property on Indian reservations), 168(k) (relating to the special allowance for certain property acquired during the period specified therein), 168(m) (relating to the special allowance for certain reuse and recycling property), and 168(n) (relating to the special allowance for qualified disaster assistance property) of the Internal Revenue Code shall not be operative for purposes of this chapter.

~~[(k)]~~ (l) Section 172 (with respect to net operating loss deductions) of the Internal Revenue Code shall be operative for purposes of this chapter, as further provided in section 235-7(d), except that sections 172(b)(1)(J) and 172(j) (both of which relate to qualified disaster losses) of the Internal Revenue Code shall not be operative for purposes of this chapter.

~~[(f)]~~ (m) Section 179 (with respect to the election to expense certain depreciable business assets) of the Internal Revenue Code shall be operative for purposes of this chapter, except ~~[that provisions relating to:~~

- ~~(1) The increase of the maximum deduction to \$100,000 for taxable years beginning after 2002 and before 2008, and the increase of the maximum deduction to \$125,000 for taxable years beginning after 2006 and before 2011, in section 179(b)(1);~~
- ~~(2) The increase of the qualifying investment amount to \$400,000 for taxable years beginning after 2002 and before 2008, and the increase of the qualifying investment amount to \$500,000 for taxable years beginning after 2006 and before 2011, in section 179(b)(2);~~
- ~~(3) The increase of the maximum deduction to \$250,000 and the increase of the qualifying investment amount to \$800,000 for taxable years beginning in 2008 or 2009, in section 179(b)(7);]~~ as provided in this subsection:
- (1) The aggregate cost provided in section 179(b)(1) which may be taken into account under section 179(a) for any taxable year shall not exceed \$25,000;
- (2) The amount at which the reduction in limitation provided in section 179(b)(2) begins shall exceed \$200,000 for any taxable year; and
- (3) The following shall not be operative for purposes of this chapter:
- ~~[(4)]~~ (A) Defining section 179 property to include computer software in section 179(d)(1);
- ~~[(5)]~~ (B) Inflation adjustments in section 179(b)(5);
- ~~[(6)]~~ (C) Irrevocable election in section 179(c)(2); and
- ~~[(7)]~~ (D) Special rules for qualified disaster assistance property in section 179(e);

~~shall not be operative for the purposes of this chapter].~~

~~[(m)]~~ (n) Section 198A (with respect to the expensing of qualified disaster assistance expenses) of the Internal Revenue Code shall not be operative for purposes of this chapter.

~~[(n)]~~ (o) Section 219 (with respect to retirement savings) of the Internal Revenue Code shall be operative for the purpose of this chapter. For the purpose of computing the limitation on the deduction for active participants in certain

pension plans for state income tax purposes, adjusted gross income as used in section 219 as operative for this chapter means federal adjusted gross income.

~~[(e)]~~ (p) Section 220 (with respect to medical savings accounts) of the Internal Revenue Code shall be operative for the purpose of this chapter, but only with respect to medical services accounts that have been approved by the Secretary of the Treasury of the United States.

~~[(p)]~~ (q) Section 265 (with respect to expenses and interest relating to tax-exempt income) of the Internal Revenue Code shall be operative for purposes of this chapter; except that sections 265(b)(3)(G) and 265(b)(7) shall not be operative and that section 265 shall not apply to expenses for royalties and other income derived from any patents, copyrights, and trade secrets by an individual or a qualified high technology business as defined in section 235-7.3. Such expenses shall be deductible.

~~[(q)]~~ (r) Section 382 (with respect to limitation on net operating loss carryforwards and certain built-in losses following ownership change) of the Internal Revenue Code shall be operative for the purposes of this chapter, except that section 382(n) shall not be operative for purposes of this chapter.

~~[(r)]~~ (s) Section 408A (with respect to Roth Individual Retirement Accounts) of the Internal Revenue Code shall be operative for the purposes of this chapter, except that section 408A(d)(3)(A)(iii) shall not be operative for purposes of this chapter. For the purposes of determining the aggregate amount of contributions to a Roth Individual Retirement Account or qualified rollover contribution to a Roth Individual Retirement Account from an individual retirement plan other than a Roth Individual Retirement Account, adjusted gross income as used in section 408A as operative for this chapter means federal adjusted gross income.

~~[(s)]~~ (t) In administering the provisions of sections 410 to 417 (with respect to special rules relating to pensions, profit sharing, stock bonus plans, etc.), sections 418 to 418E (with respect to special rules for multiemployer plans), and sections 419 and 419A (with respect to treatment of welfare benefit funds) of the Internal Revenue Code, the department of taxation shall adopt rules under chapter 91 relating to the specific requirements under such sections and to such other administrative requirements under those sections as may be necessary for the efficient administration of sections 410 to 419A.

In administering sections 401 to 419A (with respect to deferred compensation) of the Internal Revenue Code, Public Law 93-406, section 1017(i), shall be operative for the purposes of this chapter.

In administering section 402 (with respect to the taxability of beneficiary of employees' trust) of the Internal Revenue Code, the tax imposed on lump sum distributions by section 402(e) 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.

~~[(t)]~~ (u) In administering section 403 (with respect to taxation of employee annuities) of the Internal Revenue Code, any funds that represent pre-tax employee deferrals or contributions that are distributed from the annuity and used solely to obtain retirement credits under the state employees' retirement system shall not be treated as a rollover for purposes of section 403(b)(8)(A) of the Internal Revenue Code, and such funds shall be subject to income tax under this chapter.

~~[(u)]~~ (v) Section 451 (which provides general rules for taxable year of inclusion) of the Internal Revenue Code shall be operative, except that the provisions of sections 451(i)(3) and 451(i)(6), as they relate to a qualified electric utility, shall not be operative for purposes of this chapter.

~~[(v)]~~ (w) In administering section 457 (with respect to compensation plans of state and local governments and tax-exempt organizations) of the Internal Revenue Code, any funds that represent pre-tax employee deferrals or contributions that are distributed from the deferred compensation plan and used solely to obtain retirement credits under the state employees' retirement system shall not be treated as a rollover for purposes of section 457(e)(16)(A) of the Internal Revenue Code and such funds shall be subject to income tax under this chapter.

~~[(w)]~~ (x) Section 468B (with respect to special rules for designated settlement funds) 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 a rate equal to the maximum rate in effect for the taxable year imposed on estates and trusts under section 235-51.

~~[(x)]~~ (y) Section 469 (with respect to passive activities and credits limited) of the Internal Revenue Code shall be operative for the purposes of this chapter. For the purpose of computing the offset for rental real estate activities for state income tax purposes, adjusted gross income as used in section 469 as operative for this chapter means federal adjusted gross income.

~~[(y)]~~ (z) 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 in the computation thereof sections 235-3 to 235-5, and 235-7 (except subsection (c)), shall apply, and 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. Unrelated business taxable income shall not include any income from a prepaid 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.

~~[(z)]~~ (aa) Section 521 (with respect to cooperatives) and subchapter T (sections 1381 to 1388, with respect to cooperatives and their patrons) of the Internal Revenue Code shall be operative for the purposes of this chapter as to any cooperative fully meeting the requirements of section 421-23, except that Internal Revenue Code section 521 cooperatives need not be organized in Hawaii.

~~[(aa)]~~ (bb) Sections 527 (with respect to political organizations) and 528 (with respect to certain homeowners associations) of the Internal Revenue Code shall be operative for the purposes of this chapter and the taxes imposed in each section are hereby imposed by this chapter at the rates determined under section 235-71.

~~[(bb)]~~ (cc) Section 529 (with respect to qualified tuition programs) shall be operative for the purposes of this chapter, except that sections 529(c)(6) and 529(e)(3)(A)(iii) shall not be operative.

~~[(cc)]~~ (dd) Section 530 (with respect to education individual retirement accounts) of the Internal Revenue Code shall be operative for the purposes of this chapter. For the purpose of determining the maximum amount that a contributor could make to an education individual retirement account for state income tax purposes, modified adjusted gross income as used in section 530 as operative for this chapter means federal modified adjusted gross income as defined in section 530."

SECTION 5. Statutory material to be repealed is bracketed and stricken. New statutory material is underscored.

## **ACT 91**

**SECTION 6.** This Act shall take effect upon its approval; provided that the amendments made to section 235-2.4, Hawaii Revised Statutes, by section 4 of this Act shall not be repealed when section 235-2.4(a), Hawaii Revised Statutes, is repealed and reenacted on December 31, 2015, pursuant to section 6 of Act 60, Session Laws of Hawaii 2009.

(Approved June 9, 2011.)