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To: The Honorable Sylvia Luke, Chair;
The Honorable Ty J.K. Cullen, Vice Chair;
and Members of the House Committee on Finance

From: Rona M. Suzuki, Director
Department of Taxation

Re: S.B. 2920, S.D. 1, Relating to Conformity to the Internal Revenue Code

Date: Monday, June 29, 2020

Time: 2:00 P.M.

Place: Conference Room 329, State Capitol

The Department of Taxation (Department) strongly supports S.B. 2920, S.D.1.

S.B. 2920, S.D. 1, conforms Hawaii's income and estate and generation-skipping transfer taxes to the Internal Revenue Code (IRC) as of December 31, 2019. Hawaii Revised Statutes (HRS) sections 235-2.3(c) and 236E-4 require the Department to submit legislation to each regular session of the legislature to adopt the IRC as it exists on the December 31 preceding the regular session.

S.B. 2920, S.D. 1, amends HRS section 235-2.3(a) to conform the Hawaii income tax law to the operative IRC sections of subtitle A, chapter 1, as amended as of December 31, 2019. Subtitle A, chapter 1, refers to IRC sections 1-1400Z-2. S.B. 2920, S.D. 1, also amends HRS section 236E-3 to conform the Hawaii estate and generation-skipping transfer tax law to the operative IRC sections of subtitle B, as amended as of December 31, 2019. Generally, subtitle B contains the estate tax provisions and consists of IRC sections 2001-2801.

S.B. 2920, S.D. 1, currently contains the following amendments to conformity. The bill amends HRS section 235-2.4(ee) to remove the reference to IRC section 512(a)(7). This reference was added to HRS section 235-2.4(ee) in 2019 in response to the Tax Cuts and Jobs Act. However, the "Further Consolidated Appropriations Act, 2020," P. L. 116-94, enacted December 20, 2019 repealed IRC section 512(a)(7). Therefore, the Department recommends the reference to this provision be repealed. The change will have no substantive effect on any taxpayer.

In addition to P.L. 116-94, the Department reviewed the following tax measures enacted by the United States Congress during 2019 and determined no changes to conformity were necessary:

1. "Taxpayer First Act," P.L. 116-25, enacted July 1, 2019.
2. "Continuing Appropriations Act, 2020, and Health Extenders Act of 2019," P.L. 116-59, enacted September 27, 2019.
3. "Further Continuing Appropriations Act, 2020, and Further Health Extenders Act of 2019," P.L. 116-69, enacted November 21, 2019.
4. "Fostering Undergraduate Talent by Unlocking Resources for Education Act," P.L. 116-91, enacted December 19, 2019.
5. "National Defense Authorization Act for Fiscal Year 2020," P.L. 116-92, enacted December 20, 2019.

The Department recommends that this measure, be amended in several ways to address changes made to the IRC by the "Coronavirus Aid, Relief, and Economic Security Act" (CARES Act), P.L. 116-136, enacted March 27, 2020., as follows:

Amend HRS section 235-2.3(a) to conform the Hawaii income tax law to the operative IRC sections of subtitle A, chapter 1, as amended as of March 27, 2020. This can be done by amending the date on which the IRC is adopted to March 27, 2020.

Adopt certain tax related CARES Act amendments that are not amendments to the IRC itself, but are operative for Hawaii income tax purposes. These provisions are the:

1. Exclusion from gross income of loan amounts forgiven under the Paycheck Protection Program;
2. Increases to non-taxable loans from retirement plans;
3. Increases to certain charitable contributions limits; and
4. Exclusion from gross income of the amounts received as "recovery rebates" under the CARES Act (the stimulus payments).

To adopt these provisions, the Department recommends the following language be added to section 235-2.3(a):

"Sections 1106(i) (relating to exclusion of loan forgiveness from gross income), 2202(b) (relating to loans from retirement plans), and 2205 (relating to charitable contributions) of Public Law 116-136 shall be operative for purposes of this chapter. No amount received under section 2201 (relating to recovery rebates) of Public Law 116-136 shall be included in gross income for purposes of this chapter."

Make inoperative the CARES Act amendments to IRC sections 172 and 461 for Hawaii income tax purposes by conforming to these sections as they existed as of December 31, 2019. This will ensure that the repeal of the 80% limitation on net operating losses (NOLs), the carryback of NOLs arising in 2018, 2019, or 2020, and the deduction of excess business losses are not operative Hawaii income tax purposes.¹ The changes described above can be achieved by amending HRS

¹ Excess business loss is defined as deductible expenses that exceed aggregate gross income by \$250,000 or more.

section 235-2.4(n) and by adding a new HRS section 235-2.4(cc) to read as follows:

"(n) Section 172 (with respect to net operating loss deductions) of the Internal Revenue Code shall be operative for purposes of this chapter[7] in the form that it existed as of December 31, 2019, and as further provided in section 235-7(d) [7, except that section 172(b)(1)(J) and (j) (both of which relate to qualified disaster losses) of the Internal Revenue Code shall not be operative for purposes of this chapter.] ."

"(cc) Section 461 (with respect to the general rule for taxable year of deduction) of the Internal Revenue Code, shall be operative for purposes of this chapter in the form that it existed as of December 31, 2019."

In conjunction with the amendment HRS section 235-2.4(n), the following obsolete language relating to charitable contributions in HRS section 235-2.3(a) should be deleted:

~~"[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.]"~~

Thank you for the opportunity to provide testimony in support of this measure.

A BILL FOR AN ACT

RELATING TO CONFORMITY TO THE INTERNAL REVENUE CODE.

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

1 SECTION 1. The purpose of this Act is to conform Hawaii
2 income and estate and generation-skipping transfer tax laws to
3 the Internal Revenue Code.

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

6 "(a) For all taxable years beginning after December 31,
7 [~~2018,~~] 2019, as used in this chapter, except as provided in
8 section 235-2.35, "Internal Revenue Code" means subtitle A,
9 chapter 1, of the federal Internal Revenue Code of 1986, as
10 amended as of December 31, [~~2018,~~] 2019, as it applies to the
11 determination of gross income, adjusted gross income, ordinary
12 income and loss, and taxable income, except those provisions of
13 the Internal Revenue Code and federal public laws which,
14 pursuant to this chapter, do not apply or are otherwise limited
15 in application and except for the provisions of Public Law 109-
16 001 which apply to section 170 of the Internal Revenue Code.
17 The provisions of Public Law 109-001 to accelerate the deduction



1 for charitable cash contributions for the relief of victims of
2 the 2004 Indian Ocean tsunami are applicable for the calendar
3 year that ended December 31, 2004, and the calendar year ending
4 December 31, 2005.

5 Prior law shall continue to be used to determine:

6 (1) The basis of property, if a taxpayer first determined
7 the basis of property in a taxable year to which prior
8 law applies; and

9 (2) Gross income, adjusted gross income, ordinary income
10 and loss, and taxable income for a taxable year to
11 which prior law applies."

12 SECTION 3. Section 235-2.4, Hawaii Revised Statutes, is
13 amended by amending subsection (ee) to read as follows:

14 "(ee) Sections 512 to 514 (with respect to taxation of
15 business income of certain exempt organizations) of the Internal
16 Revenue Code shall be operative for the purposes of this chapter
17 as provided in this subsection.

18 "Unrelated business taxable income" means the same as in
19 the Internal Revenue Code, except that:

20 (1) In the computation of unrelated business taxable
21 income[+],



1 ~~[(A) Sections]~~ sections 235-3 to 235-5, and 235-7
 2 (except subsection (c)), shall apply; ~~[and~~
 3 ~~(B) Section 512(a)(7) shall not apply;]~~

- 4 (2) In the determination of the net operating loss
 5 deduction there shall not be taken into account any
 6 amount of income or deduction that is excluded in
 7 computing the unrelated business taxable income; and
 8 (3) Unrelated business taxable income shall not include
 9 any income from a legal service plan.

10 For a person described in section 401 or 501 of the
 11 Internal Revenue Code, as modified by section 235-2.3, the tax
 12 imposed by section 235-51 or 235-71 shall be imposed upon the
 13 person's unrelated business taxable income."

14 SECTION 4. Section 236E-3, Hawaii Revised Statutes, is
 15 amended to read as follows:

16 "**§236E-3 Conformance to the Internal Revenue Code; general**
 17 **application.** For all decedents dying, or transfers occurring,
 18 after December 31, ~~[2018]~~ 2019, as used in this chapter,
 19 "Internal Revenue Code" means subtitle B of the federal Internal
 20 Revenue Code of 1986, as amended as of December 31, ~~[2018]~~
 21 2019, as it applies to the determination of gross estate,



1 adjusted gross estate, federal taxable estate, and generation-
2 skipping transfers, except those provisions of the Internal
3 Revenue Code and federal public laws that, pursuant to this
4 chapter, do not apply or are otherwise limited in application."

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

7 SECTION 6. This Act shall take effect upon its approval;
8 provided that:

9 (1) Sections 2 and 3 shall apply to taxable years
10 beginning after December 31, 2019; and

11 (2) Section 4 shall apply to decedents dying or taxable
12 transfers occurring after December 31, 2019.



Report Title:

Conformity to the Internal Revenue Code for 2019; Income Tax;
Estate and Generation-skipping Transfer Tax

Description:

Conforms Hawaii income and estate and generation-skipping
transfer tax laws to the Internal Revenue Code of 1986, as
amended as of 12/31/2019. (SD1)

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

