July 12, 2016

The Honorable Ronald D. Kouchi,
President
and Members of the Senate
Twenty-Eighth State Legislature
State Capitol, Room 409
Honolulu, Hawai‘i 96813

The Honorable Joseph M. Souki,
Speaker and Members of the
House of Representatives
Twenty-Eighth State Legislature
State Capitol, Room 431
Honolulu, Hawai‘i 96813

Dear President Kouchi, Speaker Souki, and Members of the Legislature:

This is to inform you that on July 12, 2016, the following bill was signed into law:

HB1527 HD1 SD1 CD1 RELATING TO TAXATION
ACT 245 (16)

Sincerely,

DAVID Y. IGE
Governor, State of Hawai‘i
A BILL FOR AN ACT

RELATING TO TAXATION.

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

SECTION 1. The legislature finds that tax credits, exclusions, and deductions require periodic review to determine their tax expenditures, benefits, and continued merit and necessity. The legislature further finds that tax expenditures from the credits, exclusions, and deductions reduce revenues to the State. This requires ordinary taxpayers who do not benefit from the credits, exclusions, or deductions to compensate for the reduced revenues. Alternatively, funding for important state programs must be curtailed. The legislature further finds that good tax policy requires the equal treatment of similarly-situated taxpayers for the sake of equity and efficiency. When certain taxpayers receive special benefits to the detriment of others, it may generate resentment that leads to the loss of the general public's confidence in fair treatment by the state government.

However, the legislature also believes that certain tax credits, exclusions, and deductions are worthy of continuation for equity, efficiency, and economic and social policy. The
The legislature finds that independent review by the state auditor would help the legislature to identify and affirm the credits, exclusions, and deductions that represent good public policy. Accordingly, the purpose of this Act is to require the state auditor to periodically review certain tax credits, exclusions, and deductions for the income tax under chapter 235, Hawaii Revised Statutes, and the financial institutions tax under chapter 241, Hawaii Revised Statutes. The legislature finds that this Act is necessary to promote tax equity and efficiency, adequacy of state revenues, public transparency, and confidence in a fair state government.

SECTION 2. Chapter 23, Hawaii Revised Statutes, is amended by adding a new part to be appropriately designated and to read as follows:

"PART A. REVIEW OF TAX CREDITS, EXCLUSIONS, AND DEDUCTIONS

§23-A Review of certain credits, exclusions, and deductions under the income tax and financial institutions tax.

(a) The auditor shall conduct a review of the tax credits, exclusions, and deductions listed in sections 23-B to 23-F.

(b) In the review of a credit, exclusion, or deduction, the auditor shall:
(1) Determine the amount of tax expenditure for the credit, exclusion, or deduction for each of the previous three fiscal years;

(2) Estimate the amount of tax expenditure for the credit, exclusion, or deduction for the current fiscal year and the next two fiscal years;

(3) Determine whether the credit, exclusion, or deduction has achieved and continues to achieve the purpose for which it was enacted by the legislature;

(4) Determine whether the credit, exclusion, or deduction is necessary to promote or preserve tax equity or efficiency;

(5) If the credit, exclusion, or deduction was enacted because of its purported economic or employment benefit to the State:

(A) Determine whether a benefit has resulted, and if so, quantify to the extent possible the estimated benefit directly attributable to the credit, exclusion, or deduction; and
(B) Comment on whether the benefit, if any, outweighs
the cost of the credit, exclusion, or deduction;
and

(6) Estimate the annual cost of the credit, exclusion, or
deduction per low-income resident of the State. For
purposes of this paragraph, a "low-income resident of
the State" means an individual who is a resident of
the State and:

(A) Is the only member of a family of one and has an
income of not more than eighty per cent of the
area median income for a family of one; or

(B) Is part of a family with an income of not more
than eighty per cent of the area median income
for a family of the same size.

The cost shall be estimated by dividing the annual tax
expenditure for the credit, exclusion, or deduction
for each fiscal year under review by the number of
low-income residents of the State in the fiscal year.
The estimate determined pursuant to this paragraph is
intended to display the effect on low-income residents
of the State if they directly receive, either through
tax reduction or negative tax, the dollars saved by
elimination of the credit, exclusion, or deduction.

(c) Based on the review, the auditor shall recommend
whether the credit, exclusion, or deduction should be retained
without modification, amended, or repealed.

The auditor may recommend that a credit, exclusion, or
deduction be removed from review under sections 23-B to 23-F.
§23-B Review for 2019 and every fifth year thereafter.

(a) The credits under the income tax and financial institutions
tax listed in subsection (c) shall be reviewed in 2019 and every
fifth year thereafter.

(b) The auditor shall submit the findings and
recommendations of the reviews to the legislature and governor
at least twenty days prior to the convening of the immediately
following regular session.

(c) This section shall apply to the following:
(1) Sections 235-12.5 and 241-4.6--Credit for renewable
energy technology system installed and placed in
service in the State. For the purpose of section 23-
A(b)(5), this credit shall be deemed to have been
enacted for an economic benefit; and
(2) Section 235-17--Credit for qualified production costs incurred for a qualified motion picture, digital media, or film production.

§23-C Review for 2020 and every fifth year thereafter.

(a) The credits, exclusions, and deductions under the income tax and financial institutions tax listed in subsection (c) shall be reviewed in 2020 and every fifth year thereafter.

(b) The auditor shall submit the findings and recommendations of the reviews to the legislature and governor at least twenty days prior to the convening of the immediately following regular session.

(c) This section shall apply to the following:

(1) Section 235-7.3--Exclusion of royalties and other income derived from a patent, copyright, or trade secret of a qualified high technology business;

(2) Section 235-9.5--Exclusion for income and proceeds from stock options or stocks of a qualified high technology business or a holding company for a qualified high technology business;

(3) Sections 235-17.5 and 241-4.4--Credit for capital infrastructure costs;
(4) Sections 235-110.7 and 241-4.5--Credit for capital goods used by a trade or business;

(5) Section 235-110.91--Credit for research activity;

(6) Section 235-110.3--Credit for ethanol facility; and

(7) Section 241-3.5--Deduction for adjusted eligible net income of an international banking facility.

§23-D Review for 2021 and every fifth year thereafter.

(a) The credits and exclusions under the income tax listed in subsection (c) shall be reviewed in 2021 and every fifth year thereafter.

(b) The auditor shall submit the findings and recommendations of the reviews to the legislature and governor at least twenty days prior to the convening of the immediately following regular session.

(c) This section shall apply to the following:

(1) Section 235-4.5(a)--Exclusion of intangible income earned by a trust sited in this State;

(2) Section 235-4.5(b)--Exclusion of intangible income of a foreign corporation owned by a trust sited in this State;
(3) Section 235-4.5(c)--Credit to a resident beneficiary of a trust for income taxes paid by the trust to another state;

(4) Sections 235-55 and 235-129--Credit for income taxes paid by a resident taxpayer to another jurisdiction;

(5) Section 235-71(c)--Credit for a regulated investment company shareholder for the capital gains tax paid by the company;

(6) Section 235-110.6--Credit for fuel taxes paid by a commercial fisher;

(7) Section 235-110.93--Credit for important agricultural land qualified agricultural cost;

(8) Section 235-129(b)--Credit to S corporation shareholder for pro rata share of the tax credit earned by the S corporation in this State; and

(9) Section 209E-10--Credit for a qualified business in an enterprise zone; provided that the review of this credit pursuant to this part shall be limited in scope to income tax credits.

$23-E Review for 2022 and every fifth year thereafter.

(a) The credits and deductions under the income tax and
financial institutions tax listed in subsection (c) shall be reviewed in 2022 and every fifth year thereafter.

(b) The auditor shall submit the findings and recommendations of the reviews to the legislature and governor at least twenty days prior to the convening of the immediately following regular session.

c) This section shall apply to the following:

1. Section 235-5.5—Deduction for individual housing account deposit;
2. Section 235-7(f)—Deduction of property loss due to a natural disaster;
3. Section 235-16.5—Credit for cesspool upgrade, conversion, or connection;
4. Section 235-19—Deduction for maintenance of an exceptional tree;
5. Section 235-55.91—Credit for the employment of a vocational rehabilitation referral;
6. Section 235-110.2—Credit for in-kind services contribution for public school repair and maintenance;
(7) Sections 235-110.8 and 241-4.7--Credit for ownership of a qualified low-income housing building.

§23-F Review for 2023 and every fifth year thereafter.

(a) The credits under the income tax listed in subsection (c) shall be reviewed in 2023 and every fifth year thereafter.

(b) The auditor shall submit the findings and recommendations of the reviews to the legislature and governor at least twenty days prior to the convening of the immediately following regular session.

(c) This section shall apply to the following:

(1) Section 235-15--Credit for purchase of child passenger restraint system;

(2) Section 235-55.6--Credit for employment-related expenses for household and dependent care services;

(3) Section 235-55.7--Credit for a low-income household renter; and

(4) Section 235-55.85--Credit for food and excise tax."

SECTION 3. In codifying the new sections added by section 2 of this Act, the revisor of statutes shall substitute appropriate section numbers for the letters used in designating the new sections in this Act.
SECTION 4. This Act shall take effect on July 1, 2018.

APPROVED this 12 day of JUL, 2016

GOVERNOR OF THE STATE OF HAWAII