July 11, 2017

GOV. MSG. NO. 1291

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

The Honorable Scott K. Saiki,
Speaker and Members of the
House of Representatives
Twenty-Ninth State Legislature
State Capitol, Room 431
Honolulu, Hawai‘i 96813

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

This is to inform you that on July 11, 2017, the following bill was signed into law:

SB100 SD2 HD1 CD1 RELATING TO TAXATION
ACT 177 (17)

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 HAWAI'I:

SECTION 1. The legislature finds that, pursuant to Act 245, Session Laws of Hawaii 2016, beginning in 2019, the auditor is required to review certain credits, exclusions, and deductions under the income tax and financial institutions tax. Pursuant to Act 261, Session Laws of Hawaii 2016, beginning in 2018, the auditor is also required to review certain exemptions, exclusions, and credits under the general excise and use taxes, public service company tax, and insurance premium tax.

The legislature has chosen to delay the review schedules because relevant tax impact data may not be readily available in 2018. The department of taxation is undertaking a tax system modernization project that will be capable of efficiently collecting and reporting data on the tax expenditures from exemptions, exclusions, credits, and deductions. Thus, the legislature finds it prudent to delay the review schedules until after the tax system modernization project reaches a higher level of production.
The legislature also finds that the organic foods production tax credit should be added to the review schedule. The tax credit was established by Act 258, Session Laws of Hawaii 2016, and the schedule of income tax credit reviews was established by Act 245, Session Laws of Hawaii 2016. Because of the near simultaneous passage during the Regular Session of 2016 of the bills that became Acts 245 and 258, the organic foods production tax credit was not included in the review schedule of Act 245.

The legislature notes that the auditor has raised concerns regarding the criteria to be used to determine whether tax measures are achieving their legislative purpose. The auditor has indicated that the available legislative history is not helpful in identifying the purposes of some tax exemptions, exclusions, credits, and deductions, particularly the older ones. It is the legislature's intent to provide the auditor with more discretion in identifying the purpose of the exemptions, exclusions, credits, and deductions.

The purpose of this Act is to amend the provisions of the auditor's review of exemptions, exclusions, credits, and
deductions established under Acts 245 and 261, Session Laws of Hawaii 2016, by:

(1) Requiring the department of taxation to provide the auditor with any tax records that are necessary to conduct the reviews;

(2) Clarifying the review criteria regarding the achievement of the legislative purpose of the exemption, exclusion, credit, or deduction;

(3) Delaying the review schedules established under Act 245 and Act 261; and

(4) Adding the organic foods production tax credit that was enacted by Act 258, Session Laws of Hawaii 2016, to the review schedule.

SECTION 2. Chapter 231, Hawaii Revised Statutes, is amended by adding a new section to the part entitled "General Provisions" to be appropriately designated and to read as follows:

"§231- Auditor access to tax records or other information for reviews of exemptions, exclusions, credits, and deductions. (a) Notwithstanding any other law to the contrary, the department shall provide to the auditor any tax records and
other information maintained by the department that are requested by the auditor for the reviews of:

(1) Exemptions, exclusions, and credits under the general excise and use taxes, public service company tax, and insurance premium tax, as provided by chapter 23, part VI; and

(2) Credits, exclusions, and deductions under the income tax and financial institutions tax, as provided by chapter 23, part VII.

Any information provided to the auditor under this section marked confidential by the department shall be kept confidential by the auditor, except as provided in subsection (b).

(b) Notwithstanding any other law to the contrary, the auditor may include in a report of a review that is submitted to the legislature data that:

(1) The auditor deems necessary and relevant for the purpose of legislative review, including information received from the department of taxation pursuant to subsection (a); and
(2) Does not explicitly identify any specific taxpayer or beneficiary of a tax exemption, exclusion, credit, or deduction;

provided that any information marked confidential by the department shall be kept confidential by the legislature."

SECTION 3. Section 23-71, Hawaii Revised Statutes, is amended by amending subsection (b) to read as follows:

"(b) In the review of an exemption, exclusion, or credit, the auditor shall:

(1) Determine the amount of tax expenditure for the exemption, exclusion, or credit for each of the previous three [fiscal] calendar years;

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

(3) Determine, to the extent possible, whether the exemption, exclusion, or credit has achieved and continues to achieve the purpose for which it was enacted by the legislature[†], as reasonably identified by the auditor;
(4) Determine whether the exemption, exclusion, or credit is necessary to promote or preserve tax equity or efficiency;

(5) If the exemption, exclusion, or credit 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 exemption, exclusion, or credit; and

(B) Comment on whether the benefit, if any, outweighs the cost of the exemption, exclusion, or credit; and

(6) Estimate the annual cost of the exemption, exclusion, or credit 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 exemption, exclusion, or credit for each [fiscal] calendar year under review by the number of low-income residents of the State in the [fiscal] calendar 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 exemption, exclusion, or credit."

SECTION 4. Section 23-72, Hawaii Revised Statutes, is amended by amending its title and subsection (a) to read as follows:

"§23-72 Review for [2018] 2019 and every tenth year thereafter. (a) The exemptions and exclusions under the general excise and use taxes listed in subsection (c) shall be reviewed in [2018] 2019 and every tenth year thereafter."
SECTION 5. Section 23-73, Hawaii Revised Statutes, is amended by amending its title and subsection (a) to read as follows:

"[\text{Title}]§23-73[\text{Title}]  Review for 2020 and every tenth year thereafter.  (a) The exemptions, exclusions, and credits under the general excise tax listed in subsection (c) shall be reviewed in 2020 and every tenth year thereafter."

SECTION 6. Section 23-74, Hawaii Revised Statutes, is amended by amending its title and subsection (a) to read as follows:

"[\text{Title}]§23-74[\text{Title}]  Review for 2021 and every tenth year thereafter.  (a) The exemptions and exclusions under the general excise tax, public service company tax, or insurance premium tax listed in subsection (c) shall be reviewed in 2021 and every tenth year thereafter."

SECTION 7. Section 23-75, Hawaii Revised Statutes, is amended by amending its title and subsection (a) to read as follows:

"[\text{Title}]§23-75[\text{Title}]  Review for 2022 and every tenth year thereafter.  (a) The exemptions or exclusions under the general
excise and use taxes listed in subsection (c) shall be reviewed
in [2022] 2022 and every tenth year thereafter."

SECTION 8. Section 23-76, Hawaii Revised Statutes, is
amended by amending its title and subsection (a) to read as
follows:

"[§23-76] Review for [2022] 2023 and every tenth year
thereafter. (a) The exemptions or exclusions under the general
excise tax listed in subsection (c) shall be reviewed in [2022]
2023 and every tenth year thereafter."

SECTION 9. Section 23-77, Hawaii Revised Statutes, is
amended by amending its title and subsection (a) to read as
follows:

"[§23-77] Review for [2023] 2024 and every tenth year
thereafter. (a) The exemptions or exclusions under the general
excise and use taxes listed in subsection (c) shall be reviewed
in [2023] 2024 and every tenth year thereafter."

SECTION 10. Section 23-78, Hawaii Revised Statutes, is
amended by amending its title and subsection (a) to read as
follows:

"[§23-78] Review for [2024] 2025 and every tenth year
thereafter. (a) The exemptions or exclusions under the general
excise tax listed in subsection (c) shall be reviewed in [2025] 2025 and every tenth year thereafter."

SECTION 11. Section 23-79, Hawaii Revised Statutes, is amended by amending its title and subsection (a) to read as follows:

"[+]§23-79[+] Review for [2025] 2026 and every tenth year thereafter. (a) The exemptions, exclusions, or credits under the general excise and use taxes and insurance premium tax listed in subsection (c) shall be reviewed in [2025] 2026 and every tenth year thereafter."

SECTION 12. Section 23-80, Hawaii Revised Statutes, is amended by amending its title and subsection (a) to read as follows:

"[+]§23-80[+] Review for [2026] 2027 and every tenth year thereafter. (a) The exemptions or exclusions under the general excise and use taxes listed in subsection (c) shall be reviewed in [2026] 2027 and every tenth year thereafter."

SECTION 13. Section 23-81, Hawaii Revised Statutes, is amended by amending its title and subsection (a) to read as follows:
"[\(\text{\$23-81[\_]}\)] \text{Review for [2027] 2028 and every tenth year thereafter. (a) The exemptions or exclusions under the general excise tax listed in subsection (c) shall be reviewed in [2027] 2028 and every tenth year thereafter."

SECTION 14. Section 23-91, Hawaii Revised Statutes, is amended by amending subsection (b) to read as follows:

"(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] calendar years;

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

(3) Determine, to the extent possible, whether the credit, exclusion, or deduction has achieved and continues to achieve the purpose for which it was enacted by the legislature[\(\text{\(\text{\(\_\)}}\)], as reasonably identified by the auditor;
(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 calendar year under review by the number of low-income residents of the State in the calendar 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."

SECTION 15. Section 23-92, Hawaii Revised Statutes, is amended by amending its title and subsection (a) to read as follows:

"[+]§23-92[+] Review for [2019] 2020 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] 2020 and every fifth year thereafter."
SECTION 16. Section 23-93, Hawaii Revised Statutes, is amended by amending its title and subsection (a) to read as follows:

"§23-93 Review for [2020] 2021 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] 2021 and every fifth year thereafter."

SECTION 17. Section 23-94, Hawaii Revised Statutes, is amended as follows:

1. By amending its title and subsection (a) to read:

"§23-94 Review for [2021] 2022 and every fifth year thereafter. (a) The credits and exclusions under the income tax listed in subsection (c) shall be reviewed in [2021] 2022 and every fifth year thereafter."

2. By amending subsection (c) to read:

"(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 235-110.94--Credit for organically produced agricultural products;

(9) Section 235-129(b)--Credit to a shareholder of an S corporation for the shareholder's pro rata share of the tax credit earned by the S corporation in this State; and
(10) 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."

SECTION 18. Section 23-95, Hawaii Revised Statutes, is amended by amending its title and subsection (a) to read as follows:

"[±]§23-95[±] Review for [2022] 2023 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] 2023 and every fifth year thereafter."

SECTION 19. Section 23-96, Hawaii Revised Statutes, is amended by amending its title and subsection (a) to read as follows:

"[±]§23-96[±] Review for [2023] 2024 and every fifth year thereafter. (a) The credits under the income tax listed in subsection (c) shall be reviewed in [2023] 2024 and every fifth year thereafter."

SECTION 20. Statutory material to be repealed is bracketed and stricken. New statutory material is underscored.
SECTION 21. This Act shall take effect upon its approval.

APPROVED this 11 day of JUL, 2017

David Ige
GOVERNOR OF THE STATE OF HAWAII
THE SENATE OF THE STATE OF HAWAII

Date: May 2, 2017
Honolulu, Hawaii 96813

We hereby certify that the foregoing Bill this day passed Final Reading in the Senate of the Twenty-ninth Legislature of the State of Hawaii, Regular Session of 2017.

President of the Senate

Clerk of the Senate
THE HOUSE OF REPRESENTATIVES OF THE STATE OF HAWAII

Date: May 2, 2017
Honolulu, Hawaii

We hereby certify that the above-referenced Bill on this day passed Final Reading in the
House of Representatives of the Twenty-Ninth Legislature of the State of Hawaii, Regular
Session of 2017.

Joseph M. Souki
Speaker
House of Representatives

Brian L. Takeshita
Chief Clerk
House of Representatives