July 9, 2019

The Honorable Ronald D. Kouchi,
President
and Members of the Senate
Thirtieth State Legislature
State Capitol, Room 409
Honolulu, Hawai'i 96813

The Honorable Scott K. Saiki,
Speaker and Members of the
House of Representatives
Thirtieth State Legislature
State Capitol, Room 431
Honolulu, Hawai'i 96813

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

I am transmitting herewith SB301 SD1 HD1 CD1, without my approval and with the statement of objections relating to the measure.

SB301 SD1 HD1 CD1

RELATING TO TAXATION OF REAL ESTATE INVESTMENT TRUSTS.

Sincerely,

David Y. Ige
Governor, State of Hawai'i
STATEMENT OF OBJECTIONS TO SENATE BILL NO. 301

Honorable Members
Thirtieth Legislature
State of Hawai‘i

Pursuant to Section 16 of Article III of the Constitution of the State of Hawai‘i, I am returning herewith, without my approval, Senate Bill No. 301, entitled "A Bill for an Act Relating to Taxation of Real Estate Investment Trusts."

The purpose of this bill is to repeal the deduction for dividends paid taken by a Real Estate Investment Trust ("REIT") that is subject to Hawai‘i income taxes.

This bill is objectionable because it could discourage the business community from investing in Hawai‘i. Disallowing the dividends paid deduction for REITs could potentially stifle economic development and scare away investment capital to address our aging infrastructure. From an economic development perspective, REITs provide stable economic growth and long-term benefits – including job creation – that will extend the supply chain into rental and commercial properties.

The benefits of continuing with this federally established legislation are clear and quantifiable. REITs are an important investment vehicle for all types of investments in Hawai‘i. If the state corporate income tax is imposed on a REIT, there may be negative impacts to the State’s economic health and business climate, such as the reduction of general excise, property and state income taxes.

Overall, the unintended consequences of imposing a corporate tax on REITs, are not worth the potential benefits. Hawai‘i needs to be a place that is able to attract investment capital in order to create jobs and a sustainable economy.
For the foregoing reasons, I am returning Senate Bill No. 301 without my approval.

Respectfully,

David Y. Ige
DAVID Y. IGE
Governor of Hawai‘i
A BILL FOR AN ACT

RELATING TO TAXATION OF REAL ESTATE INVESTMENT TRUSTS.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF HAWAI'I:

SECTION 1. Section 235-2.3, Hawaii Revised Statutes, is amended by amending subsection (b) to read as follows:

"(b) The following Internal Revenue Code subchapters, parts of subchapters, sections, subsections, and parts of subsections shall not be operative for the purposes of this chapter, unless otherwise provided:

(1) Subchapter A (sections 1 to 59A) (with respect to determination of tax liability), except section 1(h)(2) (relating to net capital gain reduced by the amount taken into account as investment income), except sections 2(a), 2(b), and 2(c) (with respect to the definition of "surviving spouse" and "head of household"), except section 41 (with respect to the credit for increasing research activities), except section 42 (with respect to low-income housing credit), except sections 47 and 48, as amended, as of December 31, 1984 (with respect to certain depreciable tangible personal property), and except section
48(d)(3), as amended, as of February 17, 2009 (with respect to the treatment of United States Department of Treasury grants made under section 1603 of the American Recovery and Reinvestment Tax Act of 2009). For treatment, see sections 235-110.91, 235-110.7, and 235-110.8;

(2) Section 78 (with respect to dividends received from certain foreign corporations by domestic corporations choosing foreign tax credit);

(3) Section 86 (with respect to social security and tier 1 railroad retirement benefits);

(4) Section 91 (with respect to certain foreign branch losses transferred to specified 10-percent owned foreign corporations);

(5) Section 103 (with respect to interest on state and local bonds). For treatment, see section 235-7(b);

(6) Section 114 (with respect to extraterritorial income). For treatment, any transaction as specified in the transitional rule for 2005 and 2006 as specified in the American Jobs Creation Act of 2004 section 101(d) and any transaction that has occurred pursuant to a
binding contract as specified in the American Jobs
Creation Act of 2004 section 101(f) are inoperative;

(7) Section 120 (with respect to amounts received under
qualified group legal services plans). For treatment,
see section 235-7(a)(9) to (11);

(8) Section 122 (with respect to certain reduced uniformed
services retirement pay). For treatment, see section
235-7(a)(3);

(9) Section 135 (with respect to income from United States
savings bonds used to pay higher education tuition and
fees). For treatment, see section 235-7(a)(1);

(10) Section 139C (with respect to COBRA premium
assistance);

(11) Subchapter B (sections 141 to 150) (with respect to
tax exemption requirements for state and local bonds);

(12) Section 151 (with respect to allowance of deductions
for personal exemptions). For treatment, see section
235-54;

(13) Section 179B (with respect to expensing of capital
costs incurred in complying with Environmental
Protection Agency sulphur regulations);
(14) Section 181 (with respect to special rules for certain film and television productions);

(15) Section 196 (with respect to deduction for certain unused investment credits);

(16) Section 199 (with respect to the U.S. production activities deduction);

(17) Section 199A (with respect to qualified business income);

(18) Section 222 (with respect to qualified tuition and related expenses);

(19) Sections 241 to 247 (with respect to special deductions for corporations). For treatment, see section 235-7(c);

(20) Section 250 (with respect to foreign-derived intangible income and global intangible low-taxed income);

(21) Section 267A (with respect to certain related party amounts paid or accrued in hybrid transactions or with hybrid entities);
(22) Section 280C (with respect to certain expenses for which credits are allowable). For treatment, see section 235-110.91;

(23) Section 291 (with respect to special rules relating to corporate preference items);

(24) Section 367 (with respect to foreign corporations);

(25) Section 501(c)(12), (15), (16) (with respect to exempt organizations); except that section 501(c)(12) shall be operative for companies that provide potable water to residential communities that lack any access to public utility water services;

(26) Section 515 (with respect to taxes of foreign countries and possessions of the United States);

(27) Subchapter G (sections 531 to 565) (with respect to corporations used to avoid income tax on shareholders);

(28) Subchapter H (sections 581 to 597) (with respect to banking institutions), except section 584 (with respect to common trust funds). For treatment, see chapter 241;
(29) Section 642(a) and (b) (with respect to special rules for credits and deductions applicable to trusts). For treatment, see sections 235-54(b) and 235-55;

(30) Section 646 (with respect to tax treatment of electing Alaska Native settlement trusts);

(31) Section 668 (with respect to interest charge on accumulation distributions from foreign trusts);

(32) Subchapter L (sections 801 to 848) (with respect to insurance companies). For treatment, see sections 431:7-202 and 431:7-204;

(33) Section 853 (with respect to foreign tax credit allowed to shareholders). For treatment, see section 235-55;

(34) Section 853A (with respect to credits from tax credit bonds allowed to shareholders);

(35) Section 857(b)(2)(B) (with respect to the dividends paid deduction for real estate investment trusts);

(36) Subchapter N (sections 861 to 999) (with respect to tax based on income from sources within or without the United States), except sections 985 to 989 (with respect to foreign currency transactions). For
treatment, see sections 235-4, 235-5, and 235-7(b),
and 235-55;

Section 1042(g) (with respect to sales of stock
in agricultural refiners and processors to eligible
farm cooperatives);

Section 1055 (with respect to redeemable ground
rents);

Section 1057 (with respect to election to treat
transfer to foreign trust, etc., as taxable exchange);

Sections 1291 to 1298 (with respect to treatment
of passive foreign investment companies);

Subchapter Q (sections 1311 to 1351) (with
respect to readjustment of tax between years and
special limitations);

Subchapter R (sections 1352 to 1359) (with
respect to election to determine corporate tax on
certain international shipping activities using per
ton rate);

Subchapter U (sections 1391 to 1397F) (with
respect to designation and treatment of empowerment
zones, enterprise communities, and rural development investment areas). For treatment, see chapter 209E;

[43+] (44) Subchapter W (sections 1400 to 1400C) (with respect to District of Columbia enterprise zone);

[44+] (45) Section 14000 (with respect to education tax benefits);

[45+] (46) Section 1400P (with respect to housing tax benefits);

[46+] (47) Section 1400R (with respect to employment relief);

[47+] (48) Section 1400T (with respect to special rules for mortgage revenue bonds);

[48+] (49) Section 1400U-1 (with respect to allocation of recovery zone bonds);

[49+] (50) Section 1400U-2 (with respect to recovery zone economic development bonds);

[50+] (51) Section 1400U-3 (with respect to recovery zone facility bonds); and

[51+] (52) Subchapter Z (sections 1400Z-1 to 1400Z-2) (with respect to opportunity zones)."
SECTION 2. Section 235-71, Hawaii Revised Statutes, is amended by amending subsection (d) to read as follows:

"(d) In the case of a real estate investment trust there is imposed on the taxable income, computed as provided in sections 857 and 858 of the Internal Revenue Code but with the changes and adjustments made by this chapter (without prejudice to the generality of the foregoing, for taxable years beginning before January 1, 2020, the deduction for dividends paid is limited to [such] the amount of dividends as is attributable to income taxable under this chapter[+\text{ and, for taxable years beginning after December 31, 2019, no deductions for dividends paid shall be allowed}], a tax consisting in the sum of the following: 4.4 per cent if the taxable income is not over $25,000, 5.4 per cent if over $25,000 but not over $100,000, and on all over $100,000, 6.4 per cent. In addition to any other penalty provided by law any real estate investment trust whose tax liability for any taxable year is deemed to be increased pursuant to section 859(b)(2)(A) or 860(c)(1)(A) after December 31, 1978, (relating to interest and additions to tax determined with respect to the amount of the deduction for deficiency dividends allowed) of the Internal Revenue Code shall pay a
penalty in an amount equal to the amount of interest for which 
such trust is liable that is attributable solely to [such] the 
increase. The penalty payable under this subsection with 
respect to any determination shall not exceed one-half of the 
amount of the deduction allowed by section 859(a), or 860(a) 
after December 31, 1978, of the Internal Revenue Code for [such] 
the taxable year."

SECTION 3. Statutory material to be repealed is bracketed 
and stricken. New statutory material is underscored.

SECTION 4. This Act shall take effect upon its approval 
and shall apply to taxable years beginning after December 31, 
2019; provided that this Act shall be repealed on December 31, 
2023; provided further that sections 235-2.3(b) and 235-71(d), 
Hawaii Revised Statutes, shall be reenacted in the form in which 
they read prior to the effective date of this Act.

APPROVED this day of , 2019

GOVERNOR OF THE STATE OF HAWAII
THE SENATE OF THE STATE OF HAWAI‘I

Date: April 30, 2019
Honolulu, Hawaii 96813

We hereby certify that the foregoing Bill this day passed Final Reading in the Senate of the Thirtieth Legislature of the State of Hawai‘i, Regular Session of 2019.

President of the Senate

Clerk of the Senate
SB No. 301, SD 1, HD 1, CD 1

THE HOUSE OF REPRESENTATIVES OF THE STATE OF HAWAII

Date: April 30, 2019
Honolulu, Hawaii

We hereby certify that the above-referenced Bill on this day passed Final Reading in the House of Representatives of the Thirtieth Legislature of the State of Hawaii, Regular Session of 2019.

Scott K. Saiki
Speaker
House of Representatives

Brian L. Takeshita
Chief Clerk
House of Representatives