

JAN 17 2020

A BILL FOR AN ACT

RELATING TO TAXATION.

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

1 SECTION 1. The legislature finds that Hawaii's income tax
2 laws concerning real estate investment trusts should more
3 closely conform to federal tax law to create more consistency
4 with equitable tax policies.

5 In section 235-3, Hawaii Revised Statutes, the legislature
6 states its intent to adopt the Internal Revenue Code as then
7 amended, except that the legislature may choose to adopt none of
8 the amendments to the Internal Revenue Code or may provide that
9 certain amendments are limited in their operation.

10 The legislature further finds that real estate investment
11 trusts were given preferential tax status by the federal
12 government for the benefit of small investors to give them the
13 opportunity to invest in large scale income producing real
14 estate. The federal real estate investment trust provisions
15 allow a dividends paid deduction to the real estate investment
16 trust, thereby allowing the real estate investment trust itself
17 to not pay tax on income distributed to its shareholders, who



1 would then pay tax on that income. The federal real estate
2 investment trust provisions also provide for withholding of tax
3 by a real estate investment trust for non-residents or non-
4 citizens of the United States. Hawaii law conformed to the real
5 estate investment trust dividend paid provision in the 1960's,
6 but failed to adopt this provision for non-resident withholding.
7 This created an anomaly because a real estate investment trust
8 that does business in Hawaii, but pays dividends to shareholders
9 out of the state, results in no Hawaii income tax collected
10 either from the real estate investment trust or from its
11 shareholders, due to the fact that shareholders pay any tax on
12 dividends to the state in which they reside, not where the
13 income was generated.

14 The legislature additionally finds that real estate
15 investment trusts in Hawaii now own real estate assets of about
16 \$17 billion, generating an annual income of \$1 billion, which,
17 if taxed at the current corporate rate assessed to all other
18 corporations, would generate Hawaii taxes of \$64 million per
19 year. A 2016 analysis conducted by the department of business,
20 economic development, and tourism concluded that the State had
21 foregone about \$36 million in income tax in year 2014 due to



1 this anomaly, and that the amount of real estate investment
2 trust investments has risen substantially since 2014.

3 Some real estate investment trust shareholders live in
4 Hawaii, but a substantial majority do not. Further, while real
5 estate investment trusts own more real estate in Hawaii per
6 capita than in any other state, Hawaii ranks fortieth in the
7 nation for the number of real estate investment trust
8 shareholders as a percentage of the population. Additional
9 studies show that Hawaii is in the worst situation in this
10 regard, compared to any other state in the country. As a
11 result, many real estate investment trusts and their
12 shareholders pay a mere fraction of the Hawaii state income tax
13 compared to what other corporations pay.

14 The legislature therefore finds that it would be more
15 equitable to now adopt a withholding provision like the federal
16 system so that real estate investment trusts and their
17 shareholders, like all other corporations and business entities
18 doing real estate business in Hawaii, pay a fair tax burden
19 commensurate with the substantial privileges and resources in
20 Hawaii that were utilized to generate their profits. Real
21 estate investment trusts would still continue to receive their



1 generous federal and Hawaii income tax exemptions and continue
2 to benefit from Hawaii's low property tax rates.

3 Accordingly, the purpose of this Act is to, for taxable
4 years beginning after December 31, 2020:

5 (1) Require that real estate investment trusts file
6 returns reporting their shareholders' pro rata shares
7 of net income and net income attributable to this
8 State;

9 (2) Require withholding on all payments to shareholders;
10 and

11 (3) Appropriate funds to the department of taxation to
12 carry out the purposes of this Act.

13 SECTION 2. Chapter 235, Hawaii Revised Statutes, is
14 amended by adding a new section to part VI to be appropriately
15 designated and to read as follows:

16 "§235- Real estate investment trust returns; withholding
17 on dividends paid. (a) Every real estate investment trust
18 shall make a return for each taxable year, stating specifically:

19 (1) The items of its gross income and the deductions
20 allowable by this chapter;



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- 1 (2) The name, address, and social security or federal
- 2 identification number of each person owning stock in
- 3 the real estate investment trust at any time during
- 4 the taxable year;
- 5 (3) The number of shares of stock owned by each
- 6 shareholder at all times during the taxable year;
- 7 (4) The income attributable to the State and income not
- 8 attributable to the State with respect to each
- 9 shareholder as determined under this chapter;
- 10 (5) Any modifications required under this chapter;
- 11 (6) The amount of money and other property distributed by
- 12 the real estate investment trust during the taxable
- 13 year to each shareholder;
- 14 (7) The date of each distribution; and
- 15 (8) Any other information the department may prescribe by
- 16 form or rule.
- 17 (b) Each real estate investment trust shareholder's pro
- 18 rata share of income attributable to the State and the
- 19 shareholder's pro rata share of income not attributable to the
- 20 State, to the extent modified under this chapter, shall be taken
- 21 into account by the shareholder for the purposes of this chapter



1 under rules similar to those adopted pursuant to section 235-
2 122(c).

3 (c) The real estate investment trust, on or before the day
4 on which the return is filed, shall furnish to each person who
5 was a shareholder during the taxable year a copy of the
6 information shown on the return as the department may prescribe
7 by form or rule. Any return filed pursuant to this section, for
8 purposes of sections 235-111 and 235-112, shall be treated as a
9 return filed by the real estate investment trust under section
10 235-92.

11 (d) The department may permit composite returns and
12 payments to be made on behalf of resident shareholders.

13 (e) A real estate investment trust shall withhold and pay
14 to this State, on behalf of any shareholder, an amount equal to
15 six and four-tenths per cent multiplied by the amount of the
16 shareholder's pro rata share of the ordinary income and four per
17 cent of the capital gains attributable to the State, as
18 reflected on the real estate investment trust's return for the
19 taxable period. A real estate investment trust shall be
20 entitled to recover a payment made pursuant to this subsection
21 from the shareholder on whose behalf the payment was made.



1 (f) The amount withheld by a real estate investment trust
2 under subsection (e) shall be the minimum tax due to Hawaii by
3 each real estate investment trust shareholder on their Hawaii
4 source income. A real estate investment trust shareholder that
5 is not otherwise required to file Hawaii tax returns need not
6 file a Hawaii return to report the income received and tax paid.
7 Any real estate investment trust shareholder that is tax exempt
8 under federal income tax law shall not be liable for the minimum
9 tax on their real estate investment trust income and may file a
10 claim for refund for the amount withheld and paid to the State
11 by the real estate investment trust.

12 (g) Any amount paid by the real estate investment trust to
13 this State pursuant to subsection (e) shall be considered to be
14 a payment by the shareholder on account of the income tax
15 imposed on the shareholder for the taxable period.

16 (h) Any officer of any real estate investment trust who
17 wilfully fails to provide any information, file any return or
18 agreement, or make any payment as required by this section or
19 section 231-15.6 shall be guilty of a misdemeanor.

20 (i) Persons who are ultimately responsible for the payment
21 of the tax on any portion of the real estate investment trust's



1 income from dividend distributions due to ownership in pass
2 through entities shall be entitled to the credit for tax
3 withheld and paid by a real estate investment trust, whether the
4 person is a direct shareholder of the real estate investment
5 trust or not.

6 (j) As used in this section:

7 "Real estate investment trust" means a corporation, trust,
8 or association for which a valid election in accordance with
9 section 856 of the Internal Revenue Code, as amended, is in
10 effect."

11 SECTION 3. There is appropriated out of the general
12 revenues of the State of Hawaii the sum of \$ or so
13 much thereof as may be necessary for fiscal year 2020-2021 for
14 the purposes of reviewing and certifying returns and
15 withholdings.

16 The sum appropriated shall be expended by the department of
17 taxation for the purposes of this Act.

18 SECTION 4. New statutory material is underscored.

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1 SECTION 5. This Act, upon its approval, shall apply to
2 taxable years beginning after December 31, 2020.

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Report Title:

Taxation; Income Tax; Tax Returns; Real Estate Investment Trusts; Appropriation

Description:

Requires that real estate investment trusts file returns reporting their shareholders' pro rata shares of net income and net income attributable to this State. Requires withholding on all payments to shareholders. Appropriates funds. Applies to taxable years beginning after 12/31/2020.

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