
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 section 235-110.7,
2 Hawaii Revised Statutes, relating to the capital goods excise
3 tax credit, has been difficult to administer for both taxpayers
4 and the department of taxation because the section references
5 Internal Revenue Code provisions as of December 31, 1984. Since
6 1984, many of these Internal Revenue Code sections have been
7 repealed or substantially amended. To assist the administration
8 of this frequently used income tax credit, this Act amends
9 section 235-110.7, Hawaii Revised Statutes, to eliminate, to the
10 extent possible, references to outdated Internal Revenue Code
11 provisions. This Act is not intended to change the application
12 of section 235-110.7, Hawaii Revised Statutes.

13 In addition, federal and state case law on the federal
14 investment tax credit, which the capital goods excise tax credit
15 is based upon, has recognized that computer software is eligible
16 tangible personal property. This measure further clarifies that
17 computer software is eligible depreciable tangible personal



1 property in recognition of case law authority, notwithstanding a
2 contrary practice by the department of taxation.

3 SECTION 2. Chapter 235, Hawaii Revised Statutes, is
4 amended by adding a new part to be appropriately designated and
5 to read as follows:

6 "PART . CAPITAL GOODS EXCISE TAX CREDIT

7 §235-A Definitions. For purposes of this part:

8 "Alternative energy property" consists of the following
9 types of property:

- 10 (1) A boiler, the primary fuel for which shall be an
11 alternate substance. An alternate substance is any
12 substance other than oil, natural gas, or any product
13 of oil and natural gas;
- 14 (2) A burner, including necessary on-site equipment to
15 bring the alternate substance to the burner, for a
16 combustor other than a boiler if the primary fuel for
17 the burner will be an alternate substance;
- 18 (3) Equipment for turning an alternate substance into a
19 synthetic liquid, gaseous, or solid fuel;
- 20 (4) Equipment designed to modify existing equipment which
21 uses oil or natural gas as fuel or as feedstock so
22 that the existing equipment will use either a



1 substance other than oil and natural gas or oil mixed
2 with a substance other than oil and natural gas where
3 the other substance provides not less than twenty-five
4 per cent of the fuel or feedstock;

5 (5) Equipment to convert coal, including lignite, or any
6 non-marketable substance derived therefrom, into a
7 substitute for a petroleum or natural gas derived
8 feedstock for the manufacture of chemicals or other
9 products, or coal, including lignite, or any substance
10 derived therefrom, into methanol, ammonia, or a
11 hydroprocessed coal liquid or solid;

12 (6) Pollution control equipment required by federal,
13 state, or local law, ordinances, regulations, or rules
14 to be installed on or in connection with equipment
15 described in paragraphs (1) to (5);

16 (7) Equipment used for the unloading, transfer, storage,
17 reclaiming from storage, and preparation, including,
18 but not limited to, washing, crushing, drying, and
19 weighing, at the point of use for an alternate
20 substance for use in equipment described in paragraphs
21 (1) to (6). This includes equipment used for the



1 storage of fuel derived from garbage at the site at
2 which fuel was produced from garbage; and

- 3 (8) Equipment used to produce, distribute, or use energy
4 from a geothermal deposit, but only, in the case of
5 electricity generated by geothermal power, up to, but
6 not including, the electrical transmission state.

7 "Basis" means the cost of property.

- 8 (1) The basis of new eligible property which has been
9 constructed, reconstructed, or erected for the
10 taxpayer's use includes that portion of the cost of
11 the property that is subject to the imposition and
12 payment of tax at the rate of four per cent under
13 chapter 237 or 238.

- 14 (2) Whether the cost or other basis of the construction,
15 reconstruction, or erection is attributable to all or
16 part of a property placed in service may be determined
17 by engineering estimates or by cost accounting
18 records.

- 19 (3) In the case of reconstructed property, the cost of the
20 property does not include the adjusted basis of the
21 reconstructed property at the time the reconstruction
22 commences. However, the reconstructed property may



1 qualify as used eligible property, as discussed in
2 this section, and the cost of the property may include
3 the adjusted basis of the reconstructed property at
4 the time the reconstruction commences if the adjusted
5 basis of the property is subject to the imposition and
6 payment of tax at the rate of four per cent under
7 chapter 237 or 238.

8 (4) If constructed, reconstructed, or erected property is
9 placed in service over a span of more than one taxable
10 year, the credit shall be allowed to the taxpayer for
11 a particular taxable year with respect to so much of
12 the eligible property that is subject to the
13 imposition and payment of tax at the rate of four per
14 cent under chapter 237 or 238.

15 (5) Basis of used eligible property. The basis of used
16 eligible property is the cost of the property that is
17 subject to the imposition and payment of tax at the
18 rate of four per cent under chapter 237 or 238.

19 (6) In the case of a partnership, S corporation, estate,
20 or trust, the credit allowable is for eligible
21 property that is placed in service by the entity. The
22 basis upon which the credit is computed is determined



1 at the entity level. Each partner, S corporation
2 shareholder, or beneficiary of an estate or trust
3 shall separately take into account for its taxable
4 year with or within which the entity's taxable year
5 ends, the partner's, shareholder's, or beneficiary's
6 share of the basis and resulting credit. A partner's
7 share of the basis shall be determined in accordance
8 with the ratio in effect on the date on which the
9 eligible property is placed in service in which the
10 partners divide the general profits of the
11 partnership. The basis of partnership eligible
12 property that is subject to a special allocation that
13 is recognized under section 704(a) and 704(b) (with
14 respect to partner's distributive share) of the
15 Internal Revenue Code shall be recognized for purposes
16 of the credit, and an upward basis adjustment pursuant
17 to section 754 (with respect to manner of electing
18 optional adjustment to basis of partnership property)
19 of the Internal Revenue Code is not eligible for the
20 credit. A basis adjustment under section 754 (with
21 respect to manner of electing optional adjustment to
22 basis of partnership property) of the Internal Revenue



1 Code is not eligible for the credit because the
2 adjustment is not a transaction that is subject to the
3 imposition and payment of tax at the rate of four per
4 cent under chapter 237 or 238.

5 Each S corporation shareholder's basis of
6 eligible property is the shareholder's allocated share
7 of the corporation's basis in the eligible property.

8 A beneficiary's share of the basis is apportioned
9 between the entity and the beneficiaries, based on the
10 income of the entity allocable to each on the date the
11 eligible property is placed in service. The term
12 "beneficiary" includes an heir, legatee, or devisee.

13 (7) If a deduction is taken under section 179 (with
14 respect to election to expense certain depreciable
15 business assets) of the Internal Revenue Code the
16 portion of the basis of property for which the
17 deduction is taken is not considered in determining
18 the amount of credit allowable.

19 (8) For purposes of determining the amount of credit
20 available, the basis for vehicles subject to section
21 280F (with respect to limitations on depreciation for
22 luxury automobiles; limitations where certain property



1 is used for personal purposes) of the Internal Revenue
2 Code used predominantly for business purposes is
3 limited to an amount equal to the amount necessary to
4 obtain the maximum depreciation deduction allowed in
5 the first year for both luxury passenger automobiles
6 and trucks, vans and sport utility vehicles under
7 section 280F (with respect to limitations on
8 depreciation for luxury automobiles; limitations where
9 certain property is used for personal purposes) of the
10 Internal Revenue Code. Use is predominantly for
11 business purposes if over fifty per cent of the total
12 use is for business purposes. This limitation applies
13 before any percentage reduction for personal use, as
14 discussed in paragraph (9). If more than one taxpayer
15 has an interest in a vehicle subject to section 280F
16 (with respect to limitations on depreciation for
17 luxury automobiles; limitations where certain property
18 is used for personal purposes) of the Internal Revenue
19 Code they are treated as one taxpayer for purposes of
20 the basis limitation. The limitation shall be
21 apportioned among the taxpayers according to their
22 interests in the passenger automobile.



1 (9) Listed property shall not be treated as eligible
2 property, and the credit shall be denied if the listed
3 property does not satisfy the more-than-fifty per cent
4 business use test. If the qualified business use
5 satisfies the more-than-fifty per cent business use
6 test, but is not used one hundred per cent for
7 business, the amount of credit is limited to the
8 percentage of business use. The amount of credit
9 allowable in the taxable year in which the listed
10 property is placed in service is unaffected by any
11 increase in the business use percentage in a
12 subsequent year; provided that, if there is a
13 reduction in the business use of property, then the
14 credit taken with respect to the listed property may
15 be subject to recapture as provided in section
16 235-B(a).

17 "Biomass property" means property that is a boiler, the
18 primary fuel for which is an alternate substance, a burner,
19 including necessary on-site equipment to bring the alternate
20 substance to the burner, for a combustor other than a boiler if
21 the primary fuel will be an alternate substance, or equipment
22 for converting an alternate substance into a qualified fuel,



1 including equipment used to store fuel derived from garbage at
2 the site at which the fuel was produced from garbage. For
3 purposes of defining biomass property, an alternate substance
4 means any substance other than an inorganic substance and coal,
5 including lignite, or any coal product. Biomass property also
6 includes pollution control equipment that is required to be
7 installed on or in connection with the above equipment, as well
8 as equipment used for the unloading, transfer, storage,
9 reclaiming from storage, and preparation at point of use of an
10 alternate substance for use in that equipment.

11 "Building" means any structure or edifice that encloses a
12 space within its walls, and is usually covered by a roof. The
13 term also includes any such structure that is constructed by or
14 for a lessee, even if the structure must be removed, or
15 ownership of the structure reverts to the lessor at the
16 termination of the lease.

17 "Bulk storage" means the storage of a commodity in a large
18 mass before its consumption or use.

19 "Cogeneration equipment" means property which is an
20 integral part of a system for using the same fuel to produce
21 both qualified energy and electricity at an industrial or
22 commercial facility. For purposes of this definition, the term



1 "industrial" means the purification of water and the
2 desalinization of water.

3 "Computer software" means a pre-written set of instructions
4 or statements, which is capable of causing a computer to
5 indicate, perform, or achieve a particular function, task, or
6 result that has a general applicability and is made through a
7 non-exclusive license or other permission to use the pre-written
8 set of instructions, and which has not been prepared at the
9 special request of the purchaser to meet the purchaser's
10 particular needs.

11 "Credit" means the capital goods excise tax credit.

12 "Eligible property."

13 (1) Eligible property is defined as:

14 (A) Property which is tangible personal property or
15 other tangible property;

16 (B) Recovery property, within the meaning of section
17 168 (with respect to accelerated cost recovery
18 system) of the Internal Revenue Code without
19 regard to useful life, or any other property with
20 respect to which depreciation is allowable to the
21 taxpayer; and



1 (C) Property which has an estimated useful life or
2 recovery period, determined as of the time the
3 property is placed in service, of three years or
4 more. A property shall have the same estimated
5 useful life or recovery period as that which is
6 used for depreciation or accelerated cost
7 recovery system purposes.

8 (2) Property which is eligible for the credit is:

9 (A) New eligible property; or

10 (B) Used eligible property.

11 The terms "new eligible property" and "used eligible
12 property" are defined in this section.

13 (3) Tangible personal property, other than a central air
14 conditioning or a heating unit, may qualify as
15 eligible property regardless of whether it is used as
16 an integral part of an activity or constitutes a
17 research or storage facility used in connection with
18 such activity, as required for other tangible
19 property.

20 (4) Eligible property shall be either recovery property
21 within the meaning of section 168 (with respect to
22 accelerated cost recovery system) of the Internal



1 Revenue Code without regard to useful life, or any
2 other property with respect to which depreciation is
3 allowed by the taxpayer.

4 (A) If only part of a property is depreciable, only a
5 pro rata portion of the property may qualify as
6 eligible property.

7 (B) Property does not qualify as eligible property to
8 the extent that a deduction for depreciation
9 thereon is disallowed under section 274 (with
10 respect to disallowance of certain entertainment,
11 etc., expenses) of the Internal Revenue Code.

12 (5) Generally, any boiler, used in Hawaii, which is
13 primarily fueled by petroleum or petroleum products,
14 including natural gas, qualifies as eligible property.

15 (6) Energy property qualifies as eligible property.

16 (7) Certain classes of property that generally do not
17 qualify as eligible property and thereby are not
18 eligible for the credit include:

19 (A) A building or its structural components.

20 (B) Property purchased for use in a foreign trade
21 zone as defined in chapter 212.



1 (C) Property used by an organization which is exempt
2 from the tax imposed by this chapter, unless the
3 property is used predominantly in an unrelated
4 trade or business, the income from which is
5 subject to tax under this chapter.

6 (D) Intangible property.

7 (E) Property used for lodging.

8 (8) Exceptions to paragraph (7):

9 (A) A nonlodging commercial facility that is
10 available to persons not using the lodging
11 facility on the same basis as it is available to
12 tenants of the lodging facility may qualify as
13 eligible property.

14 (B) Property used by a hotel, motel, or other similar
15 establishment in connection with the trade or
16 business of furnishing lodging where more than
17 one half of the accommodation in the hotel,
18 motel, or other similar establishment is used by
19 transients may qualify as eligible property. An
20 accommodation shall be considered to accommodate
21 transients if the rental period is normally less
22 than thirty days.



1 (C) Coin-operated vending machines and coin-operated
2 washing machines and dryers may qualify as
3 eligible property.

4 (9) Eligible depreciable tangible personal property
5 includes computer software.

6 "Energy property" means certain property intended to reduce
7 the amount of oil, natural gas, or other energy consumed in
8 heating or cooling a building or used in an industrial process.

9 Energy property includes:

- 10 (1) Alternative energy property;
- 11 (2) Solar or wind energy property;
- 12 (3) Specially defined energy property;
- 13 (4) Recycling equipment;
- 14 (5) Hydroelectric generating property;
- 15 (6) Cogeneration equipment; and
- 16 (7) Biomass property.

17 "Hydroelectric generating property" means property
18 installed at a hydroelectric site which is:

- 19 (1) Equipment for increased capacity to generate
20 electricity by water up to, but not including, the
21 electrical transmission stage; and



1 (2) Structures for housing the generating equipment, fish
2 passageways, and dam rehabilitation property, required
3 by reason of the installation of equipment described
4 in paragraph (1) of this definition.

5 "Integral part" means property used directly in one of the
6 activities specified as a condition under which other tangible
7 property may be considered eligible property.

8 "Lease" is defined as it is for federal income tax
9 purposes.

10 "Listed property" means passenger automobiles and other
11 property used as a means of transportation; property generally
12 used for purposes of entertainment, recreation, or amusement;
13 computers and related peripheral equipment; and other property
14 as determined by the department of taxation.

15 "Manufacturing, production, and extraction" means:

16 (1) Construction, reconstruction, or making of property
17 out of scrap, salvage, junk, new, or raw material by
18 processing, manipulating, refining, or changing the
19 form of an article, or by combining or assembling two
20 or more articles;

21 (2) Cultivation of the soil;

22 (3) Raising of livestock; or



1 (4) Mining of minerals.

2 "More-than-fifty per cent business use test" means that
3 certain business use of listed property, referred to as
4 "qualified business use," must exceed fifty per cent. For
5 purposes of determining the more-than-fifty per cent business
6 use test, use in a trade or business does not include use in an
7 investment or other activity conducted for the production of
8 income. However, if the more-than-fifty-per-cent-business-use
9 test has been met, the percentage of investment use may be added
10 in when figuring the total business use for purposes of
11 calculating the amount of credit allowable.

12 "New eligible property" means property that qualifies under
13 at least one of the following conditions:

14 (1) The property is eligible property, the original use of
15 which commences with the taxpayer after the date the
16 taxpayer acquires it;

17 (2) The property is eligible property that is:

18 (A) Sold and leased back by the same taxpayer within
19 three months of the date the property was
20 originally placed in service by the taxpayer; or



1 (B) Leased to the same taxpayer within three months
2 of the date the property was originally placed in
3 service by that taxpayer; or

4 (3) The property is eligible property, the construction,
5 reconstruction, or erection of which is placed in
6 service by the taxpayer, but only with respect to that
7 portion of the basis as is discussed in paragraphs (1)
8 through (5) of the definition of "basis" in this
9 section. It is not necessary that the materials
10 entering into the construction, reconstruction, or
11 erection be new in use. Construction, reconstruction,
12 or erection begins when physical work is started on
13 the construction, reconstruction, or erection.

14 "Original use" means the first use to which the property is
15 put, whether or not it is the taxpayer's first use of the
16 property.

17 "Other tangible property" is tangible property, other than
18 tangible personal property that qualifies as eligible property
19 by meeting one of the following three conditions:

20 (1) The property is used as an integral part of
21 manufacturing, production, extraction, or furnishing



1 transportation, communication, electrical energy, gas
2 water, or sewage disposal services;

3 (2) The property is used as a research or storage facility
4 used in connection with an activity referred to in
5 paragraph (1); or

6 (3) The property is a facility used in connection with an
7 activity referred to in paragraph (1) for the bulk
8 storage of fungible commodities, including commodities
9 in a liquid or gaseous state.

10 "Placed in service" means property that is placed in
11 service in the earliest of the following taxable years:

12 (1) The taxable year in which the period for depreciation
13 with respect to the property begins;

14 (2) The taxable year in which, under the accelerated cost
15 recovery system, a claim for recovery allowances with
16 respect to the property begins; or

17 (3) The taxable year in which the property is placed in a
18 condition or state of readiness in this State and
19 available for a specifically assigned function by the
20 taxpayer.



1 In a sale-leaseback transaction, the property shall be
2 considered to be placed in service on the date the property was
3 first placed in service in this State by the seller-lessee.

4 "Property used for lodging" means property which is used
5 predominantly to furnish lodging; or in connection with the
6 furnishing of lodging.

7 (1) Property used predominantly to furnish lodging
8 includes that which is used in the living quarters of
9 a lodging facility such as, for example, beds, other
10 furniture, refrigerators, ranges, and other equipment.

11 (2) A lodging facility includes an apartment house, hotel,
12 motel, dormitory or other facility, or part of a
13 facility, where sleeping accommodations are provided
14 and let; provided that the term does not include a
15 facility which is used primarily as a means of
16 transportation such as, for example, an aircraft or
17 vessel, or to provide medical or convalescent
18 services, even though sleeping accommodations are
19 provided.

20 (3) Property used predominantly in connection with the
21 furnishing of lodging includes that which is used to
22 operate a lodging facility or to serve tenants,



1 whether furnished by the owner of the lodging facility
2 or another person; provided that property used in
3 furnishing, to the management of a lodging facility or
4 its tenants, electrical energy, water, sewage disposal
5 services, gas, telephone services or other similar
6 utility services shall not be treated as property used
7 in connection with the furnishing of lodging.

8 "Purchase" means an acquisition of property.

9 "Qualified business use" means use of listed property that
10 meets the more-than-fifty per cent business use test.

11 "Qualified energy" means steam, heat, or other forms of
12 useful energy, other than electric energy, to be used for
13 industrial, commercial, or space-heating purposes other than in
14 the production of electricity.

15 "Recapture period" means the period beginning on the first
16 day of the month the eligible property is placed in service in
17 Hawaii, and extending for a full three years.

18 "Recycling equipment" means any equipment that is used
19 exclusively to sort and prepare solid waste for recycling or in
20 the recycling of solid waste. The term recycling equipment does
21 not include any equipment used in a process after the first
22 marketable product is produced or in the case of recycling iron



1 or steel, any equipment used to reduce the waste to a molten
2 state, and in any process thereafter.

3 (1) Any equipment used in the recycling of material which
4 includes some virgin materials shall not be treated as
5 failing to meet the exclusive requirements of this
6 definition if the amount of the virgin materials is
7 ten per cent or less.

8 (2) The term recycling equipment includes any equipment
9 that is used in the conversion of solid waste into a
10 fuel or into useful energy such as steam, electricity,
11 or hot water.

12 "Sale-leaseback" is defined as it is for federal income tax
13 purposes.

14 "Sixty-six and two-third per cent rule" means that if a
15 partner's, shareholder's, or beneficiary's interest in the
16 entity is reduced below sixty-six and two-third per cent of
17 their interest at the time the credit was taken, a pro rata
18 share of the partner's, shareholder's, or beneficiary's interest
19 in the entity's eligible property shall cease to be eligible
20 property with respect to the partner, shareholder, or
21 beneficiary, and credit recapture shall be required.



1 "Solar or wind energy property" means any equipment which
2 uses solar or wind energy to generate electricity, heat or cool,
3 or provide hot water for use in a structure, or provide solar
4 process heat.

5 "Specially defined energy property" means property which is
6 installed in an existing industrial or commercial facility to
7 reduce the amount of energy consumed in the existing industrial
8 or commercial process.

9 "Specified percentage" means whichever of these two rules
10 applies: sixty-six and two-thirds per cent rule; or the
11 thirty-three and one-third per cent rule.

12 "Structural component" means parts of a building such as
13 walls, partitions, floors, ceilings, and permanent coverings;
14 all components of a central air conditioning or heating system;
15 plumbing and plumbing fixtures; electric wiring and lighting
16 fixtures, chimneys; stairs, escalators, and elevators. The term
17 structural component does not include property which is
18 contained in or attached to a building such as production
19 machinery, the sole justification for the installation of which
20 is to meet temperature or humidity requirements that are
21 essential for the operation of other machinery of the processing
22 of materials or foodstuffs. Machinery may also meet this sole



1 justification test even though it incidentally provides for the
2 comfort of employees, or serves, to an insubstantial degree,
3 areas where the temperature or humidity requirements are not
4 essential.

5 "Substantial interest" means when a transferor, or in a
6 case where the transferor is a partnership, estate or trust, or
7 S corporation, the partner, beneficiary, or shareholder, is
8 considered to have retained a substantial interest in the trade
9 or business if, after the change in form, the transferor's
10 interest in the trade or business is:

- 11 (1) Substantial in relation to the total income interest
12 of all the owners; or
- 13 (2) Equal to or greater than the transferor's interest
14 before the change in form.

15 A taxpayer shall not be considered to have retained a
16 substantial interest where the only basis for claiming
17 substantial interest is that the values of the interests
18 exchanged are equal. The determination of whether a taxpayer
19 has retained a substantial interest in the trade or business is
20 to be made immediately after the change in the form of
21 conducting the trade or business, and after each time the



1 taxpayer disposes of a portion of the taxpayer's interest in the
2 new enterprise.

3 "Tangible personal property" means any tangible property
4 except land and improvements thereto, such as buildings or other
5 inherently permanent structures, including items that are
6 structural, components of the buildings, or structures.

7 "Thirty-three and one-third per cent rule" means that once
8 there has been a recapture by reason of the sixty-six and
9 two-thirds per cent rule, there is no further recapture until
10 the partner's, shareholder's, or beneficiary's interest is
11 reduced to less than thirty-three and one-third per cent of its
12 interest at the time the credit was taken. Thereafter, any
13 reduction in interest, however small, shall again subject the
14 partner, shareholder, or beneficiary to the recapture
15 provisions.

16 "Transportation business" means airlines, bus companies,
17 shipping or trucking companies, and oil pipeline companies.

18 "Used eligible property" means property that is eligible
19 property as defined in this section and the property is not new
20 eligible property as defined in this subsection."

21 **§235-B Capital Goods excise tax credit allowed. (a)**

22 There shall be allowed to each taxpayer subject to the tax



1 imposed by this chapter a capital goods excise tax credit which
2 shall be deductible from the taxpayer's net income tax
3 liability, if any, imposed by this chapter for the taxable year
4 in which the credit is properly claimed, if the following
5 conditions are met:

- 6 (1) The taxpayer purchases or imports eligible property;
- 7 (2) The purchase or import of eligible property results in
8 a transaction that is subject to the imposition and
9 payment of tax at the rate of four per cent under
10 chapter 237 or 238;
- 11 (3) The eligible property is used by the taxpayer in a
12 trade or business; and
- 13 (4) The eligible property is placed in service within
14 Hawaii.

15 (b) The amount of the tax credit shall be four per cent of
16 the basis, as defined in section 235-A, of eligible property
17 used by the taxpayer in a trade or business and placed in
18 service in Hawaii. Any credit claimed under this section shall
19 be subject to the following limitations:

- 20 (1) In the case of eligible property for which a credit
21 for sales or use taxes paid to another state is
22 allowable under section 238-3(i), the amount of the



1 tax credit allowed under this section shall not exceed
2 the amount of use tax actually paid under chapter 238
3 relating to the tangible personal property.

4 (2) If a deduction is taken under section 179 (with
5 respect to election to expense certain depreciable
6 business assets) of the Internal Revenue Code, no tax
7 credit shall be allowed for that portion of the basis
8 of property for which the deduction was taken.

9 (3) If a taxpayer is eligible for both the income tax
10 credit under section 235-12.5, and the capital goods
11 excise tax credit for a particular solar or wind
12 energy property, the credit under section 235-12.5,
13 shall be deducted from the taxpayer's net income tax
14 liability before the capital goods excise tax credit.

15 (c) In the case of a partnership, S corporation, estate, or
16 trust, the tax credit allowable is for eligible property that is
17 placed in service in Hawaii by the entity. The basis upon which
18 the tax credit is computed shall be determined at the entity
19 level.

20 (d) If the capital goods excise tax credit allowed under
21 subsection (a) exceeds the taxpayer's net income tax liability,
22 the excess of credit over liability shall be refunded to the



1 taxpayer; provided that no refunds or payment on account of the
2 tax credit allowed by this section shall be made for amounts
3 less than \$1.

4 (e) All claims for tax credits under this section,
5 including any amended claims, shall be filed on or before the
6 end of the twelfth month following the close of the taxable year
7 for which the credits may be claimed. Failure to comply with
8 the foregoing provision shall constitute a waiver of the right
9 to claim the credit.

10 (f) The credit shall be allowed only for the first taxable
11 year in which the property is placed in service by the taxpayer.
12 If in the first taxable year in which a taxpayer places property
13 in service no portion of the property qualifies as eligible
14 property, no credit shall be allowed to the taxpayer with
15 respect to the property. If a portion of the property qualifies
16 as eligible property in the first year in which the property is
17 placed in service, then a credit only as to the portion that
18 qualifies shall be allowed to the taxpayer.

19 (g) Application for the capital goods excise tax credit
20 shall be upon forms provided by the department of taxation.

21 (h) The taxpayer shall treat the amount of credit
22 allowable and claimed as a taxable income item for the taxable



1 year in which it is properly recognized under the method of
2 accounting used to compute taxable income. Alternatively, the
3 basis of eligible property for depreciation or the accelerated
4 cost recovery system purposes for state income taxes shall be
5 reduced by the amount of credit allowable and claimed.

6 §235-C Recapture of credit. (a) Recapture of the
7 previously claimed credit applies where a recapture event occurs
8 under paragraph (2) and the percentage of credit provided in
9 paragraph (1) shall be included as income under chapter 235 or
10 241 in the year a recapture event occurs.

11 (1) Recapture percentage. Where the recovery property or
12 depreciable property ceases to be eligible property
13 within the following period, which constitutes a full
14 year after being placed in service, the accompanying
15 percentage shall be the recapture percentage:

Recapture period	Recapture percentage
One full year	100
Two full years	66
Three full years	33
Four full years	0

21 (2) Recapture event. A recapture event occurs when:



1 (A) Property ceases to be eligible property with
2 respect to a taxpayer. Property ceases to be
3 eligible property with respect to a taxpayer
4 when:

5 (i) The property ceases to be owned by taxpayer.
6 Recapture shall be triggered upon
7 disposition of the property.

8 (ii) The property ceases to be eligible property.
9 The cessation shall be treated as having
10 occurred on the first day of the taxable
11 year.

12 (B) There is a decrease in the business use of listed
13 property to less than fifty per cent. During the
14 recapture period, all or a portion of the credit
15 taken in an earlier year for listed property may
16 be subject to recapture if:

17 (i) The percentage of business use falls below
18 the percentage of business use for the year
19 the listed property was placed in service;
20 or

21 (ii) The listed property is converted from
22 business to personal use and does not



1 satisfy the more-than-fifty per cent
2 business use test.

3 (C) There is a decrease in basis of eligible
4 property. During the recapture period, all or a
5 portion of previously taken credit as determined
6 in paragraph (1) may be subject to recapture if
7 the basis of eligible property used to calculate
8 the credit decreases, either through a refund in
9 the purchase price or usage of the property for
10 personal purposes.

11 (b) Application of recapture rules to partnerships,
12 S corporations, estates, or trusts shall be as follows:

13 (1) In the case of a partnership, S corporation, estate,
14 or trust, the recapture rule applies to a partner,
15 shareholder, or beneficiary who originally received
16 the benefit of a credit if within the recapture
17 period:

18 (A) The S corporation, partnership, estate, or trust
19 disposes of eligible property;

20 (B) If eligible property otherwise ceases to be
21 eligible property in the hands of the entity; or



1 (C) The partner's, shareholder's, or beneficiary's
2 interest in the entity is reduced, for example,
3 by sale of interest in the entity, below a
4 specified percentage as defined in section 235-A.

5 (2) In making a recapture determination, there may be
6 taken into account any prior recapture determination
7 made with respect to the partner, shareholder, or
8 beneficiary in connection with the same property.

9 (c) Application of recapture rules to valid S corporation
10 election shall be as follows:

11 (1) If a C corporation makes a valid election under
12 section 235-2.4 to be an S corporation, then on the
13 last day of the taxable year immediately preceding the
14 first taxable year for which the election is
15 effective, any eligible property the basis of which
16 was taken into account to compute the C corporation's
17 credit allowable in taxable years before the first
18 taxable year for which the election is effective and
19 which has not been disposed of or otherwise ceased to
20 be eligible property with respect to the C corporation
21 before the last day shall be considered as having
22 ceased to be eligible property with respect to the



1 C corporation and the recapture rule shall apply.
2 However, the recapture rule shall not apply if the
3 S corporation and each of its shareholders on the
4 first day of the first taxable year for which the
5 election under section 235-2.4 is to be effective, or
6 on the date of the election, whichever is later,
7 execute an agreement as is described in paragraph (2).

8 (2) The agreement shall:

9 (A) Be signed by the shareholders; and on behalf of
10 the S corporation by a person who is duly
11 authorized;

12 (B) State that if eligible property for which the
13 credit was taken is later disposed of by, or
14 ceases to be eligible property with respect to
15 the S corporation during the recapture period and
16 during a taxable year for which the S election is
17 effective, each signer agrees to notify the
18 director of taxation of a disposition or
19 cessation and to be jointly and severally liable
20 to pay the director of taxation an amount equal
21 to the increase in tax provided by the recapture
22 rule;



- 1 (C) State the name, address, and taxpayer
2 identification number of each party to the
3 agreement;
- 4 (D) Be filed with the department of taxation for the
5 taxable year immediately preceding the first
6 taxable year for which the S election is
7 effective; and
- 8 (E) Be filed with the department of taxation on or
9 before the due date, including extensions of
10 time, of the return, unless the director of
11 taxation permits, upon a showing of good cause,
12 that the agreement may be filed on a later date.
- 13 (3) A shareholder's share of the amount of credit
14 recapture shall be determined as if the property had
15 ceased to be eligible property as of the last day of
16 the taxable year immediately preceding the first
17 taxable year for which the S election is effective;
18 provided that the recapture percentage shall be
19 determined as if the property ceased to be eligible
20 property on the date the property actually ceased to
21 be eligible property.



1 (d) During the recapture period, all or a portion of
2 previously taken credit as determined in subsection (a)(1) shall
3 be subject to recapture if the eligible property is transferred
4 out of the State.

5 (e) Exceptions to the recapture rule shall be as follows:

6 (1) A transfer by reason of death is not considered to be
7 a disposition of eligible property subject to the
8 recapture rule. This exception to the recapture rule
9 applies to transfers by reason of the death of a sole
10 proprietor, partner, S corporation shareholder, or
11 beneficiary of an estate or trust.

12 (2) A disposition of eligible property in a transaction to
13 which section 381(a) (with respect to carryovers in
14 certain corporate acquisitions) of the Internal
15 Revenue Code applies is not considered to be a
16 disposition of eligible property, subject to the
17 recapture rule; provided that, if the acquiring
18 corporation disposes of the eligible property before
19 the close of the recapture period, there shall be an
20 early disposition and the recapture rule shall be
21 triggered.



- 1 (3) Recapture is not required as a result of a mere change
2 in the form of conducting a trade or business if:
- 3 (A) The property is retained as eligible property in
4 the same trade or business;
- 5 (B) The transferor, or in a case where the transferor
6 is a partnership, estate or trust, or
7 S corporation, the partner, beneficiary, or
8 shareholder, of eligible property retains a
9 substantial interest in the trade or business;
- 10 (C) Substantially all the property, whether or not
11 eligible property, necessary to the trade or
12 business is transferred in the change in form;
13 and
- 14 (D) The basis of eligible property in the hands of
15 the transferee is determined in whole or in part
16 by reference to the basis of eligible property in
17 the hands of the transferor.
- 18 (4) Paragraph (3) shall not apply to the transfer of
19 eligible property if section 381 (with respect to
20 carryovers in certain corporate acquisitions) of the
21 Internal Revenue Code applies to the transfer.



1 (5) Neither an election to be treated as an S corporation,
2 nor a termination or loss of S corporation status
3 automatically triggers recapture. However, recapture
4 may result if one or more of the recapture events
5 discussed in paragraph (6) occurs. In determining
6 whether a reduction in a shareholder's interest will
7 result in recapture, the sixty-six and two-thirds per
8 cent and thirty-three and one-third per cent rules
9 apply even if the corporation is no longer an S
10 corporation.

11 (6) Property ceases to be eligible property with respect
12 to a transferor, or in a case where the transferor is
13 a partnership, estate or trust, or S corporation, the
14 partner, beneficiary or shareholder, and the
15 transferor shall make a recapture determination if
16 during the recapture period:

17 (A) The transferee disposes of eligible property;

18 (B) Eligible property otherwise ceases to be eligible
19 property in the hands of the transferee; or

20 (C) The transferor, or in a case where the transferor
21 is a partnership, estate or trust, or
22 S corporation, the partner, beneficiary, or



1 shareholder, does not retain a substantial
2 interest in the trade or business directly or
3 indirectly through ownership in other entities;
4 provided that the other entities' bases in the
5 interests are determined in whole or in part by
6 reference to the bases of the interest in the
7 hands of the transferor.

8 (f) A transfer between spouses incident to divorce is not
9 considered to be a disposition, subject to the recapture rule.
10 Subsequent to a transfer between spouses or incident to divorce,
11 a disposition by the transferee during the recapture period may
12 result in recapture to the same extent as if the disposition had
13 been made by the transferor at that later date.

14 (g) The recapture rule shall not apply to eligible
15 property which is disposed of or otherwise ceases to be eligible
16 property with respect to the taxpayer as a result of its
17 destruction or damage by fire, storm, shipwreck, or other
18 casualty, or theft.

19 (h) In the case of a partnership, a downward basis
20 adjustment pursuant to section 754 (with respect to manner of
21 electing optional adjustment to basis of partnership property)
22 of the Internal Revenue Code is not subject to recapture. Use



1 of the property is not considered to be terminated for purposes
2 of the credit.

3 SECTION 3. Section 235-110.7, Hawaii Revised Statutes is
4 repealed:

5 ~~["§235-110.7 Capital goods excise tax credit. (a) There~~
6 ~~shall be allowed to each taxpayer subject to the tax imposed by~~
7 ~~this chapter a capital goods excise tax credit which shall be~~
8 ~~deductible from the taxpayer's net income tax liability, if any,~~
9 ~~imposed by this chapter for the taxable year in which the credit~~
10 ~~is properly claimed.~~

11 ~~The amount of the tax credit shall be determined by the~~
12 ~~application of the following rates against the cost of the~~
13 ~~eligible depreciable tangible personal property used by the~~
14 ~~taxpayer in a trade or business and placed in service within~~
15 ~~Hawaii after December 31, 1987. For calendar years beginning~~
16 ~~after: December 31, 1987, the applicable rate shall be three~~
17 ~~per cent; December 31, 1988, and thereafter, the applicable rate~~
18 ~~shall be four per cent. For taxpayers with fiscal taxable~~
19 ~~years, the applicable rate shall be the rate for the calendar~~
20 ~~year in which the eligible depreciable tangible personal~~
21 ~~property used in the trade or business is placed in service~~
22 ~~within Hawaii.~~



1 ~~In the case of a partnership, S corporation, estate, or~~
2 ~~trust, the tax credit allowable is for eligible depreciable~~
3 ~~tangible personal property which is placed in service by the~~
4 ~~entity. The cost upon which the tax credit is computed shall be~~
5 ~~determined at the entity level. Distribution and share of~~
6 ~~credit shall be determined by rules.~~

7 ~~In the case of eligible depreciable tangible personal~~
8 ~~property for which a credit for sales or use taxes paid to~~
9 ~~another state is allowable under section 238 3(i), the amount of~~
10 ~~the tax credit allowed under this section shall not exceed the~~
11 ~~amount of use tax actually paid under chapter 238 relating to~~
12 ~~such tangible personal property.~~

13 ~~If a deduction is taken under section 179 (with respect to~~
14 ~~election to expense certain depreciable business assets) of the~~
15 ~~Internal Revenue Code of 1954, as amended, no tax credit shall~~
16 ~~be allowed for that portion of the cost of property for which~~
17 ~~the deduction was taken.~~

18 ~~(b) If the capital goods excise tax credit allowed under~~
19 ~~subsection (a) exceeds the taxpayer's net income tax liability,~~
20 ~~the excess of credit over liability shall be refunded to the~~
21 ~~taxpayer, provided that no refunds or payment on account of the~~



1 ~~tax credit allowed by this section shall be made for amounts~~
2 ~~less than \$1.~~

3 ~~All claims for tax credits under this section, including~~
4 ~~any amended claims, must be filed on or before the end of the~~
5 ~~twelfth month following the close of the taxable year for which~~
6 ~~the credits may be claimed. Failure to comply with the~~
7 ~~foregoing provision shall constitute a waiver of the right to~~
8 ~~claim the credit.~~

9 ~~(c) Application for the capital goods excise tax credit~~
10 ~~shall be upon forms provided by the department of taxation.~~

11 ~~(d) Sections 47 (with respect to dispositions of section~~
12 ~~38 property and the recapture percentages) of the Internal~~
13 ~~Revenue Code of 1954, as amended, as of December 31, 1984, and~~
14 ~~280F as operative for this chapter (with respect to limitation~~
15 ~~on investment tax credit and depreciation for luxury~~
16 ~~automobiles, limitation where certain property used for personal~~
17 ~~purposes) of the Internal Revenue Code of 1954, as amended,~~
18 ~~shall be operative for purposes of this section.~~

19 ~~(e) As used in this section, the definition of section 38~~
20 ~~property (with respect to investment in depreciable tangible~~
21 ~~personal property) as defined by section 48(a)(1)(A), (a)(1)(B),~~
22 ~~(a)(3), (a)(4), (a)(7), (a)(8), (a)(10)(A), (b), (c), (f), (l),~~



1 ~~(m), and (s) of the Internal Revenue Code of 1954, as amended as~~
2 ~~of December 31, 1984, is operative for the purposes of this~~
3 ~~section only.~~

4 ~~As used in this section:~~

5 ~~"Cost" means (1) the actual invoice price of the tangible~~
6 ~~personal property, or (2) the basis from which depreciation is~~
7 ~~taken under section 167 (with respect to depreciation) or from~~
8 ~~which a deduction may be taken under section 168 (with respect~~
9 ~~to accelerated cost recovery system) of the Internal Revenue~~
10 ~~Code of 1954, as amended, whichever is less.~~

11 ~~"Eligible depreciable tangible personal property" is~~
12 ~~section 38 property as defined by the operative provisions of~~
13 ~~section 48 and having a depreciable life under section 167 or~~
14 ~~for which a deduction may be taken under section 168 of the~~
15 ~~federal Internal Revenue Code of 1954, as amended.~~

16 ~~"Placed in service" means the earliest of the following~~
17 ~~taxable years:~~

18 ~~(1) The taxable year in which, under the:~~

19 ~~(A) Taxpayer's depreciation practice, the period for~~
20 ~~depreciation; or~~



1 ~~(B) Accelerated cost recovery system, a claim for~~
2 ~~recovery allowances, with respect to such~~
3 ~~property begins, or~~

4 ~~(2) The taxable year in which the property is placed in a~~
5 ~~condition or state of readiness and availability for a~~
6 ~~specifically assigned function.~~

7 ~~"Purchase" means an acquisition of property.~~

8 ~~"Tangible personal property" means tangible personal~~
9 ~~property which is placed in service within Hawaii after~~
10 ~~December 31, 1987, and the purchase or importation of which~~
11 ~~resulted in a transaction which was subject to the imposition~~
12 ~~and payment of tax at the rate of four per cent under chapter~~
13 ~~237 or 238. "Tangible personal property" does not include~~
14 ~~tangible personal property which is an integral part of a~~
15 ~~building or structure or tangible personal property used in a~~
16 ~~foreign trade zone, as defined under chapter 212."]~~

17 SECTION 4. In codifying the new sections added by
18 section 2 of this Act, the revisor of statutes shall substitute
19 appropriate section numbers for the letters used in designating
20 the new sections in this Act.

21 SECTION 5. Statutory material to be repealed is bracketed
22 and stricken.



1 SECTION 6. This Act shall take affect upon approval and
2 shall apply to taxable years beginning after December 31, 2008.



Report Title:

Capital Goods Excise Tax Credit; Repeal and Reenactment

Description:

Repeals and reenacts the capital goods excise tax credit in order to reflect the definitions and other references to the Internal Revenue Code. (SD2)

