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## 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 residents in certain  
2 rural areas in the State do not have access to public utility  
3 water services. The legislature also finds that in some of  
4 these unserved areas, private nonprofit companies, such as Napu'u  
5 Water, Inc., have been established for the sole purpose of  
6 supplying potable water to the community. Although these  
7 companies are federally tax-exempt under section 501(c)(12) of  
8 the Internal Revenue Code, they are still subject to the state  
9 income and general excise taxes. The legislature further finds  
10 that, in the interests of fairness and equity, nonprofit  
11 companies that are operated exclusively to supply potable water  
12 to communities that lack any access to public utility water  
13 services should receive the same tax treatment as water  
14 companies owned by a county or municipality.

15           The purpose of this Act is to exempt federally tax-exempt  
16 501(c)(12) privately-owned nonprofit public water systems that  
17 supply potable water from the state income and general excise  
18 taxes.



1 SECTION 2. Section 235-2.3, Hawaii Revised Statutes, is  
2 amended by amending subsection (b) to read as follows:

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

7 (1) Subchapter A (sections 1 to 59A) (with respect to  
8 determination of tax liability), except section  
9 1(h)(2) (relating to net capital gain reduced by the  
10 amount taken into account as investment income),  
11 except sections 2(a), 2(b), and 2(c) (with respect to  
12 the definition of "surviving spouse" and "head of  
13 household"), except section 41 (with respect to the  
14 credit for increasing research activities), except  
15 section 42 (with respect to low-income housing  
16 credit), except sections 47 and 48, as amended, as of  
17 December 31, 1984 (with respect to certain depreciable  
18 tangible personal property), and except section  
19 48(d)(3), as amended, as of February 17, 2009 (with  
20 respect to the treatment of United States Department  
21 of Treasury grants made under section 1603 of the  
22 American Recovery and Reinvestment Tax Act of 2009).



- 1 For treatment, see sections 235-110.91, 235-110.7, and  
2 235-110.8;
- 3 (2) Section 78 (with respect to dividends received from  
4 certain foreign corporations by domestic corporations  
5 choosing foreign tax credit);
- 6 (3) Section 86 (with respect to social security and tier 1  
7 railroad retirement benefits);
- 8 (4) Section 103 (with respect to interest on state and  
9 local bonds). For treatment, see section 235-7(b);
- 10 (5) Section 114 (with respect to extraterritorial income).  
11 For treatment, any transaction as specified in the  
12 transitional rule for 2005 and 2006 as specified in  
13 the American Jobs Creation Act of 2004 section 101(d)  
14 and any transaction that has occurred pursuant to a  
15 binding contract as specified in the American Jobs  
16 Creation Act of 2004 section 101(f) are inoperative;
- 17 (6) Section 120 (with respect to amounts received under  
18 qualified group legal services plans). For treatment,  
19 see section 235-7(a)(9) to (11);
- 20 (7) Section 122 (with respect to certain reduced uniformed  
21 services retirement pay). For treatment, see section  
22 235-7(a)(3);



- 1           (8) Section 135 (with respect to income from United States
- 2           savings bonds used to pay higher education tuition and
- 3           fees). For treatment, see section 235-7(a)(1);
- 4           (9) Section 139C (with respect to COBRA premium
- 5           assistance);
- 6           (10) Subchapter B (sections 141 to 150) (with respect to
- 7           tax exemption requirements for state and local bonds);
- 8           (11) Section 151 (with respect to allowance of deductions
- 9           for personal exemptions). For treatment, see section
- 10          235-54;
- 11          (12) Section 179B (with respect to expensing of capital
- 12          costs incurred in complying with Environmental
- 13          Protection Agency sulphur regulations);
- 14          (13) Section 181 (with respect to special rules for certain
- 15          film and television productions);
- 16          (14) Section 196 (with respect to deduction for certain
- 17          unused investment credits);
- 18          (15) Section 199 (with respect to the U.S. production
- 19          activities deduction);
- 20          (16) Section 222 (with respect to qualified tuition and
- 21          related expenses);



- 1       (17) Sections 241 to 247 (with respect to special  
2           deductions for corporations). For treatment, see  
3           section 235-7(c);
- 4       (18) Section 280C (with respect to certain expenses for  
5           which credits are allowable). For treatment, see  
6           section 235-110.91;
- 7       (19) Section 291 (with respect to special rules relating to  
8           corporate preference items);
- 9       (20) Section 367 (with respect to foreign corporations);
- 10      (21) Section 501(c)(12), (15), (16) (with respect to exempt  
11           organizations); except that section 501(c)(12) shall  
12           be operative for companies that provide potable water;
- 13      (22) Section 515 (with respect to taxes of foreign  
14           countries and possessions of the United States);
- 15      (23) Subchapter G (sections 531 to 565) (with respect to  
16           corporations used to avoid income tax on  
17           shareholders);
- 18      (24) Subchapter H (sections 581 to 597) (with respect to  
19           banking institutions), except section 584 (with  
20           respect to common trust funds). For treatment, see  
21           chapter 241;



- 1 (25) Section 642(a) and (b) (with respect to special rules  
2 for credits and deductions applicable to trusts). For  
3 treatment, see sections 235-54(b) and 235-55;
- 4 (26) Section 646 (with respect to tax treatment of electing  
5 Alaska Native settlement trusts);
- 6 (27) Section 668 (with respect to interest charge on  
7 accumulation distributions from foreign trusts);
- 8 (28) Subchapter L (sections 801 to 848) (with respect to  
9 insurance companies). For treatment, see sections  
10 431:7-202 and 431:7-204;
- 11 (29) Section 853 (with respect to foreign tax credit  
12 allowed to shareholders). For treatment, see section  
13 235-55;
- 14 (30) Section 853A (with respect to credits from tax credit  
15 bonds allowed to shareholders);
- 16 (31) Subchapter N (sections 861 to 999) (with respect to  
17 tax based on income from sources within or without the  
18 United States), except sections 985 to 989 (with  
19 respect to foreign currency transactions). For  
20 treatment, see sections 235-4, 235-5, and 235-7(b),  
21 and 235-55;



- 1       (32) Section 1042(g) (with respect to sales of stock in  
2           agricultural refiners and processors to eligible farm  
3           cooperatives);
- 4       (33) Section 1055 (with respect to redeemable ground  
5           rents);
- 6       (34) Section 1057 (with respect to election to treat  
7           transfer to foreign trust, etc., as taxable exchange);
- 8       (35) Sections 1291 to 1298 (with respect to treatment of  
9           passive foreign investment companies);
- 10      (36) Subchapter Q (sections 1311 to 1351) (with respect to  
11          readjustment of tax between years and special  
12          limitations);
- 13      (37) Subchapter R (sections 1352 to 1359) (with respect to  
14          election to determine corporate tax on certain  
15          international shipping activities using per ton rate);
- 16      (38) Subchapter U (sections 1391 to 1397F) (with respect to  
17          designation and treatment of empowerment zones,  
18          enterprise communities, and rural development  
19          investment areas). For treatment, see chapter 209E;
- 20      (39) Subchapter W (sections 1400 to 1400C) (with respect to  
21          District of Columbia enterprise zone);



- 1       (40) Section 14000 (with respect to education tax
- 2               benefits);
- 3       (41) Section 1400P (with respect to housing tax benefits);
- 4       (42) Section 1400R (with respect to employment relief);
- 5       (43) Section 1400T (with respect to special rules for
- 6               mortgage revenue bonds);
- 7       (44) Section 1400U-1 (with respect to allocation of
- 8               recovery zone bonds);
- 9       (45) Section 1400U-2 (with respect to recovery zone
- 10              economic development bonds); and
- 11       (46) Section 1400U-3 (with respect to recovery zone
- 12              facility bonds)."

13       SECTION 3. Section 237-23, Hawaii Revised Statutes, is  
14 amended by amending subsections (a), (b), and (c) to read as  
15 follows:

16       "(a) This chapter shall not apply to the following  
17 persons:

- 18       (1) Public service companies as that term is defined in
- 19              section 239-2, with respect to the gross income,
- 20              either actual gross income or gross income estimated
- 21              and adjusted, that is included in the measure of the
- 22              tax imposed by chapter 239;





- 1           (2) Public utilities owned and operated by the State or  
2           any county, or other political subdivision thereof;
- 3           (3) Fraternal benefit societies, orders, or associations,  
4           operating under the lodge system, or for the exclusive  
5           benefit of the members of the fraternity itself,  
6           operating under the lodge system, and providing for  
7           the payment of death, sick, accident, prepaid legal  
8           services, or other benefits to the members of the  
9           societies, orders, or associations, and to their  
10          dependents;
- 11          (4) Corporations, associations, trusts, or societies  
12          organized and operated exclusively for religious,  
13          charitable, scientific, or educational purposes, as  
14          well as that of operating senior citizens housing  
15          facilities qualifying for a loan under the laws of the  
16          United States as authorized by section 202 of the  
17          Housing Act of 1959, as amended, as well as that of  
18          operating a prepaid legal services plan, as well as  
19          that of operating or managing a homeless facility, or  
20          any other program for the homeless authorized under  
21          part XVII of chapter 346;



1 (5) Business leagues, chambers of commerce, boards of  
 2 trade, civic leagues, agricultural and horticultural  
 3 organizations, and organizations operated exclusively  
 4 for the benefit of the community and for the promotion  
 5 of social welfare that shall include the operation of  
 6 a prepaid legal service plan, and from which no profit  
 7 inures to the benefit of any private stockholder or  
 8 individual;

9 (6) Hospitals, infirmaries, and sanitararia;

10 (7) Companies that provide potable water and are tax  
 11 exempt under section 501(c)(12) of the Internal  
 12 Revenue Code of 1986, as amended;

13 [~~7~~] (8) Cooperative associations incorporated under  
 14 chapter 421 or Code section 521 cooperatives which  
 15 fully meet the requirements of section 421-23, except  
 16 Code section 521 cooperatives need not be organized in  
 17 Hawaii; provided that:

18 (A) The exemption shall apply only to the gross  
 19 income derived from activities that are pursuant  
 20 to purposes and powers authorized by chapter 421,  
 21 except those provisions pertaining to or



1 requiring corporate organization in Hawaii do not  
2 apply to Code section 521 cooperatives;

3 (B) The exemption shall not relieve any person who  
4 receives any proceeds of sale from the  
5 association of the duty of returning and paying  
6 the tax on the total gross proceeds of the sales  
7 on account of which the payment was made, in the  
8 same amount and at the same rate as would apply  
9 thereto had the sales been made directly by the  
10 person, and all those persons shall be so  
11 taxable; and

12 (C) As used in this paragraph, "section 521  
13 cooperatives" mean associations that qualify as a  
14 cooperative under section 521 (with respect to  
15 exemption of farmers' cooperatives from tax) of  
16 the Internal Revenue Code of 1986, as amended;

17 ~~[(8)]~~ (9) Persons affected with Hansen's disease and  
18 kokuas, with respect to business within the county of  
19 Kalawao;

20 ~~[(9)]~~ (10) Corporations, companies, associations, or trusts  
21 organized for the establishment and conduct of  
22 cemeteries no part of the net earnings of which inures



1 to the financial benefit of any private stockholder or  
2 individual; provided that the exemption shall apply  
3 only to the activities of those persons in the conduct  
4 of cemeteries and shall not apply to any activity the  
5 primary purpose of which is to produce income, even  
6 though the income is to be used for or in the  
7 furtherance of the exempt activities of those persons;  
8 and

9 [~~10~~] (11) Nonprofit shippers associations operating under  
10 part 296 of the Civil Aeronautics Board Economic  
11 Regulations.

12 (b) The exemptions enumerated in subsection (a)(3) to  
13 [~~6~~] (7) shall apply only:

14 (1) To those persons who shall have registered with the  
15 department of taxation by filing a written application  
16 for registration in such form as the department shall  
17 prescribe, shall have paid the registration fee of  
18 \$20, and shall have had the exemption allowed by the  
19 department or by a court or tribunal of competent  
20 jurisdiction upon appeal from any assessment resulting  
21 from disallowance of the exemption by the department;



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- 1           (2) To activities from which no profit inures to the  
2           benefit of any private stockholder or individual,  
3           except for death or other benefits to the members of  
4           fraternal societies; and
- 5           (3) To the fraternal, religious, charitable, scientific,  
6           educational, communal, or social welfare activities of  
7           such persons, or to the activities of [~~such~~]  
8           hospitals, infirmaries, [~~and~~] sanitarium [~~as such~~], and  
9           potable water companies, and not to any activity the  
10          primary purpose of which is to produce income even  
11          though the income is to be used for or in furtherance  
12          of the exempt activities of such persons.
- 13          (c) To obtain allowance of an exemption:
- 14          (1) A person under subsection (a) (3) to [~~(6)~~] (7), who  
15          has received or applied for recognition of tax exempt  
16          status under section 501(c) (3), (4), (6), [~~or~~] (8), or  
17          (12) of the Internal Revenue Code of 1986, as amended,  
18          or who is a subordinate person of a person who has  
19          received a group exemption letter under section  
20          501(c) (3), (4), (6), [~~or~~] (8), or (12) of the Internal  
21          Revenue Code of 1986, as amended, shall register with  
22          the department by filing a statement attaching a copy



1 of the exemption or application for recognition of  
 2 exempt status and any particular facts that the  
 3 department may require; and

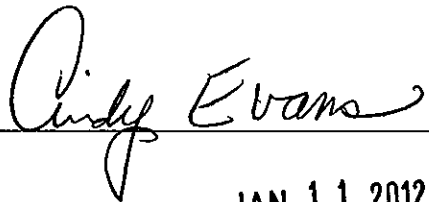
4 (2) All other persons under subsection (a)(3) to ~~[(6)]~~ (7)  
 5 shall file an application for exemption in the form of  
 6 an affidavit or affidavits setting forth in general  
 7 all facts affecting the right to the exemption and  
 8 ~~[such]~~ any particular facts ~~[as]~~ that the department  
 9 may require, to which shall be attached ~~[such]~~ any  
 10 records, papers, and other information as the  
 11 department may prescribe."

12 SECTION 4. Statutory material to be repealed is bracketed  
 13 and stricken. New statutory material is underscored.

14 SECTION 5. This Act shall take effect upon approval;  
 15 provided that sections 2 and 3 shall apply to taxable years  
 16 beginning after December 31, 2011.

17

INTRODUCED BY:

  
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JAN 11 2012



**Report Title:**

Taxation; Potable Water

**Description:**

Exempts federally tax-exempt 501(c)(12) privately-owned nonprofit public water systems that supply potable water from the state income and general excise taxes.

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