

ACT 239

S.B. NO. 320

A Bill for an Act Relating to Taxation.

Be It Enacted by the Legislature of the State of Hawaii:

PART I

SECTION 1. Chapter 235, Hawaii Revised Statutes, is amended as follows:

1. By adding a new section to be appropriately designated and to read as follows:

“§235- Food tax credit. (a) Each resident individual taxpayer, who files an individual income tax return for a taxable year, and who is not

claimed or is not otherwise eligible to be claimed as a dependent by another taxpayer for federal or Hawaii state individual income tax purposes, may claim a food tax credit of \$45 against the resident taxpayer's individual income tax liability for the taxable year for which the individual income tax return is being filed; provided that a resident individual who has no income or no income taxable under this chapter and who is not claimed or is not otherwise eligible to be claimed as a dependent by a taxpayer for federal or Hawaii state individual income tax purposes may claim this credit. The food tax credit of \$45 shall be multiplied by the number of qualified exemptions to which the taxpayer is entitled.

(b) For the purposes of this section, a qualified exemption is defined to include those exemptions permitted under this chapter; provided that a person for whom exemption is claimed has physically resided in the State for more than nine months during the taxable year; and provided further that multiple exemptions shall not be granted because of age, deficiencies in vision or hearing, or other disability. For purposes of claiming the credit only, a minor child receiving support from the department of social services and housing of the State, social security survivor's benefits, and the like, may be considered a dependent and a qualified exemption of the parent or guardian.

(c) The tax credit under this section shall not be available to (1) any person who has been convicted of a felony and who has been committed to prison and has been physically confined for the full taxable year; (2) any person who would otherwise be eligible to be claimed as a dependent but who has been committed to a youth correctional facility and has resided at the facility for the full taxable year; or (3) any misdemeanor who has been committed to jail and has been physically confined for the full taxable year.

(d) The tax credits claimed by a resident taxpayer pursuant to this section shall be deductible from the resident taxpayer's individual income tax liability, if any, for the tax year in which they are properly claimed. If the tax credits claimed by a resident taxpayer exceed the amount of income tax payment due from the resident taxpayer, the excess of credits over payments due shall be refunded to the resident taxpayer; provided that tax credits properly claimed by a resident individual who has no income tax liability shall be paid to the resident individual; and provided further that no refunds or payment on account of the tax credits allowed by this section shall be made for amounts less than \$1.

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

(f) This section shall not be effective after December 31, 1990."

2. By adding a new section to be appropriately designated and to read as follows:

"§235- Capital goods excise tax credit. (a) There shall be allowed to each taxpayer subject to the tax imposed by this chapter a capital goods excise tax credit which shall be deductible from the taxpayer's net income tax liability, if any, imposed by this chapter for the taxable year in which the credit is property¹ claimed.

The amount of the tax credit shall be determined by the application of the following rates against the cost of the eligible depreciable tangible personal property used by the taxpayer in a trade or business and purchased

ACT 239

and placed in service within Hawaii after December 31, 1987. For calendar years beginning after:

- December 31, 1987, the applicable rate shall be 3 per cent;
- December 31, 1988, and thereafter, the applicable rate shall be 4 per cent.

For taxpayers with fiscal taxable years, the applicable rate shall be the rate for the calendar year in which the eligible tangible personal property used in the trade or business is purchased and placed in service within Hawaii.

In the case of partners, S corporation shareholders, or beneficiaries of estates and trusts who are taxable on the distributive share of net income received, the credit under this section for the taxable year shall be allowable only to the extent of the ratio of the distributive share of income received from the partnership, S corporation, estate or trust to the entire gross income subject to the tax imposed by this chapter.

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

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

(b) If the capital goods excise tax credit allowed under subsection (a) exceeds the taxpayer's net income tax liability, the excess of credit over liability shall be refunded to the taxpayer; provided that no refunds or payment on account of the tax credit allowed by this section shall be made for amounts less than \$1.

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

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

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

(e) As used in this section, the definition of section 38 property (with respect to investment in depreciable tangible personal property) as defined by section 48(a)(1)(A), (a)(1)(B), (a)(3), (a)(4), (a)(7), (a)(8), (a)(10)(A), (b), (c), (f), (l), (m), and (s) of the Internal Revenue Code of 1954, as amended as of December 31, 1984, is operative for the purposes of this section only.

As used in this section:

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

"Eligible depreciable tangible personal property" is section 38 property as defined by the operative provisions of section 48 and having a

depreciable life under section 167 or for which a deduction may be taken under section 168 of the federal Internal Revenue Code of 1954, as amended.

“Purchased and placed in service” means the date the property was acquired, or available or ready for use, whichever is earlier. Property purchased and placed in service does not include property which was owned or used at any time during 1987 by the taxpayer or related person, or property acquired in a transaction in which the user of such property does not change.

“Tangible personal property” means tangible personal property which is purchased and placed in service within Hawaii after December 31, 1987, and the purchase or importation of which resulted in a transaction which was subject to the imposition and payment of tax at the rate of four per cent under chapter 237 or 238. “Tangible personal property” does not include tangible personal property which is an integral part of a building or structure or tangible personal property used in a foreign trade zone, as defined under chapter 212.”

3. By adding a new section to be appropriately designated and to read as follows:

“§235- Certain unearned income of minor children taxed as if parent’s income. (a) In the case of any child to whom this section applies, the tax imposed by this chapter shall be equal to the greater of:

- (1) The tax imposed by section 235-51 without regard to this section, or
- (2) The sum of:
 - (A) The tax which would be imposed by section 235-51 if the taxable income of such child for the taxable year were reduced by the net unearned income of such child, plus
 - (B) Such child’s share of allocable parental tax.

(b) This section shall apply to any child for any taxable year if:

- (1) Such child has not attained age fourteen before the close of the taxable year, and
- (2) Either parent of such child is alive at the close of the taxable year.

(c) For the purpose of this section:

- (1) The term “allocable parental tax” means the excess of:
 - (A) The tax which would be imposed by section 235-51 on the parent’s taxable income if such income included the net unearned income of all children of the parent to whom this section applies, over,
 - (B) The tax imposed by section 235-51 on the parent without regard to this section.

For purposes of subparagraph (A), net unearned income of all children of the parent shall not be taken into account in computing any deduction or credit of the parent.

- (2) A child’s share of any allocable parental tax of a parent shall be equal to an amount which bears the same ratio to the total allocable parental tax as the child’s net unearned income bears to the aggregate net unearned income of all children of such parent to whom this section applies.

(d) For purposes of this section:

- (1) The term “net unearned income” means the excess of:
 - (A) The portion of the gross income for the taxable year which is not earned income as defined in the Internal Revenue Code, over,
 - (B) The sum of:

- (i) The amount in effect for the taxable year under section 63(c)(5)(A) (relating to the limitation on standard deduction in the case of certain dependents) of the Internal Revenue Code as operative under section 235-2.4(a), plus
 - (ii) The greater of the amount described in clause (i) or, if the child itemizes the child's deductions for the taxable year, the amount of the deductions allowed by this chapter for the taxable year which are directly connected with the production of the portion of gross income referred to in subparagraph (A).
- (2) The amount of the net unearned income for any taxable year shall not exceed the individual's taxable income for such taxable year.
- (e) For purposes of this section, the parent whose taxable income shall be taken into account shall be:
- (1) In the case of parents who are not married (within the meaning of section 235-93), the custodial parent of the child, and
 - (2) In the case of married individuals filing separately, the individual with the greater taxable income.
- (f) The parent of any child to whom this section applies for any taxable year shall provide the social security number of such parent to such child and such child shall include such parent's social security number on the child's return of tax imposed by this section for such taxable year."

4. Section 235-1 is amended by adding a new definition to be appropriately inserted and to read as follows:

"Internal Revenue Code of 1954, as amended" includes the Internal Revenue Code of 1986 and the Internal Revenue Code of 1986, as amended."

5. Section 235-2.3 is amended by amending subsections (a) and (b) to read as follows:

"(a) For all taxable years beginning after December 31, [1985,] 1986, as used in this chapter "Internal Revenue Code" means subtitle A, chapter 1 of the federal Internal Revenue Code of 1954 as amended as of December 31, [1985,] 1986, as it applies to the determination of gross income, adjusted gross income, mtordinary income and loss, and taxable income except those provisions of the Internal Revenue Code and federal Public Law which pursuant to this chapter, this section, and sections 235-2.4 and 235-2.5 do not apply or are otherwise limited in application[.]; provided that section 1202 (with respect to deduction for capital gains) of the Internal Revenue Code of 1954 as amended as of December 31, 1986, shall be operative for the purposes of this chapter until March 31, 1987, and shall apply to any capital gains properly taken before April 1, 1987, except that the deduction provided in section 1202(a) shall be 55 per cent of the net capital gain.

Sections 235-2, 235-2.1, and 235-2.2 shall continue to be used to determine (1) the basis of property, if a taxpayer first determined the basis of property in a taxable year to which such sections apply, and if such determination was made before January 1, 1978, and (2) gross income, adjusted gross income, ordinary income and loss, and taxable income for a taxable year to which such sections apply where such taxable year begins before January 1, 1978.

(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 [58] 59) (with respect to determination of tax liability)[.], except sections 47 and 48, as amended, as of December 31, 1984 (with respect to certain depreciable tangible personal property). For treatment, see section 235-
- (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 103 (with respect to interest on [certain governmental obligations].) state and local bonds. For treatment, see section 235-7(b).
- [(5) Section 103A (with respect to mortgage subsidy bonds).
- (6)] (5) Section 120 (with respect to amounts received under qualified group legal services plans). For treatment, see sections 235-2.4[,] and 235-7(a)(10) to (12)[, and 235-9(a)(2) and (5)].
- [(7)] (6) Section 122 (with respect to certain reduced uniformed services retirement pay). For treatment, see section 235-7(a)(3).
- (7) Subchapter B (sections 141 to 150) (with respect to tax exemption requirements for state and local bonds).
- (8) Section 151 (with respect to allowance of deductions for personal exemptions). For treatment, see section 235-54.
- (9) Section 169 (with respect to amortization of pollution control facilities). For treatment, see section 235-11.
- (10) Section 196 (with respect to deduction for certain unused investment credits).
- [(11) Section 221 (with respect to deduction for two-earner married couples).
- (12)] (11) Subchapter B, part VIII (sections 241 to 250) (with respect to special deductions for corporations), except sections 248 (with respect to organizational expenditures) and 249 (with respect to limitation on deduction of bond premium on repurchase). For treatment, see section 235-7(c).
- [(13)] (12) Section 269A (with respect to personal service corporations formed or availed of to avoid or evade income tax).
- [(14)] (13) Section 280C (with respect to certain expenses for which credits are allowable).
- [(15)] (14) Section 280D (with respect to portion of chapter 45 taxes for which credit or refund is allowable under section 6429).
- [(16)] (15) Section 291 (with respect to special rules relating to corporate preference items).
- [(17)] (16) Section 367 (with respect to foreign corporations).
- [(18)] (17) [Subchapter F (sections 501 to 528)] Section 501(c)(12), (15), (16) (with respect to exempt organizations)], except as provided in section 235-2.4. For treatment, see section 235-9].
- (18) Section 515 (with respect to taxes of foreign countries and possessions of the United States).
- (19) Section 521 (with respect to exemption of farmers cooperatives from tax). For treatment, see section 421-23.
- [(19)] (20) Subchapter G (sections 531 to 565) (with respect to corporations used to avoid income tax on shareholders).

ACT 239

- [(20)] (21) Subchapter H (sections 581 to [597]) 596 (with respect to banking institutions). For treatment, see chapter 241.
- [(21)] (22) Section 642(a), (b), and (d) (with respect to special rules for credits and deductions).
- [(22)] (23) Section 668 (with respect to interest charge on accumulation distributions from foreign trusts).
- [(23)] (24) Subchapter L (sections 801 to [845]) 846 (with respect to insurance companies). For treatment, see sections 431-318 and 431-320.
- [(24)] (25) Section 853 (with respect to foreign tax credit allowed to shareholders). For treatment, see section 235-55.
- [(25)] (26) Subchapter N (sections 861 to 999) (with respect to tax based on income from sources within or without the United States), except part IV (sections 991 to 997) (with respect to domestic international sales corporations). For treatment, see sections 235-4, 235-5, and 235-7(b).
- [(26)] (27) Section 1055 (with respect to redeemable ground rents).
- [(27)] (28) Section 1057 (with respect to election to treat transfer to foreign trust, etc., as taxable exchange).
- [(28)] (29) Section 1201 (with respect to alternative tax). For treatment, see section 235-71(a).
- [(29)] (30) Subchapter Q (sections [1301] 1311 to 1351) (with respect to readjustment of tax between years and special limitations).
- [(30)] (31) Subchapter T (sections 1381 to 1388) (with respect to cooperatives and their patrons). For treatment, see chapter 421."

6. Section 235-2.4 is amended to read as follows:

"§235-2.4 Operation of certain Internal Revenue Code provisions. (a) Section 63 (with respect to taxable income defined) of the Internal Revenue Code shall be operative for the purposes of this chapter, except that the [zero-bracket amount in section 63(d)] standard deduction amount in section 63(c) of the Internal Revenue Code shall instead mean:

- [(1)] \$1,000 in the case of:
 - (A) A joint return as provided by section 235-93, or
 - (B) A surviving spouse (as defined in section 2(a) of the Internal Revenue Code),
- (2) \$800 in the case of an individual who is not married and who is not a surviving spouse (as so defined),
- (3) \$500 in the case of a married individual filing a separate return, or
- (4) Zero in any other case.]
- (1) \$1,700 in the case of:
 - (A) A joint return as provided by section 235-93, or
 - (B) A surviving spouse (as defined in section 2(a) of the Internal Revenue Code),
- (2) \$1,500 in the case of a head of household (as defined in section 2(b) of the Internal Revenue Code),
- (3) \$1,000 in the case of an individual who is not married and who is not a surviving spouse or head of household, or
- (4) \$850 in the case of a married individual filing a separate return.

Section 63(c)(4) shall not be operative in this State. Section 63(c)(5) shall be operative, except that the limitation on standard deduction in the case of certain dependents shall be the greater of \$500 or such individual's earned income. Section 63(f) shall not be operative in this State.

(b) Section 219 (with respect to retirement savings) of the Internal Revenue Code shall be operative for the purpose of this chapter. For the purpose of computing the limitation on the deduction for active participants in certain pension plans for state income tax purposes, adjusted gross income as used in section 219 as operative for this chapter means federal adjusted gross income.

[(b)] (c) In administering the provisions of sections 410 to [415] 417 (with respect to special rules relating to pensions, profit sharing, stock bonus plans, etc.), sections 418 to 418E (with respect to special rules for multiemployer plans), and sections 419 and 419A (with respect to treatment of welfare benefit funds) of the Internal Revenue Code, the department of taxation shall adopt rules under chapter 91 relating to the specific requirements under such sections and to such other administrative requirements under those sections as may be necessary for the efficient administration of sections 410 to 419A.

In administering sections 401 to 419A (with respect to deferred compensation) of the Internal Revenue Code, Public Law 93-406, section 1017(i), shall be operative for the purposes of this chapter.

In administering section 402 (with respect to the taxability of beneficiary of employees' trust) of the Internal Revenue Code, the tax imposed on lump sum distributions by section 402(e) of the Internal Revenue Code shall be operative for the purposes of this chapter and the tax imposed therein is hereby imposed by this chapter at the rate determined under this chapter.

(d) Section 468B (with respect to special rules for designated settlement funds) shall be operative for the purposes of this chapter and the tax imposed therein is hereby imposed by this chapter at a rate equal to the maximum rate in effect for the taxable year imposed on estates and trusts under section 235-51.

(e) Section 469 (with respect to passive activities and credits limited) shall be operative for the purposes of this chapter. For the purpose of computing the offset for rental real estate activities for state income tax purposes, adjusted gross income as used in section 469 as operative for this chapter means federal adjusted gross income.

[(c)] (f) Sections 512 to [515] 514 (with respect to taxation of business income of certain exempt organizations) of the Internal Revenue Code shall be operative for the purposes of this chapter as provided in this subsection.

The persons and organizations exempted by section 235-9 shall, if subject to tax under the Internal Revenue Code upon their "unrelated business taxable income", be taxed thereon under this chapter. For the purposes of this subsection the term "taxable income" as used in subsection [(d)(2)] (h)(2) of this section and section 235-71 shall be read as "unrelated business taxable income".

"Unrelated business taxable income" means the same as in the Internal Revenue Code, except that in the computation thereof sections 235-3 to 235-5, and 235-7 (except subsection (c)), shall apply, and in the determination of the net operating loss deduction under section 235-7(d) there shall not be taken into account any amount of income or deduction which is excluded in computing the unrelated business taxable income. Unrelated business taxable income shall not include any income from a prepaid legal service plan.

(g) Sections 527 (with respect to political organizations) and 528 (with respect to certain homeowners associations) shall be operative for the purposes of this chapter and the taxes imposed in each such section are hereby imposed by this chapter at the rates determined under section 235-71.

[(d)] (h) Section 641 (with respect to imposition of tax) of the Internal Revenue Code shall be operative for the purposes of this chapter subject to the following:

- (1) The deduction for exemptions shall be allowed as provided in section 235-54(b).
- (2) The deduction for contributions and gifts in determining taxable income shall be limited to the amount allowed in the case of an individual, unless the contributions and gifts are to be used exclusively in the State.
- (3) The tax imposed by section 1(e) of the Internal Revenue Code as applied by section 641 of the Internal Revenue Code is hereby imposed by this chapter at the rate and amount as determined under section 235-51[(e)] on estates and trusts.

[(e)] (i) Section 644 (with respect to special rule for gain on property transferred to trust at less than fair market value) of the Internal Revenue Code shall be operative for the purposes of this chapter and the tax imposed therein is hereby imposed by this chapter at the rate determined under this chapter; except that the determination of the interest rate established under section 6621 of the Internal Revenue Code referred to in section 644(a)(2) of the Internal Revenue Code shall instead be the interest rate established under section 231-39(b)(4).

[(f)] (i) Section 667 (with respect to treatment of amounts deemed distributed by trusts in preceding years) of the Internal Revenue Code shall be operative for the purposes of this chapter and the tax imposed therein is hereby imposed by this chapter at the rate determined under this chapter; except that the reference to tax-exempt interest to which section 103 of the Internal Revenue Code applies in section 667(a) of the Internal Revenue Code shall instead be a reference to tax-exempt interest to which section 235-7(b) applies.

[(g)] (k) Sections 991 to 997 (with respect to domestic international sales corporations) of the Internal Revenue Code shall be operative for the purposes of this chapter; provided that any corporation electing to be a domestic international sales corporation under this chapter shall be incorporated and have its principal place of business in this State.

[(h)] (l) Section 1034 (with respect to rollover of gain on sale of principal residence) of the Internal Revenue Code shall be operative for the purpose of this chapter; provided section 1034(a) (with respect to nonrecognition of gain) of the Internal Revenue Code shall apply only to:

- (1) A taxpayer who purchases a replacement residence which is located within the State, or
- (2) A taxpayer who is a resident of the State, taxable upon the taxpayer's entire income, computed without regard to source within the State.

[(i)] (m) Section 1212 (with respect to capital loss carrybacks and carryforwards) of the Internal Revenue Code shall be operative for the purposes of this chapter; except that for the purposes of this chapter the capital loss carryback provisions of section 1212 shall not be operative and the capital loss carryforward allowed by section 1212(a), shall be limited to five years.

[(j)] (n) Subchapter S (sections 1361 to 1379) (with respect to tax treatment of S corporations and their shareholders) of chapter 1 of the Internal Revenue Code shall be operative for the purposes of this chapter subject to the following:

- (1) The term S corporation as defined in section 1361 of the Internal Revenue Code means a corporation which does not have[

- (A) A nonresident as a shareholder; or
- (B) A] a resident who is an individual who has taken up residence in the State after attaining the age of sixty-five years and before July 1, 1976, and who is taxed under this chapter only on the basis of income received or derived from property owned, personal services performed, trade or business carried on, and any and every other source in the State;

unless the individual resident [in subparagraph (B)] shall have waived the benefit of section 3, Act 60, Session Laws of Hawaii 1976, as to income includible in the individual's gross income under this chapter and as to such gross income shall have consented to the taxation thereof in the same manner as if the individual had taken up residence in the State after June 30, 1976.

- (2) An election under section 1362 of the Internal Revenue Code shall not be effective for any taxable year of the corporation unless there is also in effect for such taxable year an election for federal income tax purposes under subchapter S of chapter 1 of the Internal Revenue Code.
- (3) The tax imposed by section 1374 of the Internal Revenue Code [is hereby imposed by this chapter at an amount equal to 3.08 per cent on the amount by which the net capital gain of the corporation exceeds \$25,000. For the purposes of section 1374(c)(3) of the Internal Revenue Code the amount of tax to be determined shall not exceed 3.08 per cent on the net capital gain attributable to property acquired as provided in section 1374(c)(3)(B) of the Internal Revenue Code and having a basis described in section 1374(c)(3)(C) of the Internal Revenue Code.] is hereby imposed by this chapter at an amount equal to 6.4 per cent of the recognized built-in gain.
- (4) The tax imposed by section 1375(a) of the Internal Revenue Code is hereby imposed by this chapter at an amount equal to [6.435] 6.4 per cent of the amount of the excess net passive income for the taxable year.”

7. Section 235-7 is amended by amending subsection (a) to read as follows:

“(a) There shall be excluded from gross income, adjusted gross income, and taxable income:

- (1) Income not subject to taxation by the State under the Constitution and laws of the United States;
- (2) Rights, benefits, and other income exempted from taxation by section 88-91, having to do with the state retirement system, and the rights, benefits, and other income, comparable to the rights, benefits, and other income exempted by section 88-91, under any other public retirement system;
- (3) Any compensation received in the form of a pension for past services[, or paid as a weekly benefit for unemployment up to but not in excess of the amount provided by the employment security law but the amount of the exclusion shall not exceed the exclusion allowed under section 85 of the Internal Revenue Code made operative for the purposes of this chapter (it being the intention of this provision to exempt that amount whether paid from a fund or account in the federal or state treasury or

- paid by an employer or by a trust or other means provided by an employer)];
- (4) Compensation paid to a patient affected with Hansen's disease employed by the State or the United States in any hospital, settlement, or place for the treatment of Hansen's disease;
 - (5) Except as otherwise expressly provided, payments made by the United States or this State, under an act of Congress or a law of this State, which by express provision or administrative regulation or interpretation are exempt from both the normal and surtaxes of the United States, even though not so exempted by the Internal Revenue Code itself;
 - (6) All proceeds received by organizations enumerated under section 237-23(a)(5) to (8), resulting from the sale of brooms which are manufactured by blind persons working at the adult blind broom shop;
 - (7) Any income expressly exempted or excluded from the measure of the tax imposed by this chapter by any other law of the State, it being the intent of this chapter not to repeal or supersede any such express exemption or exclusion;
 - (8) The first \$500 received by each member of the reserve components of the army, navy, air force, marine corps, coast guard of the United States of America, and the Hawaii national guard as compensation for performance of duty as such;
 - (9) Income derived from the operation of ships or aircraft if such income is exempt under the Internal Revenue Code pursuant to the provisions of an income tax treaty or agreement entered into by and between the United States and a foreign country, provided that the tax laws of the local governments of that country reciprocally exempt from the application of all of their net income taxes, the income derived from the operation of ships or aircraft which are documented or registered under the laws of the United States;
 - (10) The value of legal services provided by a prepaid legal service plan to a taxpayer, the taxpayer's spouse, and the taxpayer's dependents;
 - (11) Amounts paid, directly or indirectly, by a prepaid legal service plan to a taxpayer as payment or reimbursement for the provision of legal services to the taxpayer, the taxpayer's spouse, and the taxpayer's dependents;
 - (12) Contributions by an employer to a prepaid legal service plan for compensation (through insurance or otherwise) to the employer's employees for the costs of legal services incurred by the employer's employees, their spouses, and their dependents."

8. Section 235-7 is amended by amending subsection (c) to read as follows:

"(c) The deductions of or based on dividends paid or received, allowed to a corporation under chapter 1, subchapter B, Part VIII of the Internal Revenue Code, shall not be allowed. In lieu thereof there shall be allowed as a deduction the entire amount of dividends received by any corporation upon the shares of stock of a national banking association, or received by a small business investment company operating under the Small Business Investment Act of 1958 (Public Law 85-699) upon shares of stock qualifying under paragraph (3) below, [eighty-five] eighty per cent of the amount received by any corporation as dividends:

- (1) Upon the shares of stock of another corporation, if at the date of payment of the dividend at least ninety-five per cent of the other corporation's capital stock is owned by one or more corporations doing business in this State and if the other corporation is subjected to an income tax in another jurisdiction (but subjection to federal tax does not constitute subjection to income tax in another jurisdiction);
- (2) Upon the shares of stock of a bank or insurance company organized and doing business under the laws of the State;
- (3) Upon the shares of stock of another corporation, if at least fifteen per cent of the latter corporation's business, for the taxable year of the latter corporation preceding the payment of the dividend, has been attributed to this State.

However, except for national bank dividends, the deductions under this subsection are not allowed when they would not have been allowed under section 243 of the Internal Revenue Code, as amended by Public Law 85-866, by reason of subsections (b) and (c) of section 246 of the Internal Revenue Code, as [so] amended. For the purposes of this subsection fifteen per cent of a corporation's business shall be deemed to have been attributed to this State if fifteen per cent or more of the entire gross income of the corporation as defined in this chapter (which for the purposes of this subsection shall be computed without regard to source in the State and shall include income not taxable by reason of the fact that it is from property not owned in the State or from a trade or business not carried on in the State in whole or in part) shall, under section 235-5 and the other provisions of this chapter, have been attributed to the State and subjected to assessment of the taxable income therefrom (including the determination of the resulting net loss, if any)."

9. Section 235-8 is repealed.

10. Section 235-9 is amended to read as follows:

"§235-9 Exemptions; generally. [(a)] Except as provided in sections 235-61 to 235-67 relating to withholding and collection of tax at source, and section 235-2.4[(e)] relating to "unrelated business taxable income", the following persons and organizations shall not be taxable under this chapter:

- [(1)] Banks, building and loan associations, industrial loan companies, financial corporations, small business investment companies, and development companies taxable under chapter 241; and insurance companies [and], agricultural cooperative associations, and fish marketing associations exclusively taxable under other laws[;
- (2) Corporations, companies, associations, or trusts conducted solely for charitable, religious, educational, prepaid legal services, or scientific purposes within the State, including fraternal beneficiary societies;
- (3) Corporations, companies, associations, or trusts organized for the establishment and conduct of cemeteries, no part of the net earnings of which inures to the financial benefit of any private shareholder or individual;
- (4) Business leagues, chambers of commerce, real estate boards, or boards of trade, not organized for profit, and no part of the net earnings of which inures to the benefit of any private shareholder or individual;
- (5) Civic leagues or organizations, not organized for profit but operated exclusively for the promotion of social welfare, which shall

include the operation of a prepaid legal service plan, or local associations of employees, the membership of which is limited to the employees of a designated person or persons, and the net earnings of which are devoted exclusively to charitable, educational, prepaid legal service, or recreational purposes within the State;

- (6) Labor organizations;
- (7) Clubs organized and operated exclusively for pleasure, recreation, and other nonprofit purposes, no part of the net earnings of which inures to the benefit of any private shareholder;
- (8) A trust forming part of a stock bonus, pension, or profit-sharing plan of an employer for the exclusive benefit of the employer's employees or their beneficiaries, and which meets the requirements of the Internal Revenue Code for exemption from the tax thereby imposed.

(b) Notwithstanding that any person is exempted from taxation by the Internal Revenue Code, nevertheless if the person is not exempted from taxation by this chapter, the person or it shall be taxed in accordance with this chapter].”

11. Section 235-51 is amended to read as follows:

“§235-51 Tax imposed on individuals; rates. (a) There is hereby imposed on the taxable income of (1) every taxpayer who files a joint return under section 235-93; and (2) every surviving spouse a tax determined in accordance with the following table:

If taxable income is:	The tax is:
Not over \$1,000	No Tax
Over \$1,000, but not over \$2,000	2.25% of excess over \$1,000
Over \$2,000, but not over \$3,000	\$22.50 plus 3.25% of excess over \$2,000
Over \$3,000, but not over \$4,000	\$55.00 plus 4.5% of excess over \$3,000
Over \$4,000, but not over \$5,000	\$100.00 plus 5.0% of excess over \$4,000
Over \$5,000, but not over \$7,000	\$150.00 plus 6.5% of excess over \$5,000
Over \$7,000, but not over \$11,000	\$280.00 plus 7.5% of excess over \$7,000
Over \$11,000, but not over \$21,000	\$580.00 plus 8.5% of excess over \$11,000
Over \$21,000, but not over \$29,000	\$1,430.00 plus 9.5% of excess over \$21,000
Over \$29,000, but not over \$41,000	\$2,190.00 plus 10.0% of excess over \$29,000
Over \$41,000, but not over \$61,000	\$3,390.00 plus 10.5% of excess over \$41,000
Over \$61,000	\$5,490.00 plus 11.0% of excess over \$61,000]

In the case of any taxable year beginning after December 31, 1986, and ending before January 1, 1988:

If the taxable income is:

The tax shall be:

<u>Not over \$2,000</u>	<u>2.25% of taxable income</u>
<u>Over \$2,000 but not over \$4,000</u>	<u>\$45.00 plus 4.25% of excess over \$2,000</u>
<u>Over \$4,000 but not over \$6,000</u>	<u>\$130.00 plus 6.25% of excess over \$4,000</u>
<u>Over \$6,000 but not over \$10,000</u>	<u>\$255.00 plus 7.25% of excess over \$6,000</u>
<u>Over \$10,000 but not over \$20,000</u>	<u>\$545.00 plus 8.25% of excess over \$10,000</u>
<u>Over \$20,000 but not over \$28,000</u>	<u>\$1,370.00 plus 9.25% of excess over \$20,000</u>
<u>Over \$28,000 but not over \$40,000</u>	<u>\$2,110.00 plus 9.75% of excess over \$28,000</u>
<u>Over \$40,000</u>	<u>\$3,280.00 plus 10% of excess over \$40,000</u>

In the case of any taxable year beginning after December 31, 1987, and ending before January 1, 1989:

<u>If the taxable income is:</u>	<u>The tax shall be:</u>
<u>Not over \$2,400</u>	<u>2.25% of taxable income</u>
<u>Over \$2,400 but not over \$4,400</u>	<u>\$54.00 plus 4.25% of excess over \$2,400</u>
<u>Over \$4,400 but not over \$6,400</u>	<u>\$139.00 plus 6.25% of excess over \$4,400</u>
<u>Over \$6,400 but not over \$10,400</u>	<u>\$264.00 plus 7.25% of excess over \$6,400</u>
<u>Over \$10,400 but not over \$20,400</u>	<u>\$554.00 plus 8.25% of excess over \$10,400</u>
<u>Over \$20,400 but not over \$28,400</u>	<u>\$1,379.00 plus 9.25% of excess over \$20,400</u>
<u>Over \$28,400 but not over \$40,400</u>	<u>\$2,119.00 plus 9.75% of excess over \$28,400</u>
<u>Over \$40,400</u>	<u>\$3,289.00 plus 10% of excess over \$40,400</u>

In the case of any taxable year beginning after December 31, 1988:

<u>If the taxable income is:</u>	<u>The tax shall be:</u>
<u>Not over \$3,000</u>	<u>2.25% of taxable income</u>
<u>Over \$3,000 but not over \$5,000</u>	<u>\$67.50 plus 4.25% of excess over \$3,000</u>
<u>Over \$5,000 but not over \$7,000</u>	<u>\$152.50 plus 6.25% of excess over \$5,000</u>
<u>Over \$7,000 but not over \$11,000</u>	<u>\$277.50 plus 7.25% of excess over \$7,000</u>
<u>Over \$11,000 but not over \$21,000</u>	<u>\$567.50 plus 8.25% of excess over \$11,000</u>
<u>Over \$21,000 but not over \$29,000</u>	<u>\$1,392.50 plus 9.25% of excess over \$21,000</u>
<u>Over \$29,000 but not over \$41,000</u>	<u>\$2,132.50 plus 9.75% of excess over \$29,000</u>
<u>Over \$41,000</u>	<u>\$3,302.50 plus 10% of excess over \$41,000</u>

ACT 239

(b) There is hereby imposed on the taxable income of every head of a household a tax determined in accordance with the following table:

[If taxable income is:	The tax is:
Not over \$800	No Tax
Over \$800, but not over \$1,300	2.25% of excess over \$800
Over \$1,300, but not over \$1,800	\$11.25 plus 2.75% of excess over \$1,300
Over \$1,800, but not over \$2,300	\$25.00 plus 3.9% of excess over \$1,800
Over \$2,300, but not over \$2,800	\$44.50 plus 4.1% of excess over \$2,300
Over \$2,800, but not over \$3,800	\$65.00 plus 5.5% of excess over \$2,800
Over \$3,800, but not over \$5,800	\$120.00 plus 6.6% of excess over \$3,800
Over \$5,800, but not over \$10,800	\$252.00 plus 7.9% of excess over \$5,800
Over \$10,800, but not over \$20,800	\$647.00 plus 9.15% of excess over \$10,800
Over \$20,800, but not over \$30,800	\$1,562.00 plus 10.05% of excess over \$20,800
Over \$30,800, but not over \$40,800	\$2,567.00 plus 10.5% of excess over \$30,800
Over \$40,800, but not over \$60,800	\$3,617.00 plus 10.75% of excess over \$40,800
Over \$60,800	\$5,767.00 plus 11.0% of excess over \$60,800]

In the case of any taxable year beginning after December 31, 1986,
and ending before January 1, 1988:

<u>If the taxable income is:</u>	<u>The tax shall be:</u>
<u>Not over \$1,000</u>	<u>2.25% of taxable income</u>
<u>Over \$1,000 but not over \$2,000</u>	<u>\$22.50 plus 3.25% of excess over \$1,000</u>
<u>Over \$2,000 but not over \$3,000</u>	<u>\$55.00 plus 5.25% of excess over \$2,000</u>
<u>Over \$3,000 but not over \$5,000</u>	<u>\$107.50 plus 6.25% of excess over \$3,000</u>
<u>Over \$5,000 but not over \$10,000</u>	<u>\$232.50 plus 7.25% of excess over \$5,000</u>
<u>Over \$10,000 but not over \$20,000</u>	<u>\$595.00 plus 8.9% of excess over \$10,000</u>
<u>Over \$20,000 but not over \$40,000</u>	<u>\$1,485.00 plus 9.8% of excess over \$20,000</u>
<u>Over \$40,000</u>	<u>\$3,445.00 plus 10% of excess over \$40,000</u>

In the case of any taxable year beginning after December 31, 1987,
and ending before January 1, 1989:

<u>If the taxable income is:</u>	<u>The tax shall be:</u>
<u>Not over \$1,200</u>	<u>2.25% of taxable income</u>

<u>Over \$1,200 but not over \$2,200</u>	<u>\$27.00 plus 3.25% of excess over \$1,200</u>
<u>Over \$2,200 but not over \$3,200</u>	<u>\$59.50 plus 5.25% of excess over \$2,200</u>
<u>Over \$3,200 but not over \$5,200</u>	<u>\$112.00 plus 6.25% of excess over \$3,200</u>
<u>Over \$5,200 but not over \$10,400</u>	<u>\$237.00 plus 7.25% of excess over \$5,200</u>
<u>Over \$10,400 but not over \$20,400</u>	<u>\$614.00 plus 8.9% of excess over \$10,400</u>
<u>Over \$20,400 but not over \$40,400</u>	<u>\$1,504.00 plus 9.8% of excess over \$20,400</u>
<u>Over \$40,400</u>	<u>\$3,464.00 plus 10% of excess over \$40,400</u>

In the case of any taxable year beginning after December 31, 1988:

If the taxable income is:

<u>Not over \$1,500</u>
<u>Over \$1,500 but not over \$2,500</u>
<u>Over \$2,500 but not over \$3,500</u>
<u>Over \$3,500 but not over \$5,500</u>
<u>Over \$5,500 but not over \$11,000</u>
<u>Over \$11,000 but not over \$21,000</u>
<u>Over \$21,000 but not over \$41,000</u>
<u>Over \$41,000</u>

The tax shall be:

<u>2.25% of taxable income</u>
<u>\$33.75 plus 3.25% of excess over \$1,500</u>
<u>\$66.25 plus 5.25% of excess over \$2,500</u>
<u>\$118.75 plus 6.25% of excess over \$3,500</u>
<u>\$243.75 plus 7.25% of excess over \$5,500</u>
<u>\$642.50 plus 8.9% of excess over \$11,000</u>
<u>\$1,532.50 plus 9.8% of excess over \$21,000</u>
<u>\$3,492.50 plus 10% of excess over \$41,000</u>

(c) There is hereby imposed on the taxable income of (1) every unmarried individual (other than a surviving spouse, or the head of a household) and (2) on the taxable income of every married individual who does not make a single return jointly with the individual's spouse under section 235-93 a tax determined in accordance with the following table:

[If taxable income is:

<u>Not over \$800</u>
<u>Over \$800, but not over \$1,300</u>
<u>Over \$1,300, but not over \$1,800</u>
<u>Over \$1,800, but not over \$2,300</u>
<u>Over \$2,300, but not over \$2,800</u>
<u>Over \$2,800, but not over \$3,800</u>
<u>Over \$3,800, but not over \$5,800</u>
<u>Over \$5,800, but</u>

The tax is:

<u>No Tax</u>
<u>2.25% of excess over \$800</u>
<u>\$11.25 plus 3.25% of excess over \$1,300</u>
<u>\$27.50 plus 4.5% of excess over \$1,800</u>
<u>\$50.00 plus 5.0% of excess over \$2,300</u>
<u>\$75.00 plus 6.5% of excess over \$2,800</u>
<u>\$140.00 plus 7.5% of excess over \$3,800</u>
<u>\$290.00 plus 8.5% of</u>

ACT 239

not over \$10,800
Over \$10,800, but
not over \$14,800
Over \$14,800, but
not over \$20,800
Over \$20,800, but
not over \$30,800
Over \$30,800

excess over \$5,800
\$715.00 plus 9.5% of
excess over \$10,800
\$1,095.00 plus 10.0% of
excess over \$14,800
\$1,695.00 plus 10.5% of
excess over \$20,800
\$2,745.00 plus 11.0% of
excess over \$30,800]

In the case of any taxable year beginning after December 31, 1986,
and ending before January 1, 1988:

If the taxable income is:

Not over \$1,000
Over \$1,000 but
not over \$2,000
Over \$2,000 but
not over \$3,000
Over \$3,000 but
not over \$5,000
Over \$5,000 but
not over \$10,000
Over \$10,000 but
not over \$14,000
Over \$14,000 but
not over \$20,000
Over \$20,000

The tax shall be:

2.25% of taxable income
\$22.50 plus 4.25% of
excess over \$1,000
\$65.00 plus 6.25% of
excess over \$2,000
\$127.50 plus 7.25% of
excess over \$3,000
\$272.50 plus 8.25% of
excess over \$5,000
\$685.00 plus 9.25% of
excess over \$10,000
\$1,055.00 plus 9.75% of
excess over \$14,000
\$1,640.00 plus 10% of
excess over \$20,000

In the case of any taxable year beginning after December 31, 1987,
and ending before January 1, 1989:

If the taxable income is:

Not over \$1,200
Over \$1,200 but
not over \$2,200
Over \$2,200 but
not over \$3,200
Over \$3,200 but
not over \$5,200
Over \$5,200 but
not over \$10,200
Over \$10,200 but
not over \$14,200
Over \$14,200 but
not over \$20,200
Over \$20,200

The tax shall be:

2.25% of taxable income
\$27.00 plus 4.25% of
excess over \$1,200
\$69.50 plus 6.25% of
excess over \$2,200
\$132.00 plus 7.25% of
excess over \$3,200
\$277.00 plus 8.25% of
excess over \$5,200
\$689.50 plus 9.25% of
excess over \$10,200
\$1,059.50 plus 9.75% of
excess over \$14,200
\$1,644.50 plus 10% of
excess over \$20,200

In the case of any taxable year beginning after December 31, 1988:

If the taxable income is:

Not over \$1,500
Over \$1,500 but

The tax shall be:

2.25% of taxable income
\$33.75 plus 4.25% of

<u>not over \$2,500</u>	<u>excess over \$1,500</u>
<u>Over \$2,500 but</u>	<u>\$76.25 plus 6.25% of</u>
<u>not over \$3,500</u>	<u>excess over \$2,500</u>
<u>Over \$3,500 but</u>	<u>\$138.75 plus 7.25% of</u>
<u>not over \$5,500</u>	<u>excess over \$3,500</u>
<u>Over \$5,500 but</u>	<u>\$283.75 plus 8.25% of</u>
<u>not over \$10,500</u>	<u>excess over \$5,500</u>
<u>Over \$10,500 but</u>	<u>\$696.25 plus 9.25% of</u>
<u>not over \$14,500</u>	<u>excess over \$10,500</u>
<u>Over \$14,500 but</u>	<u>\$1,066.25 plus 9.75% of</u>
<u>not over \$20,500</u>	<u>excess over \$14,500</u>
<u>Over \$20,500</u>	<u>\$1,651.25 plus 10% of</u>
	<u>excess over \$20,500</u>

[(d) There is hereby imposed on the taxable income of every married individual who does not make a single return jointly with the individual's spouse under section 235-93 a tax determined in accordance with the following table:

If taxable income is:	The tax is:
Not over \$500	No Tax
Over \$500, but not over \$1,000	2.25% of excess over \$500
Over \$1,000, but not over \$1,500	\$11.25 plus 3.25% of excess over \$1,000
Over \$1,500, but not over \$2,000	\$27.50 plus 4.5% of excess over \$1,500
Over \$2,000, but not over \$2,500	\$50.00 plus 5.0% of excess over \$2,000
Over \$2,500, but not over \$3,500	\$75.00 plus 6.5% of excess over \$2,500
Over \$3,500, but not over \$5,500	\$140.00 plus 7.5% of excess over \$3,500
Over \$5,500, but not over \$10,500	\$290.00 plus 8.5% of excess over \$5,500
Over \$10,500, but not over \$14,500	\$715.00 plus 9.5% of excess over \$10,500
Over \$14,500, but not over \$20,500	\$1,095.00 plus 10.0% of excess over \$14,500
Over \$20,500, but not over \$30,500	\$1,695.00 plus 10.5% of excess over \$20,500
Over \$30,500	\$2,745.00 plus 11.0% of excess over \$30,500

(e) [(d) The tax imposed by section 235-2.4[(f)] on estates and trusts shall be determined in accordance with the following table:

[If taxable income is:	The tax is:
Not over \$500	2.25% of taxable income
Over \$500, but not over \$1,000	\$11.25 plus 3.25% of excess over \$500
Over \$1,000, but not over \$1,500	\$27.50 plus 4.5% of excess over \$1,000
Over \$1,500, but not over \$2,000	\$50.00 plus 5% of excess over \$1,500

ACT 239

Over \$2,000, but not over \$3,000	\$75.00 plus 6.5% of excess over \$2,000
Over \$3,000, but not over \$5,000	\$140.00 plus 7.5% of excess over \$3,000
Over \$5,000, but not over \$10,000	290.00 plus 8.5% of excess over \$5,000
Over \$10,000, but not over \$14,000	715.00 plus 9.5% of excess over \$10,000
Over \$14,000, but not over \$20,000	\$1,095.00 plus 10% of excess over \$14,000
Over \$20,000, but not over \$30,000	\$1,695.00 plus 10.5% of excess over \$20,000
Over \$30,000	\$2,745.00 plus 11% of excess over \$30,000]

In the case of any taxable year beginning after December 31, 1986,
and ending before January 1, 1988:

<u>If the taxable income is:</u>	<u>The tax shall be:</u>
<u>Not over \$1,000</u>	<u>2.25% of taxable income</u>
<u>Over \$1,000 but not over \$2,000</u>	<u>\$22.50 plus 4.25% of excess over \$1,000</u>
<u>Over \$2,000 but not over \$3,000</u>	<u>\$65.00 plus 6.25% of excess over \$2,000</u>
<u>Over \$3,000 but not over \$5,000</u>	<u>\$127.50 plus 7.25% of excess over \$3,000</u>
<u>Over \$5,000 but not over \$10,000</u>	<u>\$272.50 plus 8.25% of excess over \$5,000</u>
<u>Over \$10,000 but not over \$14,000</u>	<u>\$685.00 plus 9.25% of excess over \$10,000</u>
<u>Over \$14,000 but not over \$20,000</u>	<u>\$1,055.00 plus 9.75% of excess over \$14,000</u>
<u>Over \$20,000</u>	<u>\$1,640.00 plus 10% of excess over \$20,000</u>

In the case of any taxable year beginning after December 31, 1987,
and ending before January 1, 1989:

<u>If the taxable income is:</u>	<u>The tax shall be:</u>
<u>Not over \$1,200</u>	<u>2.25% of taxable income</u>
<u>Over \$1,200 but not over \$2,200</u>	<u>\$27.00 plus 4.25% of excess over \$1,200</u>
<u>Over \$2,200 but not over \$3,200</u>	<u>\$69.50 plus 6.25% of excess over \$2,200</u>
<u>Over \$3,200 but not over \$5,200</u>	<u>\$132.00 plus 7.25% of excess over \$3,200</u>
<u>Over \$5,200 but not over \$10,200</u>	<u>\$277.00 plus 8.25% of excess over \$5,200</u>
<u>Over \$10,200 but not over \$14,200</u>	<u>\$689.50 plus 9.25% of excess over \$10,200</u>
<u>Over \$14,200 but not over \$20,200</u>	<u>\$1,059.50 plus 9.75% of excess over \$14,200</u>
<u>Over \$20,200</u>	<u>\$1,644.50 plus 10% of excess over \$20,200</u>

In the case of any taxable year beginning after December 31, 1988:

<u>If the taxable income is:</u>	<u>The tax shall be:</u>
<u>Not over \$1,500</u>	<u>2.25% of taxable income</u>
<u>Over \$1,500 but not over \$2,500</u>	<u>\$33.75 plus 4.25% of excess over \$1,500</u>
<u>Over \$2,500 but not over \$3,500</u>	<u>\$76.25 plus 6.25% of excess over \$2,500</u>
<u>Over \$3,500 but not over \$5,500</u>	<u>\$138.75 plus 7.25% of excess over \$3,500</u>
<u>Over \$5,500 but not over \$10,500</u>	<u>\$283.75 plus 8.25% of excess over \$5,500</u>
<u>Over \$10,500 but not over \$14,500</u>	<u>\$696.25 plus 9.25% of excess over \$10,500</u>
<u>Over \$14,500 but not over \$20,500</u>	<u>\$1,066.25 plus 9.75% of excess over \$14,500</u>
<u>Over \$20,500</u>	<u>\$1,651.25 plus 10% of excess over \$20,500</u>

[(f) (e) Any taxpayer, other than a corporation, acting as a business entity in more than one state who is required by this chapter to file a return may elect to report and pay a tax of .5 per cent of its annual gross sales (1) where the taxpayer's only activities in this State consist of sales; and (2) who does not own or rent real estate or tangible personal property; and (3) whose annual gross sales in or into this State during the tax year is not in excess of \$100,000.

(f) If a taxpayer has a net capital gain for any taxable year to which this subsection applies, then the tax imposed by this section shall not exceed the sum of:

- (1) The tax computed at the rates and in the same manner as if this subsection had not been enacted on the greater of:
 - (A) The taxable income reduced by the amount of net capital gain, or
 - (B) The amount of taxable income taxed at a rate below 7.25 per cent, plus
- (2) A tax of 7.25 per cent of the amount of taxable income in excess of the amount determined under paragraph (1)(A).

This subsection shall apply to individuals, estates, and trusts for taxable years beginning after December 31, 1986.

(g) This section shall not be effective after December 31, 1990."

12. Section 235-52 is amended to read as follows:

"§235-52 Tax in case of joint return or return of surviving spouse. In the case of a joint return of a husband and wife under section 235-93, the tax imposed, as near as may be, by this chapter shall be twice the tax which would be imposed if the taxable income were cut in half [subject to the inclusion of zero-bracket amounts]. For purposes of this section and section 235-53, a return of a surviving spouse, as defined in the Internal Revenue Code, shall be treated as a joint return of a husband and wife under section 235-93."

13. Section 235-53 is amended by amending subsection (a) to read as follows:

"(a) Imposition of tax table tax:

- (1) In general. In lieu of the tax imposed by section 235-51, there is hereby imposed for each taxable year on the [tax table income of every individual whose tax table income for such year does not exceed the ceiling amount,] taxable income of every individual:
(A) Who does not itemize the individual's deductions for the taxable year; and
(B) Whose taxable income for such taxable year does not exceed the ceiling amount,
 a tax determined under tables, applicable to such taxable year, which shall be prescribed by the director. In the tables so prescribed, the amounts of tax shall be computed on the basis of the rates prescribed by section 235-51.
- (2) Ceiling amount defined. For purposes of paragraph (1), the term "ceiling amount" means, with respect to any taxpayer, the amount (not less than \$20,000) determined by the director for the tax rate category in which such taxpayer falls.
- (3) Certain taxpayers with large number of exemptions. The director may exclude from the application of this section taxpayers in any tax rate category having more than the number of exemptions for that category determined by the director.
- (4) Tax table income defined. For purposes of this section, the term "tax table income" means adjusted gross income:
 (A) Reduced by the excess itemized deductions, and
 (B) Increased (in the case of a married individual filing a separate return where either spouse itemizes deductions) by the unused zero-bracket amount.]
- (3) Authority to prescribe tables for taxpayers who itemize deductions. The director may provide that this section shall apply also for any taxable year to individuals who itemize their deductions. Any tables prescribed under the preceding sentence shall be on the basis of taxable income."

14. Section 235-53 is amended by amending subsection (d) to read as follows:

"(d) Taxable income. Whenever it is necessary to determine the taxable income of an individual to whom this section applies, the taxable income shall be determined under section [63 (with respect to taxable income defined) of the Internal Revenue Code as made operative in this chapter.] 235-2.4(a)."

15. Section 235-54 is amended by amending subsection (a) to read as follows:

"(a) In computing the taxable income of any individual, there shall be deducted, in lieu of the personal exemptions allowed by the Internal Revenue Code, personal exemptions computed as follows: Ascertain the number of exemptions which the individual can lawfully claim under the Internal Revenue Code, add an additional exemption for the taxpayer or the taxpayer's spouse who is sixty-five years of age or older within the taxable year, and multiply that number by [the amount as shown below for the corresponding taxable years as follows:

- (1) Effective with respect to taxable years beginning after December 31, 1979, the amount shall be \$1,000.
- (2) Effective with respect to taxable years beginning after December 31, 1984, the amount shall be \$1,040.] \$1,040, for taxable years beginning after December 31, 1984.

A nonresident shall be entitled to the same personal exemptions as a resident, without proration of the personal exemptions on account of income from sources outside the State. In the case of an individual with respect to whom an exemption under this section is allowable to another taxpayer for a taxable year beginning in the calendar year in which the individual's taxable year begins, the personal exemption amount applicable to such individual under this subsection for such individual's taxable year shall be zero."

16. Section 235-55.6 is amended by amending subsection (e) to read as follows:

"(e) Special rules. For purposes of this section:

- (1) Maintaining household. An individual shall be treated as maintaining a household for any period only if over half the cost of maintaining the household for such period is furnished by such individual (or, if such individual is married during such period, is furnished by such individual and the individual's spouse).
- (2) Married couples must file joint return. If the taxpayer is married at the close of the taxable year, the credit shall be allowed under subsection (a) only if the taxpayer and the taxpayer's spouse file a joint return for the taxable year.
- (3) Marital status. An individual legally separated from the individual's spouse under a decree of divorce or of separate maintenance shall not be considered as married.
- (4) Certain married individuals living apart. If:
 - (A) An individual who is married and who files a separate return:
 - (i) Maintains as the individual's home a household which constitutes for more than one-half of the taxable year the principal place of abode of a qualifying individual, and
 - (ii) Furnishes over half of the cost of maintaining such household during the taxable year, and
 - (B) During the last six months of such taxable year such individual's spouse is not a member of such household, such individual shall not be considered as married.
- (5) Special dependency test in case of divorced parents, etc. If:
 - (A) Paragraph (2) or (4) of section 152(e) of the Internal Revenue Code of 1954, as amended, applies to any child with respect to any calendar year; and
 - (B) Such child is under age fifteen or is physically or mentally incompetent of caring for the child's self; in the case of any taxable year beginning in such calendar year, such child shall be treated as a qualifying individual described in subsection (b)(1)(A) or (B) (whichever is appropriate) with respect to the custodial parent (within the meaning of section 152(e)(1) of the Internal Revenue Code of 1954, as amended), and shall not be treated as a qualifying individual with respect to the noncustodial parent.
- (6) Payments to related individuals. No credit shall be allowed under subsection (a) for any amount paid by the taxpayer to an individual:
 - (A) With respect to whom, for the taxable year, a deduction under section [151(e)] 151(c) of the Internal Revenue

Code of 1954, as amended (relating to deduction for personal exemptions for dependents) is allowable either to the taxpayer or the taxpayer's spouse, or

- (B) Who is a child of the taxpayer (within the meaning of section [151(e)(3)] 151(c)(3) of the Internal Revenue Code of 1954, as amended) who has not attained the age of nineteen at the close of the taxable year.

For purposes of this paragraph, the term "taxable year" means the taxable year of the taxpayer in which the service is performed.

- (7) Student. The term "student" means an individual who during each of five calendar months during the taxable year is a full-time student at an educational organization.
- (8) Educational organization. The term "educational organization" means a school operated by the department of education or licensed under chapter 298, or a university, college, or community college."

17. Section 235-61 is amended by amending subsection (c) to read as follows:

"(c) For each withholding period (whether weekly, biweekly, monthly, or otherwise) the amount of tax to be withheld under this section shall be at a rate which, for the taxable year, will yield the tax imposed by section 235-51 upon each employee's annual wage, as estimated from the employee's current wage in any withholding period, but (for the purposes of this subsection) of the rates provided by section 235-51 the maximum to be taken into consideration shall be eight per cent. The tax for the taxable year shall be calculated upon the following assumptions:

- (1) That the employee's annual wage, as estimated from the employee's current wage in the withholding period, will be the employee's sole income for the taxable year;
- (2) That there will be no deductions therefrom in determining adjusted gross income;
- (3) That in determining taxable income there [will be deductions in the amount of \$1,000 (\$800 in the case of an individual who is not married and who is not a surviving spouse);] shall be a standard deduction allowance which shall be an amount equal to one exemption (or more than one exemption if so prescribed by the director) unless (A) the taxpayer is married and the taxpayer's spouse is an employee receiving wages subject to withholding, or (B) the taxpayer has withholding exemption certificates in effect with respect to more than one employer. For the purposes of this section, any standard deduction allowance under this paragraph shall be treated as if it were denominated a withholding exemption.
- (4) That in determining taxable income there also will be deducted the amount of exemptions and withholding allowances granted to the employee in the computation of taxable income, as shown by a certificate to be filed with the employer as provided by subsection (f); and
- (5) If it appears from the certificate filed pursuant to subsection (f) that the employee is, under section 235-93, entitled to make a joint return, that the employee and the employee's spouse will so elect."

18. Section 235-61 is amended by amending subsection (g) to read as follows:

“(g) In determining the deduction allowed by subsection (c)(4) an employee shall be entitled to withholding allowances or additional reductions in withholding under this subsection [with respect to a payment of wages equal to the number determined by dividing by \$1,000 the excess of the employee’s estimated itemized deductions over an amount equal to \$1,000 (\$800 in the case of an individual who is not married and who is not a surviving spouse)]. In determining the number of additional withholding allowances or the amount of additional reductions in withholding under this subsection, the employee may take into account (to the extent and in the manner provided by rules) estimated itemized deductions and tax credits allowable under this chapter; and such additional deductions and other items as may be specified by the director in rules. For the purposes of this subsection a fractional number shall not be taken into account unless it amounts to one-half or more, in which case it shall be increased to the next whole number.

(1) As used in this subsection, unless the context otherwise requires:

(A) “Estimated itemized deductions” means the aggregate amount which the employee reasonably expects will be allowed as deductions under sections 235-2.3, 235-2.4, and 235-7, other than the deductions referred to in Internal Revenue Code section 151 and those deductions required to be taken into account in determining adjusted gross income under Internal Revenue Code section 62(a) (with the exception of paragraph [13] 10 thereof) for the estimation year. In no case shall such aggregate amount be greater than the sum of:

(i) The amount of such deductions [(or the zero bracket amount (within the meaning of section 235-2.4(a)))] reflected in the employee’s net income tax return for the taxable year preceding the estimation year of (if such a return has not been filed for such preceding taxable year at the time the withholding exemption certificate is furnished the employer) the second taxable year preceding the estimation year, [and] or

(ii) The amount of estimated itemized deductions and tax credits allowable under this chapter and such additional deductions to which entitled, and

[(ii)] (iii) The amount of the employee’s determinable additional deductions for the estimation year.

(B) “Estimated wages” means the aggregate amount which the employee reasonably expects will constitute wages for the estimation year.

(C) “Determinable additional deductions” means those estimated itemized deductions which:

(i) Are in excess of the deductions referred to in subparagraph (A) [(or the zero bracket amount)] reflected on the employee’s net income tax return for the taxable year preceding the estimation year; and

(ii) Are demonstrably attributable to an identifiable event during the estimation year or the preceding taxable year which can reasonably be expected to

- cause an increase in the amount of such deductions on the net income tax return for the estimation year.
- (D) "Estimation year", in the case of an employee who files the employee's return on the basis of a calendar year, means the calendar year in which the wages are paid; provided that in the case of an employee who files the employee's return on a basis other than the calendar year, the employee's estimation year, and the amounts deducted and withheld to be governed by such estimation year, shall be determined under rules prescribed by the director of taxation.
- (2) Under this subsection, the following special rules shall apply:
- (A) Married individuals. The number of withholding allowances to which a husband and wife are entitled under this subsection shall be determined on the basis of their combined wages and deductions. This subparagraph shall not apply to a husband and wife who filed separate returns for the taxable year preceding the estimation year and who reasonably expect to file separate returns for the estimation year.
- (B) Limitation. In the case of employees whose estimated wages are at levels at which the amounts deducted and withheld under this chapter generally are insufficient (taking into account a reasonable allowance for deductions and exceptions) to offset the liability for tax under this chapter with respect to the wages from which such amounts are deducted and withheld, the director may by rule reduce the withholding allowances to which such employees would, but for this subparagraph, be entitled under this subsection.
- (C) Treatment of allowances. For purposes of this chapter, any withholding allowance under this subsection shall be treated as if it were denominated a withholding exemption.
- (3) The director may prescribe tables by rule under chapter 91 pursuant to which employees shall determine the number of withholding allowances to which they are entitled under this subsection."

19. Section 235-71 is amended to read as follows:

"§235-71 Tax on corporations; rates; credit of shareholder of regulated investment company. (a) A tax at the rates herein provided shall be assessed, levied, collected, and paid for each taxable year on the taxable income of every corporation, including a corporation carrying on business in partnership, except that in the case of a regulated investment company the tax is as provided by subsection (b) and further that in the case of a real estate investment trust as defined in section 856 of the Internal Revenue Code of 1954 the tax is as provided in subsection (d). "Corporation" includes any professional corporation incorporated pursuant to chapter [416.] 415A.

The tax [shall be at the rate of 3.08 per cent on such amount of capital gain as, under the Internal Revenue Code, is entitled to the alternative tax treatment, and] on all [other] taxable income [the tax] other than income from capital gains shall be at the rate of [5.85] 4.4 per cent if the taxable income is not over \$25,000, [and on all over \$25,000, 6.435 per cent.] 5.4 per cent if over \$25,000 but not over \$100,000, and on all over \$100,000, 6.4 per cent; provided that the tax imposed on capital gain entitled to the alternate

tax treatment under the Internal Revenue Code shall be imposed at the rate of 3.08 per cent on the amount of capital gain received before April 1, 1987, and 4 per cent of the amount of capital gain received after March 31, 1987.

(b) In the case of a regulated investment company there is imposed on the taxable income, computed as provided in sections 852 and 855 of the Internal Revenue Code but with the changes and adjustments made by this chapter (without prejudice to the generality of the foregoing, the deduction for dividends paid is limited to such amount of dividends as is attributable to income taxable under this chapter), a tax consisting in the sum of the following: [5.85] 4.4 per cent if the taxable income is not over \$25,000, [and on all over \$25,000, 6.435 per cent; 3.08 per cent on the amount of capital gain which is taxed under section 852(b)(3)(A) of the Internal Revenue Code.] 5.4 per cent if over \$25,000 but not over \$100,000, and on all over \$100,000, 6.4 per cent; provided that the tax imposed on the amount of capital gain which is taxed under section 852(b)(3)(A) of the Internal Revenue Code shall be 3.08 per cent of the amount received before April 1, 1987, and 4 per cent of the amount received after March 31, 1987.

(c) In the case of a shareholder of a regulated investment company there is hereby allowed a credit in the amount of [3.08 per cent of] the tax imposed on the amount of capital gains which by section 852(b)(3)(D) of the Internal Revenue Code is required to be included in the shareholder's return and on which there has been paid to the State by the regulated investment company the tax [of 3.08 per cent] at the rate imposed by subsection (b); the amount of this credit may be applied or refunded as provided in section 235-110.

(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, the deduction for dividends paid is limited to such amount of dividends as is attributable to income taxable under this chapter), a tax consisting in the sum of the following: [5.85] 4.4 per cent if the taxable income is not over \$25,000, [and on all over \$25,000, 6.435 per cent; 3.08 per cent on the amount of capital gain which is taxed under section 857(b)(3)(A) of the Internal Revenue Code.] 5.4 per cent if over \$25,000 but not over \$100,000, and on all over \$100,000, 6.4 per cent; provided that the tax imposed on the amount of capital gain which is taxed under section 857(b)(3)(A) of the Internal Revenue Code shall be 3.08 per cent of the amount received before April 1, 1987, and 4 per cent of the amount received after March 31, 1987. 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 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 taxable year.

(e) Any corporation acting as a business entity in more than one state and which is required by this chapter to file a return and whose only activities in this State consist of sales and which does not own or rent real estate or tangible personal property and whose annual gross sales in or into this State during the tax year are not in excess of \$100,000 may elect to report and pay a tax of .5 per cent of such annual gross sales."

ACT 239

SECTION 2. The effective dates and transitional provisions of Public Law 99-514, the Tax Reform Act of 1986, which relate to sections of the federal Internal Revenue Code of 1986 which are operative for the purposes of chapter 235, Hawaii Revised Statutes, are adopted and made part of this Act; except that such adoption shall not result in the inclusion of income for purposes of taxation under chapter 235, Hawaii Revised Statutes, before January 1, 1987.

SECTION 3. This Part, upon its approval, shall apply with respect to taxable years beginning after December 31, 1986, except as otherwise provided in this Part; provided that section 1(2) of this Part shall apply with respect to taxable years beginning after December 31, 1987. If a taxpayer's taxable year includes the effective date of the tax rate changes (unless that date is the first day of the taxable year), then, (1) the tentative taxes shall be computed by applying the rate for the period before the effective date change, and the rate for the period on and after such date, to the taxable income for the entire taxable year; and (2) the tax for such taxable year shall be the sum of that proportion of each tentative tax which the number of days in each period bears to the number of days in the entire taxable year.

PART II

SECTION 4. Chapter 237, Hawaii Revised Statutes, is amended by adding two new sections to be appropriately designated and to read as follows:

“§237- Exemption for sales of tangible personal property shipped out of the State. (a) There shall be exempted from, and excluded from the measure of, the taxes imposed by this chapter all of the value or gross proceeds arising from the manufacture, production, or sale of tangible personal property:

- (1) Shipped by the manufacturer, producer, or seller to a point outside the State where the property is resold or otherwise consumed or used outside the State in the purchaser's or the taxpayer's business; or
- (2) The sale of which is exempt under section 237-24(19).

(b) For the purposes of this section, the manufacturer, producer, or seller shall take from the purchaser, a certificate, in such form as the department shall prescribe, certifying that the tangible personal property purchased is to be resold or otherwise consumed or used outside the State in the purchaser's business. Any purchaser who shall furnish such a certificate shall be obligated to pay to the seller, upon demand, if the property purchased is not resold or otherwise consumed or used outside the State in the purchaser's business, the amount of the additional tax which by reason thereof is imposed upon the seller.

(c) This section shall not affect the application of section 237-13(2)(A).

§237- Exemption of certain computer services. (a) There shall be exempted from, and excluded from the measure of, the taxes imposed by this chapter all of the gross proceeds arising from technical services necessary for the production and sale of computer software where that software is shipped or transmitted by the provider of technical services to a customer at a point outside the State for use outside the State.

As used in this section:

“Computer software” means a set of computer programs, procedures, or associated documentation concerned with the operation and function of a

computer system, and includes both systems and application programs and subdivisions, such as assemblers, compilers, routines, generators, and utility programs.

“Technical services” include the development, design, modification, and programming of computer software.

(b) For the purposes of this section, the provider of technical services shall take from the purchaser a certificate, in such form as the department shall prescribe, certifying that the software purchased is to be used outside the State. Any purchaser who shall furnish such a certificate shall be obligated to pay to the provider of technical services, upon demand, if the software purchased is used or sold by the purchaser in the State, the amount of the additional tax which by reason of such use or sale is imposed upon the provider of technical services.”

SECTION 5. Section 237-21, Hawaii Revised Statutes, is amended to read as follows:

“**§237-21 Apportionment.** If any person, other than persons liable to the tax on manufacturers as provided by section 237-13(1), is engaged in business both within and without the State or in selling goods for delivery outside the State, and if under the Constitution or laws of the United States or section 237- or 237- the entire gross income of such person cannot be included in the measure of this tax, there shall be apportioned to the State and included in the measure of the tax that portion of the gross income which is derived from activities within the State, to the extent that the apportionment is required by the Constitution or laws of the United States[.] or section 237- or 237-. In the case of a tax upon the production of property in the State the apportionment shall be determined as in the case of the tax on manufacturers. In other cases, if and to the extent that the apportionment cannot be accurately made by separate accounting methods, there shall be apportioned to the State and included in the measure of this tax that proportion of the total gross income, so requiring apportionment, which the cost of doing business within the State, applicable to the gross income, bears to the cost of doing business both within and without the State, applicable to the gross income.”

SECTION 6. Section 237-25, Hawaii Revised Statutes, is amended by amending subsections (d) and (e) to read as follows:

“(d) Millers or processors of sugar, and canners of pineapple and pineapple juice, shall be exempt from tax only when the products are sold, as provided in subsection (a), for use and consumption in the State. The manufacturers, claiming tax exemption for such products, shall furnish the department of taxation certificates of the purchasers, in the form prescribed by the department, certifying that such products have been purchased for use and consumption in the State. As to sugar, pineapple, and pineapple juice, milled, processed, or canned in the State and sold as provided in subsection (a) but not for use and consumption in the State, the miller, processor, or canner shall be [subject to the tax imposed upon the miller, processor, or canner, as a manufacturer, by section 237-13(1).] exempt from tax as provided in section 237-

(e) The exemption granted by this section [shall not apply to the privilege of manufacturing or producing products sold for delivery outside the State or shipped or transported out of the State, but in other cases of products sold in the State as provided in subsection (a), the exemption] shall apply to the seller of products sold in the State as provided in subsection (a) in respect of the privilege of manufacturing or producing, as well as the

ACT 239

privilege of selling, and the value or gross proceeds of sales of the products so sold shall be excluded from the measure of the tax imposed by chapter 237 upon the seller as a manufacturer or producer, [save] as provided in subsection (d).”

SECTION 7. This Part shall take effect on January 1, 1988.

PART III

SECTION 8. Chapter 241, Hawaii Revised Statutes, is amended by adding a new section to be appropriately designated and to read as follows:

“§241- Capital goods excise tax credit. The capital goods excise tax credit provided under section 235- shall be operative for this chapter after December 31, 1987.”

SECTION 9. This Part, upon its approval, shall apply to taxable years beginning after December 31, 1987.

PART IV

SECTION 10. Statutory material to be repealed is bracketed. New statutory material is underscored.²

SECTION 11. Subject to the foregoing effective dates, this Act shall take effect upon its approval.

(Approved June 24, 1987.)

Note

1. So in original.
2. Edited pursuant to HRS §23G-16.5.