



MULTISTATE INCOME/FRANCHISE TAX

Hawaii enacts pass-through entity tax election

Tax Alert

Overview

On June 1, 2023, Hawaii [Senate Bill 1437](#) (S.B. 1437) was enacted into law. Under the legislation, qualifying pass-through entities may make an annual election to pay an entity level state tax. The bill is effective on January 1, 2024 and applies to taxable years beginning after December 31, 2022.

This Tax Alert summarizes some of the provisions of S.B. 1437.

Hawaii pass-through entity tax election

- Entities eligible for the pass-through entity tax (“PTET”) election include partnerships and S corporations.
- A separate election shall be made for each tax year in the form and manner prescribed by the director of the Hawaii Department of Taxation (“Department”).
- The election for that tax year is irrevocable once made and shall be binding on all the partners, shareholders, and members of the pass-through entity.
- S.B. 1437 does not provide guidance on the due date of the election.

Pass-through entity tax calculation

- The PTET is imposed on the sum of all members’ distributive shares and guaranteed payments of Hawaii taxable income. However, the distributive shares and guaranteed payments of members who are corporations are excluded from the tax base and are not subject to the PTET.
- The tax rate for the PTET is equal to the highest individual income tax rate under Haw. Rev. Stat. section 235-51, which is currently 11%.
- A pass-through entity may carry forward losses to subsequent tax years as long as the entity elects to be subject to the PTET.

Pass-through entity tax credit

- Every member of an electing pass-through entity is entitled to a credit against their Hawaii income tax equal to the member's share of the PTET. However, excess credits are nonrefundable. The bill does not provide guidance on whether excess credits may be carried forward or are permanently lost.
- Any member claiming the credit is not entitled to deduct PTET—that is paid and imposed on that member's distributive share or guaranteed payment from the electing pass-through entity—from the member's Hawaii state taxable income.

Credit for residents who pay income tax to another state

- Every member who is a resident or a part-year resident is entitled to a credit against their Hawaii income tax equal to the direct or indirect member's pro rata share of taxes paid to another state (including the District of Columbia), on income of any partnership or S corporation of which the person is a member.
 - To be eligible for tax paid to another state, the tax must be substantially similar to Hawaii's PTET.
 - Excess credits for taxes paid to another state are nonrefundable and do not carry forward.
 - The credit for taxes paid to another state must be calculated in a form and manner prescribed by the director of the Department and the calculation must be consistent with Hawaii's PTET provisions.

Other considerations

- A nonresident individual who is a member of an electing pass-through entity is not required to file an income tax return for a tax year if the member's only source of Hawaii income is from electing pass-through entities and such entities file and pay the PTET due.
- Each pass-through entity—for each tax year—must report to each of its members, the member's pro rata share of the PTET.
- S.B. 1437 authorizes the Department to promulgate rules to implement the provisions of the bill.

Get in touch

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Have a question relating to this or any other pass-through entity tax regime? Reach out to one of our national multistate pass-through entity tax specialists.

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