



STATE OF HAWAII
DEPARTMENT OF TAXATION

P.O. BOX 259
HONOLULU, HAWAII 96809

June 8, 1989

TAX INFORMATION RELEASE

No. 89-4

RE: The Taxpayer Who Is Entitled To The Capital Goods Excise Tax Credit When The Parties Characterize A Transaction As A Lease Or Sale-leaseback.

This Tax Information Release ("TIR") is limited to the issue of who is entitled to the capital goods excise tax credit ("credit") when the parties characterize a transaction as a lease or sale-leaseback (as defined in section I).

Note that the analysis in this TIR should be made only if:

- (1) The acquired property is eligible for the credit (i.e., new or used section 38 property as defined in section I); and
- (2) The transaction is subject to the imposition and payment of tax at the rate of four per cent under chapter 237 or 238, HRS;

I. GENERAL DEFINITIONS FOR PURPOSES OF TIR NO. 89-4

"Acquired" means purchased and placed in service (as defined in TIR No. 88-6) for transactions occurring during calendar year 1988, and placed in service (as defined in TIR No. 88-6) for transactions occurring after December 31, 1988. The terms "purchased and placed in service" and "placed in service" focus on when a claim for the credit may be filed. The timing difference between transactions occurring during calendar year 1988, and transactions occurring after December 31, 1988, is a result of recent legislation (i.e., Act 7, SLH 1989 ("Act 7")).

"Lease" and "sale-leaseback" are defined as they are for federal income tax purposes. The Department adopts the federal income tax characterization of an acquisition. For example, if a transaction is characterized as a lease for federal income tax purposes, the transaction will likewise be characterized as a lease for credit purposes.

"New section 38 property" is defined as stated in TIR No. 88-6 for property acquired both during calendar year 1988, and after December 31, 1988.

"Property acquired after December 31, 1988" includes fiscal year taxpayer acquisitions occurring after December 31, 1988.

"Property acquired during calendar year 1988" includes fiscal year taxpayer acquisitions occurring during the period beginning January 1, 1988, to December 31, 1988.

"Used section 38 property" is defined differently for property acquired during calendar year 1988, and for property acquired after December 31, 1988. For property acquired during calendar year 1988, the term "used section 38 property" is defined as stated in TIR No. 88-6.

In contrast, for property acquired after December 31, 1988, the term "used section 38 property" requires that the property be:

- (1) Section 38 property (as defined in TIR No. 88-6); and
- (2) Not new section 38 property (as defined in TIR No. 88-6).

Note that unlike the case of property acquired during calendar year 1988, property acquired after December 31, 1988, may qualify as used section 38 property even if the property is used by the same person both before and after the acquisition.

The reason for the change in the definition of the term "used section 38 property" is Act 7. Act 7, effective for taxable years after December 31, 1988, amends, among other provisions, section 235-110.7(e), Hawaii Revised Statutes, by deleting the following language:

"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. [Emphasis added.]

As a result of the above stated statutory amendment, the requirement (as stated in TIR No. 88-6) that used section 38 property not be property which is used by the same person both before and after the acquisition is inapplicable for property acquired after December 31, 1988.

II. IN GENERAL

The determination of the taxpayer who is entitled to the credit when the parties characterize a transaction as a lease or sale-leaseback requires an analysis of:

Whether the transaction is, in fact, a lease or sale-leaseback for federal income tax purposes.

The characterization of a transaction as a lease or sale-leaseback determines who is the economic owner ("owner") of the property and thereby entitled to the tax benefits (e.g., credit) associated with the property. Only one party, the owner of the property, is entitled to claim any available credit.

III. LEASE

If a transaction is a lease for federal income tax purposes, the lessor, entering into a lease agreement with respect to property which is eligible for the credit (i.e., new or used section 38 property), is treated as the owner of the property. The lessor may thereby claim any available credit.

IV. SALE-LEASEBACK

If a transaction is a sale-leaseback for federal income tax purposes, the buyer/lessor, entering into a sale-leaseback arrangement with respect to property which is eligible for the credit (i.e., new section 38 property for transactions occurring during calendar year 1988, and new or used section 38 property for transactions occurring after December 31, 1988) is treated as the owner of the property. The buyer/lessor may thereby claim any available credit.

V. SALE

(Note: For purposes of this paragraph, the term "lessee" is used for convenience, without intending to suggest the propriety of the parties' characterization of the transaction as a lease.) If the parties characterize the transaction as a lease, but it is in reality a sale for federal income tax purposes, the lessee is the owner of the property. Assuming that the property is eligible for the credit, the lessee may thereby claim any available credit.


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