

DEPARTMENT OF TAXATION

Amendment to Chapter 18-235
Hawaii Administrative Rules

August 12, 1997

SUMMARY

1. §18-235-7-03(c) is amended.

§18-235-7-03 **Exclusion of pension income.** ***

(c) As used in this section:

"By reason of retirement, disability, or death" describes benefits paid because of retirement, including attainment of age 70-1/2 (to comply with section 401(a)(9)(C), IRC, with respect to required beginning date); disability as defined in section 72(m)(7) (with respect to meaning of "disabled"), IRC; or death. A benefit payment is not made by reason of retirement, disability, or death if it is actually or constructively received prior to retirement, disability, or death, even though the benefit payment is the same as the amount of benefits which would have been enjoyed upon retirement. A payment made by reason of retirement, disability, or death does not include:

- (1) An amount paid because of separation from service before retirement;
- (2) An employer contribution to a non-qualified pension plan that is deemed to be received by the employee upon vesting before retirement under Treas. Reg. §1.402(b)-1(b) (with respect to taxability of employee when rights under nonexempt trust change from nonvested to vested); or
- (3) An early distribution subject to federal penalty tax under section 72(t) (with respect to 10 per cent additional tax on early distributions from qualified retirement plans), IRC.

"Employer contribution" means the aggregate amount of contributions that are either made by the employer, or made for the employer by members of a group of affiliated corporations as provided by section 404(a)(3)(B) (with respect to profit sharing plan of affiliated group), IRC. These amounts are included in the employer contribution even though section 72(f) (with respect to special rules for computing employees' contributions) or 101(b) (with respect to employees' death benefits), IRC, may provide that the amounts are considered employee contributions for some purposes. The employer contribution does not include any amounts included in pretax employee contribution or previously

taxed contribution. Employer contribution does not include any amounts contributed by a plan beneficiary under an elective right; provided that an amount otherwise qualifying as an employer contribution shall not be disqualified as to a particular beneficiary solely because (1) the beneficiary determined the contribution amount in his or her capacity as an officer, partner, member, or sole proprietor, or (2) the beneficiary is allowed or is allocated all or a portion of the deduction allowable under section 162 or 404, IRC, attributable to the contribution.

"Exclusion ratio" means the ratio described in subsection (e)(1).

"Pension." A pension:

- (1) Provides an employee with compensation for past services, generally measured by such factors as years of employees' service and compensation received;
- (2) May be in the form of a (A) periodic or systematic payment of benefits to the employee over a period of years (e.g., usually for life after retirement), or (B) lump sum in lieu of periodic or systematic payments;
- (3) Is to be received by the employee by reason of retirement, disability, or death;
- (4) Is attributable to employer contribution;
- (5) Includes a stock bonus, pension, profit sharing, or annuity plan, as those terms are defined in sections 401 (with respect to qualified pension, profit sharing, and stock bonus plans) and 403 (with respect to taxation of employee annuities), IRC;
- (6) Need not be qualified within the meaning of section 401, IRC; and
- (7) May be paid to the employee, the employee's spouse upon retirement or disability, or a deceased employee's beneficiary.

"Pretax employee contribution" means the aggregate amount of voluntary contributions made by the employee under any elective right, such as contributions to: (1) individual retirement accounts to which an employer

does not contribute (see subsection (d)(2) for rollover individual retirement accounts); (2) IRC section 401(k) plans (with respect to cash or deferred arrangements); (3) IRC section 408(k)(6) plans (with respect to elective salary reduction contributions to simplified employee pension arrangements); or (4) IRC section 457 plans (with respect to deferred compensation plans of state and local governments and tax exempt organizations); but it does not include previously taxed contribution. These amounts are included in the pretax employee contribution even though the IRC may provide that the amounts are considered employer contributions for some purposes.

"Previously taxed contribution" means the aggregate amount of contributions that:

- (1) Were included in the employee's gross income under the Hawaii Income Tax Law, whether or not Hawaii income tax was actually due or paid; or
- (2) Would not have been includable in gross income under the Hawaii Income Tax Law applicable at the time of contribution if the employee were a Hawaii resident and the contributions were paid directly to the employee at the time.

Previously taxed contribution includes amounts included in the gross income of an employee under section 402(b) (with respect to taxability of beneficiary of nonexempt trust) or 403(c) (with respect to taxability of beneficiary under nonqualified annuities or under annuities purchased by exempt organizations), IRC.

[Eff 2/16/82; am and ren §18-235-7-03 12/8/94; am 1/1/98] (Auth: HRS §§231-3(9), 235-118) (Imp: HRS §235-7)

DEPARTMENT OF TAXATION

The amendment to chapter 18-235, Hawaii Administrative Rules, on the Summary page dated August 12, 1997, was adopted on August 12, 1997, following public hearings held on July 29, 1997 and August 12, 1997, after public notice was published in The Honolulu Advertiser, the Honolulu Star-Bulletin, The Garden Island, The Maui News, and the Hawaii Tribune-Herald on June 27, 1997.

This amendment shall take effect on January 1, 1998.

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Director of Taxation

APPROVED:

Benjamin J. Cayetano
Governor
State of Hawaii

Date: _____

APPROVED AS TO FORM:

Deputy Attorney General

Filed