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DEPARTMENT OF TAXATION ANNOUNCEMENT NO. 2007-20

RE: Extensions of Time to File Income Tax Returns.

The Department has amended section 18-235-98, Hawaii Administrative Rules ("HAR"), with the amendments effective as of October 6, 2007. The amended rules apply to any income tax return required to be filed on or after October 6, 2007[1], without regard to any extensions. The version of section 18-235-98, HAR in effect prior to October 6, 2007 applies to any income tax returns required to be filed before October 6, 2007, without regard to any extensions. For more information regarding the rules in effect prior to October 6, 2007, please refer to Department of Taxation Announcement No. 2007-18.

In other words, if an individual's taxable year ends on December 31, 2006, the income tax return would become due on April 20, 2007, without regard to any extension; and therefore, the previous extension rules apply to that income tax return. If a taxpayer's taxable year ends on June 30, 2007, its income tax returns would be subject to the amended rules, effective as of October 6, 2007, because the income tax would first become due on October 20, 2007.

The amended rules provide for automatically granted six-month extensions of time to file income tax returns if certain conditions are met.

REQUIREMENTS FOR INDIVIDUAL TAXPAYERS

Individuals are automatically granted a six-month extension without the need to file anything with the Department unless an additional tax payment must be made on or before April 20. As long as the following conditions are met, an individual taxpayer is deemed to have made an application for the six-month extension to file income tax returns on the prescribed due date:

1. On or before April 20th, 100% of the properly estimated tax liability is paid (see discussion below);
2. The tax return is filed on or before the expiration of the six-month extension period;
3. The tax return is accompanied by full payment of any tax not already paid; and

[1] In general, income tax returns are due on or before the 20th day of the fourth month following the close of the taxable year unless the 20th day falls on a weekend or legal holiday, in which case the due date is the next business day following the 20th day. See § 235-97(b), HRS;§ 231-21, HRS. For purposes of this announcement, it is assumed that the 20th day does not fall on a weekend or legal holiday.

4. The taxpayer is not bound by a court order to file a tax return on or before the prescribed due date.

If the individual must make an additional payment of tax on or before April 20 in order to meet the condition requiring payment of 100% of the properly estimated tax liability, the individual must attach Form N-101A to the payment.

REMINDER: An extension of time to file an income tax return is not an extension of time to pay the income tax liability. Interest will accrue on any tax liability not paid on or before April 20.

WARNING: Failure to meet any of the conditions will result in the extension being deemed invalid and penalties and interest shall be assessed on the amount of tax owed as if no extension had been granted. In that case, penalties and interest will be imposed from April 20.

REQUIREMENTS FOR PARTNERSHIPS, ESTATES, TRUSTS, OR REMICs

Partnerships, estates, trusts, or real estate mortgage investment conduits are granted a six-month extension if the following conditions are met:

1. An application for automatic extension (Form N-100) is filed on or before the due date prescribed by statute for filing the return, showing the full amount of properly estimated tax liability;
2. On or before the 20th day of the fourth month following the close of the taxable year, 100% of the properly estimated tax liability, if any, is paid (see discussion below);
3. The tax return is filed on or before the expiration of the six-month extension period;
4. The tax return is accompanied by full payment of any tax not already paid; and
5. The taxpayer is not bound by a court order to file a tax return on or before the prescribed due date.

REMINDER: An extension of time to file an income tax return is not an extension of time to pay the income tax liability. Interest will accrue on any tax liability not paid on or before the 20th day of the fourth month following the end of the taxable year.

WARNING: Failure to meet any of the conditions will result in the extension being deemed invalid and penalties and interest shall be assessed on the amount of tax owed as if no extension had been granted. In that case, penalties and interest will be imposed from April 20 or the original due date for a fiscal year filer.

REQUIREMENTS FOR CORPORATIONS

Corporations are granted a six-month extension if the following conditions are met:

1. An application for automatic extension (Form N-301) is filed on or before the due date prescribed by statute for filing the return;
2. On or before the 20th day of the fourth month following the close of the taxable year, 100% of the properly estimated tax liability is paid (see discussion below);

3. The tax return is filed on or before the expiration of the six-month extension period;
4. The tax return is accompanied by full payment of any tax not already paid; and
5. The taxpayer is not bound by a court order to file a tax return on or before the prescribed due date.

REMINDER: An extension of time to file an income tax return is not an extension of time to pay your income tax liability. Interest will accrue on any tax liability not paid on or before the 20th day of the fourth month following the end of the taxable year.

WARNING: Failure to meet any of the conditions will result in the extension being deemed invalid and penalties and interest shall be assessed on the amount of tax owed as if no extension had been granted. In that case, penalties and interest will be imposed from April 20 or the original due date for a fiscal year filer.

NO SIGNATURES REQUIRED ON APPLICATIONS FOR EXTENSIONS

No signature is required on any application filed by a taxpayer requesting an automatic six-month extension of time to file income tax returns. The forms will be revised in the future to reflect this change.

USE OF CURRENT FORMS AFTER THE EFFECTIVE DATE

Of the forms currently used to request extensions (Forms N-100, N-100A, N-101A, N-101B, and N-301), only Forms N-100, N-101A, or N-301 should be used to request a six-month extension for taxable years ending on or after June 30, 2007, even though these forms may indicate an extension period of less than six months.

PROPERLY ESTIMATED TAX LIABILITY CONDITION

All taxpayers must meet the condition of paying 100% of their properly estimated tax liability by April 20 or, if the taxpayer is a fiscal year filer, the 20th day of the fourth month following the end of the taxable year.

Properly estimated tax liability means the taxpayer made a bona fide and reasonable attempt at the time the extension was submitted to locate and gather all of the necessary information to make a proper estimate of tax liability for the taxable year. Individuals not filing Form N-101A are deemed to have submitted the extension on April 20 for purpose of this condition.

Whether a taxpayer has properly estimated the tax liability depends upon the facts and circumstances present in each individual case. The Department understands that the need for an extension may arise from a taxpayer having to wait for other entities to account for the taxable year, for example, partners waiting for a partnership to issue a K-1. Nevertheless, the rules require the taxpayer to make an honest and reasonable attempt to gather all information necessary to estimate its tax liability and to pay that estimated tax liability by the original due date of the return.

In order to give taxpayers some certainty regarding this condition, the taxpayer will be presumed to have met the condition if the amount paid by the original due date is 90% or more of the amount of tax as shown on the tax return.

If the amount paid by the original due date is less than 90% of the amount of tax as shown on the tax return, the taxpayer will have the burden of proving that the taxes paid on or before the original due date were based upon a proper estimate of income tax liability. In such cases, a taxpayer may submit a statement signed under penalty of perjury with its tax return explaining how the payment of tax on or before the original due date was based upon a proper estimate of tax liability. This statement should be a cover letter attached to the first page of the return.

For ease of administration, the department may automatically assess penalties and interest in circumstances where less than 90% of the taxes shown on the tax return were paid on or before the original due date. If a taxpayer receives a notice assessing penalties and interest for this reason and the taxpayer believes that a proper estimate of tax liability was made, the taxpayer should submit a statement signed under penalty of perjury explaining how the payment of tax on or before the original due date was based upon a proper estimate of tax liability. If a taxpayer demonstrates that the amount paid by the original due date constituted 100% of the properly estimated tax liability as of the original due date, the penalties and any interest associated with the penalties will be reversed.

CONFORMITY TO THE FEDERAL FILING EXTENSION RULES

To the extent possible, the Hawaii rules conform to the federal rules that provide extensions of time to file income tax returns. Minor formal differences still exist due largely to the difference in penalty provisions.

Unlike the Hawaii extension rules, the federal rules do not explicitly condition the grant of an extension to file upon the payment of the properly estimated tax liability (except in the case of corporations). However, federal law still requires full payment of tax by the original due date, unless a separate extension of time to pay tax is granted.

The reason that the Hawaii rules must condition the grant of an extension upon the payment of properly estimated tax liability is because the Hawaii Revised Statutes do not contain a failure to pay penalty substantially similar to the federal income tax penalty. If a taxpayer fails to make a full payment of federal income tax by the original due date, the federal taxpayer is assessed a penalty unless the taxpayer can demonstrate that the failure to pay was due to reasonable cause and not willful neglect. For purposes of federal income tax, reasonable cause is presumed, for the period of an extension of time to file, if (i) the excess of the amount of tax shown on the individual income tax return over the amount of tax paid on or before the regular due date of the return is no greater than 10 percent of the amount of the tax shown on the individual income tax return and (ii) any balance due shown on the individual income tax return is remitted with the return. Although the path is different, the outcome is the same for Hawaii income tax purposes. If an individual Hawaii taxpayer meets the same two conditions in relation to its Hawaii income tax liability, then the individual Hawaii taxpayer will not be subject to a penalty.

Another minor difference from the federal income tax extension rules is that Hawaii individual taxpayers are not required to file an application in order to request an extension of time to file a Hawaii income tax return, but all other taxpayers must file an application to request an extension. For federal income tax purposes, all taxpayers, including individuals, must file an application to request an extension.

In conformity with the federal rules that provide extensions of time to file income tax returns, applications for an extension of time to file a Hawaii income tax return no longer require a signature.

ADDITIONAL INFORMATION

For more information, please contact the Rules Office at 808-587-1577.

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