

LINDA LINGLE
GOVERNOR

JAMES R. AIONA, JR.
LT. GOVERNOR



KURT KAWAFUCHI
DIRECTOR OF TAXATION

SANDRA L. YAHIRO
DEPUTY DIRECTOR

STATE OF HAWAII
DEPARTMENT OF TAXATION
P.O. BOX 259
HONOLULU, HAWAII 96809

PHONE NO: (808) 587-1510
FAX NO: (808) 587-1560

LATE

SENATE COMMITTEE ON EDUCATION

TESTIMONY REGARDING SB 2251 RELATING TO TAXATION

TESTIFIER: KURT KAWAFUCHI, DIRECTOR OF TAXATION (OR DESIGNEE)
DATE: JANUARY 28, 2008
TIME: 1:15PM
ROOM: 225

This bill proposes a deduction from gross income for contributions made to Hawaii's "TuitionEDGE" 529 College Savings Plan.

The Department of Taxation (Department) **strongly supports** this measure; however **prefers the approach taken in the Administration measure, SB 3000.**

I. HAWAII'S 529 PLAN, GENERALLY

Section 529 of the Internal Revenue Code allows states to sponsor programs that allow contributions to qualifying educational accounts that grow tax-free for purposes of financing certain qualifying education costs. Hawaii's 529 college savings plan is vested in Chapter 256, Hawaii Revised Statutes, and is overseen by the Department of Budget & Finance. With the high costs of post-secondary education, it is important that investment vehicles with tax benefits be provided for those saving for college.

II. DEDUCTIONS ARE IMPORTANT TO ENCOURAGE INVESTMENT

To ensure Hawaii taxpayers take advantage of Hawaii's TuitionEDGE 529 program, it is important that tax incentives are available to taxpayers. The benefits of tax incentives are twofold:

- (1) Additional investment is attracted to Hawaii's plan, which commensurately lowers the cost of administering the fund for the fund participants; and
- (2) Additional investment is encouraged from taxpayers so that additional revenue will be saved for the plan beneficiaries, which will help lower the financial burden of college tuition and other costs.

This bill, as well as the Administration measure, seeks to provide meaningful tax incentives

for individuals to participate in Hawaii's TuitionEDGE 529 program.

III. OTHER JURISDICTIONS ALLOW INCENTIVES

Many other states offer similar tax incentives for contributions to their respective 529 college savings plans. Incentives include both deductions and a credit.

IV. TECHNICAL COMMENTS ON THIS MEASURE

THE DEPARTMENT PREFERS SB 3000—The Department prefers the approach taken in SB 3000 because it allows for a higher deduction, as well as provides a greater deduction for those filing as heads of household or surviving spouse. The instant measure does not contain specific provisions for persons filing in the latter categories.

The deductions allowed should include:

- A taxpayer filing a single return
- Married individuals filing separate returns; and
- Married individuals filing joint returns; heads of household; or those with a surviving spouse designation.

RECAPTURE PROVISION—The Department suggests that a recapture provision be included in this measure, which would require any deducted amount of income to be included in income in a subsequent year if the plan is rolled-over into a non-Hawaii plan.

PROHIBITED DEPOSITS—The Committee may also want to consider adding provisions that specify any "circular" use of account funds will be precluded from qualifying for the deduction. For example, if an account holder withdraws funds from the account and uses those funds to "re-deposit" funds in the account, no deduction should be allowed for the "re-deposit."

In sum, this bill provides targeted tax incentives to those trying to effectively save for the financial burdens of a college education. Hawaii should capitalize on these investment vehicles by providing incentives for its taxpayers to assure that every person can effectively save for education.

This bill will result in a revenue loss of approximately \$1.4 million per year.

The Department strongly recommends the Committee pass this measure.