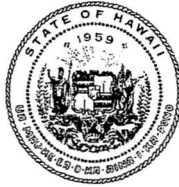


LINDA LINGLE
GOVERNOR

JAMES R. AIONA, JR.
LT. GOVERNOR



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

PHONE NO: (808) 587-1540
FAX NO: (808) 587-1560

KURT KAWAFUCHI
DIRECTOR OF TAXATION

SANDRA L. YAHIRO
DEPUTY DIRECTOR

HOUSE COMMITTEE ON FINANCE

TESTIMONY REGARDING HB 35 RELATING TO INCOME TAX CREDIT

TESTIFIER: KURT KAWAFUCHI, DIRECTOR OF TAXATION (OR DESIGNEE)

DATE: FEBRUARY 26, 2009

TIME: 10:00AM

ROOM: 308

This bill proposes a one-time tax credit required by the Hawaii constitution when general fund excess revenues meet certain thresholds.

The Department of Taxation (Department) **supports the intent** of this measure; however has **concerns regarding its revenue impact**.

CONSTITUTIONALLY REQUIRED—The Hawaii Constitution requires the Legislature to provide a tax credit or tax refund when the state general fund balance at the close of each of two successive fiscal years exceeds 5% of the general fund revenues for each of two fiscal years. The Department understands that these conditions have been satisfied because of the surplus in general fund revenues realized these past two fiscal years.

The Department supports the concept of this legislation, which is to return to taxpayers, the excess revenues realized by the State for the past two fiscal years. The purpose of the constitutional requirement to return excess revenues is essentially to ensure that state government does not become a profit center. Government should not be in the business of profiting from taxpayers. Taxes laid and collected should only be sufficient to cover government operating costs.

SUPPORT FOR MUCH LARGER AMOUNTS IN YEARS PAST—In prior years, the Department would have much preferred a larger constitutional refund when there were budget surpluses. During this legislative session, there is a major budget shortfall that the Legislature and Administration must work together to patch. The amount of the constitutional credit this session must reflect the state's serious fiscal forecast.

REVENUE IMPACT—The revenue impact of this measure is indeterminate. For the Committee's information, based on the 2006 individual tax returns filed by residents, a total of 1,056,297 exemptions qualify for the tax credit

TAXBILLSERVICE

126 Queen Street, Suite 304

TAX FOUNDATION OF HAWAII

Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: INCOME, Tax refund credit

BILL NUMBER: SB 1319; HB 35 (Identical)

INTRODUCED BY: SB by Hanabusa by request; HB 35 by M. Oshiro

BRIEF SUMMARY: Provides that each resident individual taxpayer may claim a general income tax credit in addition to any other credits allowed under HRS chapter 235. The tax credit shall be multiplied by the number of qualified exemptions claimed on the taxpayer's income tax return, but multiple exemptions for age or physical disabilities shall not be recognized. The credit shall be paid to each person who has been a resident of the state for at least nine months as defined in HRS section 235-1, whether or not such qualified resident was physically in the state for nine months. The credit shall be deductible from income tax liability for the 2009 tax year. Stipulates that this measure meets the constitutional provisions of Article VII, section 6, mandating the disposition of excess revenues. As introduced, the amount of the credit is blank.

EFFECTIVE DATE: Upon approval

STAFF COMMENTS: The "disposition of excess revenues" provision was adopted in tandem with the general fund expenditure ceiling in the belief that if the state adhered to the spending ceiling, Hawaii's generous tax system would produce substantial surplus revenues. Although the refund provision was not a part of the initial discussion of the ceiling, with the realization that revenues would far exceed the needs under the ceiling, the provision was added to insure the return of the funds rather than allowing bureaucrats to sit on these excess funds.

Under the constitutional provision, whenever the general fund balance at the end of a fiscal year exceeds 5% of the general fund revenues received in that year, for two consecutive years, the legislature at the next regular session following the second consecutive year of excess balances, must provide for a tax refund or credit. This has occurred and a return of excess revenues is necessary.

While the constitutionally mandated tax refund may be viewed as tax relief, it is actually a signal that the state's tax structure is generating more than what is needed to operate state government. It is a signal that, more than likely, the tax rates and structure are taking too much in tax dollars from the economy and that lawmakers need to address that issue. Although providing a tax refund at this time when forecasted revenues are falling and there are insufficient funds to underwrite the state's biennial budget seems incredible, it nonetheless underscores the lack of effort in the past to reduce the overall tax burden as surpluses ballooned in better times.

Had lawmakers made some downward adjustments in tax rates, they might not be faced with the current dilemma of having to find revenues in a slowing economy. Taxpayers might have been more forgiving of a temporary hike in taxes to help balance the state budget. But as many know, Hawaii has amongst the highest per capita tax burdens in the nation. Nearly every possible transaction, source of income, or type

of property has been tapped for a tax or a fee. This is because lawmakers have lost sight of what government should be and nothing else, that is insuring the health, safety and welfare of the community. Laws have been imposed that create additional costs for taxpayers, in particular, businesses in Hawaii such that the state's economy is on the verge of being destroyed.

Faced with the widening budget shortfall, lawmakers will, no doubt, attempt to raise taxes even while they provide for this constitutionally mandated tax refund credit. Raising taxes will certainly drive the proverbial stake into the heart of the state's economy in this economic downturn. Businesses will be forced out of business, taking with them the jobs that Hawaii's people need. While the national economy will recover, eventually, the same may not be true for Hawaii. If, in fact, lawmakers resort to raising taxes in this down economy, recovery will be a lot longer in coming for the state, if ever. Should the economy recover and Hawaii is somehow blessed with another period of prosperity, generating large surpluses, hopefully lawmakers of that future time will take heed should the constitutionally mandated refund be triggered and actually do something about lowering the burden of taxes.

Digested 2/24/09