SB 1197

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

SENATE COMMITTEE ON WAYS & MEANS
TESTIMONY REGARDING SB 1197
RELATING TO THE ECONOMY

TESTIFIER: KURT KAWAFUCHI, DIRECTOR OF TAXATION (OR DESIGNEE)
DATE: FEBRUARY 5, 2009
TIME: 9:30AM
ROOM: 211

This measure requires the Department of Taxation to provide a biennial report on tax expenditures to the Legislature, with an analysis of costs, effectiveness, among other information.

The Department of Taxation (Department) **provides comments** on this measure.

CURRENT REPORTS—The Department is presently obligated to provide reports on Hawaii income patterns of individuals and other entities, as well as provide tax credit reports. Though there is no prescribed deadline for these reports, the Department is diligent about producing and making these reports available as soon as practicable.

SUPPORT FOR GOOD DATA GENERALLY—The Department agrees with the spirit of this measure, which is to provide effective and usable tax data. The Department's Tax Research & Planning office is dedicated to studying the effects of tax laws, their changes, and their effects on the economy.

INFORMATION MAY NOT BE AS CURRENT AS THE LEGISLATURE WOULD LIKE—The Department points out that tax data and information is substantially lagged due to filing deadlines of April and October of the year following the tax year at issue. This means that the Department's data on tax credits can be several years old.

SOME INFORMATION WILL BE DIFFICULT TO DERIVE—The Department also points out inherent flaws with obtaining certain tax data, especially for exemptions, deductions, and exclusions. Because of the efficiencies needed for a brief tax return, certain exemptions, deductions, and exclusions are aggregated on a single line. They are not broken down into specifics. If each exemption, exclusion, or deduction were needed to be reported, the tax return could be extremely long and cumbersome. Also, certain exemptions are not even reported on a return because they are "exempt" from tax. Form and computer changes, which could be very expensive, would be needed to capture the required data.

NEED FOR RESOURCES—The Department also points out that this legislation would capitalize the existing resources of the Department. Moreover, this legislation may negatively impact other departmental research and planning priorities. If this bill becomes law, the Department respectfully requests additional resources in order to assure compliance with its provisions.

L E G I S L A T I V E

TAXBILLSERVICE

126 Queen Street, Suite 304 TAX FOUNDATION OF HAWAII Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: ADMINISTRATION, Annual report on tax expenditures

BILL NUMBER: SB 1197

INTRODUCED BY: Fukunaga

BRIEF SUMMARY: Adds a new section to HRS chapter 231 to require the department of taxation to submit an annual report to the legislature on or before September 15 in each odd-numbered year, on all tax expenditures currently in effect in the state. Defines "tax expenditure" as a credit, deduction, exclusion, exemption, or any other tax benefit provided under state law.

The annual report shall contain: (1) a detailed description of each tax expenditure; (2) the statutory authority for each tax expenditure; (3) the purpose and original intent of each tax expenditure; (4) the actual revenue loss for the most recent fiscal year for each tax expenditure, or an estimate if the actual amount cannot be determined; and (5) whether each tax expenditure has successfully achieved the intended purpose for which the tax expenditure was enacted and currently serves.

Requires any legislation establishing new or expanded tax expenditures or extending the sunset date for an existing tax expenditure shall include: (1) a sunset provision; (2) a requirement for an evaluation or study that may also include requirements for the submission of information by taxpayers benefitting from a tax expenditure; (3) recapture provisions if a taxpayer fails to meet any requirements that are necessary to qualify for the new tax benefit; and (4) measurable goals or objectives.

EFFECTIVE DATE: July 1, 2009

STAFF COMMENTS: The proposed measure would require the department of taxation to provide a comprehensive tax expenditure report detailing any tax benefit provided by the state. While this would entail a detailed description of each "tax expenditure" along with its economic performance, with the numerous credits, deductions, exclusions, etc., it is questionable whether the department of taxation has the resources and staff to undertake such a project.

A similar measure was introduced last year to require the department of taxation to conduct an evaluation of the high tech business tax credits. In their examination of the high technology business investment tax credit, the most recent Tax Review Commission reiterated the findings of the previous Tax Review Commission that stated that, "A tax incentive program is a potential 'black hole' because it is a future benefit of unknown proportions, which is determined by the favored taxpayer's interpretation of what the tax credit should be, and is claimed on a tax return which is confidential."

The most recent Tax Review Commission brought in outside consultants to assess the costs and benefits of the high technology tax credits, but the results were not definitive because they could not obtain current data on the cost of the credit or on the operations of the qualified high tech businesses. They also found data to be incomplete due to confusion about filing requirements when the certification for the credits were changed. In its final recommendations with respect to the high technology tax credit and tax credits in general, the Commission recommended increased transparency and timely disclosure and suggested that a confidentiality waiver should be required of those taxpayers claiming tax credits so that pertinent data can be released to the public and that all beneficiaries of tax credits be required to file truth-in-disclosure reports in addition to income tax returns. If an analysis of all tax expenditures is to be conducted, first the legislature should consider the recommendation of the Commission to require a waiver of confidentiality so that successes or failures of individual taxpayers can be tracked and evaluated. The legislature has already adopted a similar waiver of confidentiality when it required American Hawaii Cruises to open its books by Act 228, SLH 1991, in order to secure its exemption from the public service company tax.

Given that these tax credits, tax exclusions, and tax exemptions are a back door expenditure of public dollars, the granting of these preferences should be subjected to the same scrutiny that appropriation and expenditure of tax dollars are subjected to under the rubric of the procurement code. How can policymakers justify the establishment of such tax incentives when there is no means by which to measure whether or not the promise of jobs, economic stimulation, or growth in the industry has resulted if this information is not available?

Conversely, if these beneficiaries want to feed on public dollars through these tax incentives, then they should be more than willing to reveal how those dollars were used and how those dollars benefitted the taxpaying public. The analogy is something akin to having to put the quarter in the juke box if one wants to dance. Although it will take resources, at the very least, the tax department should begin to collect this data as these preferences have a substantial impact on the revenue base and tax collections. During the late 1970's when money was also tight, the department of budget and finance used to publish a listing of all exemptions but placed no dollar figure on each as they were not in the position to collect that information. The department of taxation, on the other hand, already does collect some data about tax credits and publishes that information. However, with the help of technology, the department should be able to collect data such as exemptions from the general excise tax as that is specific information that the claimant must file on his or her return. Exclusions may be a bit more difficult to capture as that is not a number that may be required to be listed as it is an exclusion of a certain type of income, such as pensions. However, that data probably could be collected from federal data for Hawaii.

Digested 2/4/09

HAWAII GOVERNMENT EMPLOYEES ASSOCIATION
AFSCME Local 152, AFL-CIO

AFSCME
LOCAL 152, AFL-CIO

RANDY PERREIRA
Executive Director
Tel: 808.543.0011
Fax: 808.528.0922

NORA A. NOMURA
Deputy Executive Director
Tel: 808.543.0003
Fax: 808.528.0922

DEREK M. MIZUNO
Deputy Executive Director
Tel: 808.543.0055
Fax: 808.523.6879

The Twenty-Fifth Legislature, State of Hawaii
Hawaii State Senate
Committee on Ways and Means

Testimony by
Hawaii Government Employees Association
February 5, 2009

S.B. 1197– RELATING TO THE ECONOMY

The Hawaii Government Employees Association supports the purpose and intent of S.B. 1197, which will require an evaluation of all tax expenditures (including credits and exemptions) provided by the State of Hawaii. The bill will enable the Legislature to make more fiscally sound and effective spending decisions because the Department of Taxation must report to the Legislature annually on all tax expenditures in effect.

As drafted, the bill will allow legislators to identify tax expenditures, credits and exemptions and determine whether these should be continued based upon their actual cost and benefit. In these difficult economic times, states need to ensure that tax expenditures are regularly evaluated and that ineffective or overly expensive tax breaks are repealed.

Thank you for the opportunity to testify in support of S.B. 1197.

Respectfully submitted,

Nora A. Nomura
Deputy Executive Director