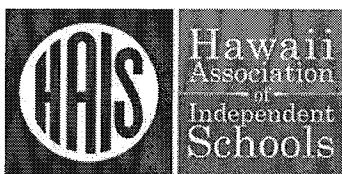


SB 1346



LATE

March 4, 2009
9:30 a.m.
Conference Room 211

TESTIMONY TO
THE SENATE COMMITTEE ON WAYS AND MEANS

RE: SB 1346 SD1 – Relating to Taxation

Chair Kim, Vice Chair Tsutsui, and Members of the Committee:

My name is Robert Witt and I am executive director of the Hawaii Association of Independent Schools (HAIS), which represents 97 private and independent schools in Hawaii and educates over 30,000 elementary and secondary students statewide.

The Association supports the intent of Senate Bill 1346, Senate Draft 1 – Relating to Taxation, which proposes an increase in the general excise tax to generate additional funding for early education and public schools in Hawaii.

While HAIS primarily advocates on behalf of Hawaii's independent schools, our board of directors places high priority on the active participation of the Association in the educational community for the benefit of all children, in all schools. To that end, we are regular contributors to the State's educational policy dialogue, collaborating with the Department of Education and other education-related organizations in both the public and private sectors to support early childhood education, public elementary and secondary education, charter school education, and higher education.

We steadfastly believe that when investments are made in schools the returns are enormous, and that an increase in our state's overall investment in education – through means like those proposed by this measure, such as dedicated funding transmitted directly to public schools and complex areas from the State and tax credits for those who volunteer their services at public schools – will produce significant dividends for all of us in Hawaii, for many years to come.

Thank you for this opportunity to testify.

The beverage container deposit program has been very successful for several reasons. Most importantly it has increased the recycle rate substantially in our county. Before the program our recycling rate was around 20%. Since the program was initiated the rate has climbed to over 70%. Our records show that the number to people recycling has increased steadily over the last four years. We see this trend continuing into the future.

The HI5 program has also provided income to many families that helps put food on the table. The number of customers we have who not only bring their own containers but also collect from others is large. Many of these people collect from parks, bars and restaurants, social events, and the like. They are helping to keep our island clean and free of litter while supporting their families. Any disruption to the program would impact many more people than just those of us directly involved in the business of recycling.

SB 884 proposes actions that we feel will be very detrimental to the program. The current HI5 fee structure just barely provides for viable redemption center operations. Operators depend upon the handling fees to keep the doors open. The value of the commodities in recent months has dropped so low that income no longer covers processing and shipping cost. We expect this situation to improve later this year but now is not the time to rock the boat. SB 884 would rock the boat.

Our community can't afford to lose the redemption and recycling infrastructure that has developed over the last several years. Keeping Maui litter-free is too important.

Tom Reed

President

Aloha Recycling



HAWAII GOVERNMENT EMPLOYEES ASSOCIATION
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

LATE

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

Testimony by
Hawaii Government Employees Association
March 4, 2009

S.B. 1346, S.D. 1 – RELATING
TO TAXATION

The Hawaii Government Employees Association supports the overall purpose and intent of S.B. 1346, S.D. 1. The bill accomplishes several important objectives. First, it increases the 4% general excise tax by an unspecified amount and allocates a portion of the increase for public education. This would provide a sustained source of funding for public education. However, it also offsets the general excise tax increase by establishing general excise tax exemptions for food, various medical expenses and a portion of rental income, and increasing standard deductions for those in lower income tax brackets.

We are opposed to creating an Educational Funding Commission that would provide oversight for general excise tax revenues raised through the proposed legislation and to decide how the funds are allocated. This amounts to another layer of bureaucracy. Instead, the responsibility should rest with the Board of Education, assisted by the Department of Education. The BOE and DOE should be held accountable for the choices they make with this additional source of funds.

The current budgetary challenges can be addressed in part by raising the general excise tax rate while offsetting this increase by making the State's income tax more progressive and increasing certain tax credits for individuals/families. Careful consideration of budget choices, including tax expenditures, is also warranted.

Some tax increases will be needed to avoid the negative effects of deep budget cuts. While tax increases also reduce economic activity, they have a smaller impact on consumption because some of the money paid in taxes might otherwise have been saved rather than spent. Modest tax increases are less harmful to the economy than significant budget reductions.

The answer to solving our budget deficit is a package of thoughtful proposals contained in S.B. 1346, S.D. 1, which includes a combination of a tax increase with significant tax

Hawaii State Senate, Committee on Ways and Means
S.B. 1346, S.D. 1 – Relating to Taxation
March 4, 2009
Page 2

relief. Thank you for the opportunity to testify in support of S.B. 1346, S.D. 1 with these suggested amendments.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Nora A. Nomura", with a horizontal line extending to the right.

Nora A. Nomura
Deputy Executive Director

LATE

Department of Taxation

Position Summary

Senate Committee on Ways & Means/March 4, 2009

1346

Bill Number	Bill Title "Relating to..."	Position	Comments	Revenue Impact	Methodology
SB 1106 SD 1	TAXATION	Support Intent; Request Amendments Contained in SB 1230 SD 1	The Department suggests that the substance of the HARPTA amendments contained in SB 1230 SD 1 subsection (h) be adopted. The Department's provision requires the seller to obtain a tax clearance as to the specified tax matters.	Unknown revenue gains. This bill estimated a potential annual shortfall of \$1.3 million in withholding tax revenues by nonresident sellers of real property.	This bill estimated a potential annual shortfall of \$1.3 million in withholding tax revenues by nonresident sellers of real property. The requirement that nonresident sellers furnish a tax clearance to the bureau of conveyance will help eliminate that estimated shortfall from nonresident sellers of real property and may also increase other revenues due from TAT and GET. The Department will incur additional cost to process the tax clearance certificates for nonresident sellers.

SB 1346 SD 1

TAXATION

Opposed to any tax increases and cannot support unbudgeted revenue loss.

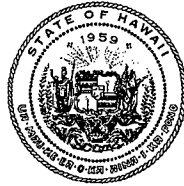
See written comments.

*Exempting food: Revenue loss \$135 million per year
*Exempting medical services, glasses and non-prescription drugs: revenue loss \$126 million per year.
*Exempting rental units the first blank dollars per month: indeterminate, amount is blank.
*Doubling the standard deduction: revenue loss \$37.5 million per year.
*Tax credit for school volunteer service: revenue loss indeterminate, blank amount in the bill.
*Increase in GET: revenue gain or loss depends on the increase (blank amount in the bill) and an indeterminate (blank) amount to be deposited into the new educational special fund.
* Special Fund: indeterminate for the newly created education special fund, the amount is blank in the bill.

Data sources include Hawaii Income Patterns: Business & Individuals; Consumer Expenditure Survey, DBEDT Survey of Visitor Expenditure.

LINDA LINGLE
GOVERNOR

JAMES R. AIONA, JR.
LT. GOVERNOR



KURT KAWAFUCHI
DIRECTOR OF TAXATION

SANDRA L. YAHIRO
DEPUTY DIRECTOR

LATE

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 1346 SD 1
RELATING TO TAXATION**

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

DATE: MARCH 4, 2009

TIME: 9:30AM

ROOM: 211

This measure seeks to increase the general excise tax (GET), as well as provide various GET exemptions, increase the standard deduction, among other things.

The Senate Committee on Education & Housing amended the measure by eliminating the Earned Income Tax Credit and defecting its effective date.

The Department of Taxation (Department) **opposes the tax increase** and cannot support the other components at this time due to the fiscal implications. The Department provides the following comments—

I. GET INCREASE

A. *General Comments*

This measure seeks to increase the GET by an unspecified amount. The GET is the broadest of state taxes applying to all gross income or gross proceeds of a business, unless exempt. The GET collections also constitute over 50% of the general fund revenues. The GET is an effective tax because of its broad base and low rate. It is capable of having such a low rate purely as a result of the breadth of its tax. To modify the tax base or to increase its rate could dramatically impact the tax policy and collection that the State has relied upon for decades.

The Department opposes the GET increase at this time. At a time when the State's economy is struggling greatly, the Department cannot support a 25% tax increase on the daily costs incurred by Hawaii families, assuming a 1 percent increase. Though the increase in GET is laudably offset by various exemptions and credits, the Department is unsure that such offsets will markedly reduce such a regressive tax increase.

In short, the Department cannot support a tax increase such as this when the economy cannot handle such an increase and Hawaii will become a less attractive and more regressive state to live and conduct business.

B. Revenue Estimate

The GET tax increase proposed in this measure will result in an indeterminate revenue gain due to its blank amount.

II. GET INCREASE FOR DEPOSIT TO THE BENEFIT OF SCHOOLS

Though the Department appreciates the intent of providing additional funding for schools, the Department believes that the current Department of Education budget is sufficient.

Moreover, during a time when the budget and the general fund are at their most delicate point this session, the Department cannot support a tax increase to fund a special fund. Any discussion of increasing tax revenues this session must be deposited to the benefit of the general fund in order to balance the budget this session.

III. CREDIT FOR VOLUNTARY SERVICES

A. General Comments

The measure provides an unspecified credit for volunteer services performed for public schools by a resident. In addition, it excludes from the credit volunteer services that are performed by a person who is also a paid employee of the school.

The Department is concerned with the definition of "volunteer services," which could leave the determination up to the individual taxpayer and be subject to varying interpretations. The Department would also have to expend substantial resources to insure that only qualified individuals obtain the credit and would need to inquire of the schools whether the individual did in fact volunteer some services and that the services provided were material. In order to alleviate some of the burden on the Department, the Department suggests that the taxpayer should be required to obtain a certification from schools stating the taxpayer did provide volunteer services of the type that is being encouraged by this legislation.

This measure could also open the door to fraud and collusion by a school employee and other individuals whereby the employee could verify that services were performed when in fact none were in order for the individuals to obtain the credit.

The Department also notes that the amount of the credit received by an individual would be subject to state and federal income tax.

B. Revenue Impact

This credit will result in an indeterminate revenue loss because the credit amount is blank.

IV. EXEMPTION FOR FOOD, OVER-THE-COUNTER DRUGS, AND MEDICAL SERVICES FROM GET

A. General Comments

The Department generally supports tax relief in the form of a general excise tax exemption on certain foods and nonprescription drugs, as well as medical services; however, such relief cannot be afforded at this time.

The Department generally supports measures that assist struggling families and individuals by decreasing their state tax burdens. This bill specifically targets the overly regressive nature of the GET, which applies at the same rate to all taxpayers, regardless of their income level, to all staples of life. This exemption mitigates the regressive effects of the GET imposed on food and over-the-counter medications that is passed on to consumers. By eliminating the GET on these items, lower income families will have more to spend on the necessities of life.

The measure fails to adequately define "food item" or "over-the-counter medicine." "Food item" is defined as "any food or food product for home consumption except alcoholic beverages, tobacco, and food products prepared at the place of sale or at another location and sold primarily for immediate or nearly immediate consumption. In the case of those persons who are sixty-five years of age or older or who receive supplemental security income benefits under Title XVI of the Social Security Act (42 U.S.C. §1381 et. seq.), and their spouses, "food items" includes meals prepared by and served in senior citizens' centers, apartment buildings occupied primarily by senior citizens, private nonprofit establishments (eating or otherwise) that feed senior citizens, private establishments that contract with the appropriate agency of the State to offer meals for senior citizens at concessional prices, and meals prepared for and served to residents of federally subsidized housing for the elderly." This definition leaves unanswered whether such things as candy or soft drinks (which in many jurisdictions is not deemed to be food exempt from sales tax) is or is not exempt from the GET. To truly comprehend whether certain food products are exempt, the analysis is typically over whether the items are fresh produce, milk or other fresh beverages, or contain flour in their ingredients.

Likewise, "over-the-counter nonprescription medicine" is defined as "drugs or medications that can be purchased without a prescription (for example, aspirin, cough syrup, and laxatives)". This leaves to speculation about whether various items are or are not subject to the exemption. For example, is common rubbing alcohol and other ointments, vitamins, and food supplements included as an over-the-counter nonprescription medicine? The Department foresees substantial unease by the retailing community because of the lack of guidance on what constitutes a food stuff or an over-the-counter nonprescription medicine, and the Department would be required to expend substantial resources to draft rules over the meaning of these phrases.

B. Revenue Impact

The exemptions discussed above result in the following revenue impacts—

- Exemption for food--\$135 million per year
- Exemption for medical services and nonprescription drugs--\$126 million per year

V. GET EXEMPTION ON RENT

A. General Comments

The Department recognizes the importance of providing assistance for low-income rental housing.

The Department has concerns over the GET exemption on rent. The GET is a tax on the business, or in this case the landlord. The Department is unsure that the economic benefit of exempting rent from the GET will necessarily calculate into lower rents. There is no requirement that a landlord has to charge lower rent simply because it will no longer be taxed.

B. Revenue Impact

The exemption for rental income is indeterminate because the amount is blank.

VI. INCREASING THE STANDARD DEDUCTION

A. General Comments

The Department generally supports tax relief in the form of increasing the standard deduction; however such relief cannot be afforded at this time.

Hawaii's personal income tax system consists of nine brackets with top rate of 8.25% kicking in at an income level of \$40,000 for individuals. Increasing the Hawaii standard deduction will provide timely and meaningful tax relief in the following substantial ways:

- 1). **FEWER LOW-INCOME TAXPAYERS WILL OWE TAX**—Currently, the very low-income citizens of Hawaii are paying state income tax, but not federal income tax. This disparity is exclusively due to the fact that Hawaii's standard deduction is markedly lower than the federal, thus requiring the poor to file. By raising the standard deduction, a large percentage of the very low-income will have immediate tax relief because they won't owe any Hawaii taxes.
- 2). **LESS ITEMIZED DEDUCTIONS**—By increasing the standard deduction, more filers will be able to take the standard deduction, rather than itemize. The larger standard deduction will increase collections, lower fraud, and relieve the burden faced by the

Department in processing itemized schedules.

- 3). **REFLECTS THE REALITY OF HAWAII'S COST OF LIVING**—Under this proposal, Hawaii's tax system becomes more progressive and equitable by providing tax relief directly to the low-income taxpayers whom, as a group, almost always rely on the standard deduction to deal with the high cost of living. This proposal will keep more money in the pockets of Hawaii citizens who need tax relief the most, rather than waiting for a tax refund.

Increasing Hawaii's standard deduction is also better tax policy when compared to the alternative of providing an earned income tax credit because:

- 1) Raising the standard deduction wholly eliminates low-income taxpayers from any income tax assessments;
- 2) There is a substantial amount of fraud that accompanies the earned income tax credit that the State could avoid;
- 3) Raising the standard deduction helps far more taxpayers;
- 4) Tax professionals almost unanimously support the notion of increasing the standard deduction; and
- 5) The standard deduction is far easier than the earned income credit for taxpayers to understand.

B. Revenue Impact

Increasing the standard deduction will result in a revenue loss of \$37.5 million per year.

VII. METHODOLOGY

The Department's methodology for arriving at its revenue estimates was based upon data sources including Hawaii Income Patterns: Business & Individuals; Consumer Expenditure Survey, DBEDT Survey of Visitor Expenditure.