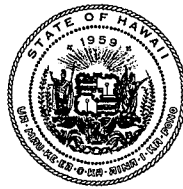


SB 337

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 337
RELATING TO CONFORMANCE OF STATE PERSONAL EXEMPTION TO
FEDERAL PERSONAL EXEMPTION**

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

This measure seeks to amend Hawaii income tax law to conform to the federal personal exemption.

The Department of Taxation (Department) **supports the tax relief** contemplated by this measure; provided that this can be funded from other sources.

SUPPORT FOR CONFORMITY—The Department strongly supports the conforming nature of this measure. Conforming to the Internal Revenue Code on amounts such as the personal exemption (as well as the standard deduction and rate brackets) is sound tax policy. However, the Department is concerned that the current draft of the bill does not accomplish the purpose of the bill. To conform to the federal personal exemption, section 235-2.3(b)(10) needs to be deleted.

EFFECTIVE TAX RELIEF—In general, the Department is supportive of legislation that helps ensure that the taxpayers are provided meaningful relief from Hawaii's high cost of living. The relief provided via the personal exemption is particularly important for low-income individuals who are in greatest need of every dollar possible. Increases to the personal exemption amounts are critical for all taxpayers as Hawaii's cost of living has grown over the past 20 years while Hawaii's personal exemption amount has not been amended since the 1985 taxable year. By increasing the personal exemption, more of the poor who are least able to pay tax will fall off the tax roles.

TIMELY TAX RELIEF—This measure is also timely tax relief given the fact that the state and nation are facing the largest economic slowing since the Great Depression.

CURRENT FEDERAL EXEMPTION RATE—The Department points out that the state's personal exemption will more than triple by conforming to the federal personal exemption, which is \$3,500 for 2008 and \$3,650 for 2009.

REVENUE IMPACT—This legislation will result in a revenue loss of \$116.7 million per year.

TAXBILLSERVICE

126 Queen Street, Suite 304

TAX FOUNDATION OF HAWAII

Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: INCOME, Adopt federal personal exemption

BILL NUMBER: SB 337

INTRODUCED BY: Slom and 1 Democrat

BRIEF SUMMARY: Amends HRS section 235-54(a) by repealing specified amounts for the personal exemption and conforms the state personal exemption amount to the federal personal exemption amount. Makes a conforming amendment to HRS section 235-2.45(a).

EFFECTIVE DATE: January 1, 2010; applicable to tax years beginning after December 31, 2009

STAFF COMMENTS: The state personal exemption stands at \$1,040. This measure would replace the state's personal exemption amounts with the federal personal exemption amounts. Currently the federal personal exemption amount is \$3,500 for 2008 and for 2009 - \$3,650. It should be noted that at the federal level those amounts are indexed for inflation and therefore rise each year as the cost of living increases. In addition, while the federal personal exemption looks very generous when compared to Hawaii's current personal exemption, it should be remembered that the federal marginal income tax rates are higher than state tax rates. By tying Hawaii's personal exemption to that of the federal level, lawmakers will surrender their oversight to federal policy makers. Should federal lawmakers decide to tinker with the personal exemption amounts, that decision will be made without local input.

Regardless, some sort of adjustment of the personal exemption is long overdue. When lawmakers were implored to adjust income tax rates in the 1998 session by the Economic Revitalization Task Force (ERTF), the focus was primarily on dropping the top tax rate to be competitive with other states in attracting new investment to the state thereby creating jobs for Hawaii's people. And while rates and brackets were adjusted across the board, nothing was done to eliminate many of the truly poor from having to pay state income taxes. The last time the personal exemption was increased was in 1984 effective for tax years beginning in 1985. Thus, it has been more than 20 years since the personal exemption has been adjusted.

Another alternative to increasing the personal exemption would be to increase the standard deduction thus raising the floor before which the state starts to impose its personal income tax. This would insure that those at the bottom end of the income spectrum earn a more substantial sum before they are asked to pay state income taxes.

Digested 2/3/09