
From: Tina Desuacido [tina500@juno.com]
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TRANSMISSION OF TESTIMONY

DATE: Wednesday, January 26, 2011
TO: House Committee on Economic Revitalization & Business
FROM: Tax Foundation of Hawaii

Total Pages 6

FOR: Rep. Angus McKelvey, Chair

Testifier: Lowell L. Kalapa, President - Tax Foundation of Hawaii

(Mr. Kalapa will not appear in person at the hearing.)

Date of Hearing - Thursday, January 27, 2011

Time of Hearing - 9:00 am

HB 801 - Relating to Taxation (2 pages)
HB 810 - Relating to Employment (2 pages)
HB 811 - Relating to Employment (2 pages)

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Thank you.

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126 Queen Street, Suite 304

TAX FOUNDATION OF HAWAII

Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: INCOME, Make work opportunity credit operative

BILL NUMBER: HB 801

INTRODUCED BY: Say

BRIEF SUMMARY: Adds a new section to HRS chapter 235 to make the work opportunity credit of the Internal Revenue Code (IRC) section 51 operative for Hawaii income tax purposes except that: (1) “qualified first year wages” for any year shall not exceed \$6,000; (2) the term “wages” shall not include any amount paid to or incurred by an individual who begins work for an employer before January 1, 2010 or after December 31, 2013; and (3) no credit shall be available for any wages paid or incurred before January 1, 2010, or after December 31, 2013.

Taxpayers may claim a work opportunity credit as provided by IRC sections 38 and 51 equal to 40% of the qualified first year wages paid or incurred by the taxpayer. The credit shall be deductible from the taxpayer's net income tax liability for the taxable year in which the credit is properly claimed.

If the work opportunity credit claimed by a taxpayer exceeds the amount of income tax payment due from the taxpayer, the excess of the credit over payment due may be carried over and claimed in subsequent tax years until exhausted; provided that any excess tax credit shall not be refundable.

Requires all claims for a credit including any carryover credit to be filed on or before the end of the twelfth month following the close of the taxable year for which the credit may be claimed. Failure to properly claim the credit shall constitute a waiver of the right to claim the credit.

The director of taxation may adopt rules that shall be exempt from the public notice requirements of chapter 91; except that the director shall hold at least one public hearing before rules adoption. The director shall also prepare forms necessary to carry out this section.

This section shall not apply to taxable years beginning after 12/31/013; provided that HRS section 235-2.3 shall be reenacted in the form in which it read on the day prior to the effective day of this act.

EFFECTIVE DATE: Tax years beginning after December 31, 2010

STAFF COMMENTS: This measure would make the federal work opportunity credit operable for Hawaii income tax purposes but: (1) limit the first year qualifying wages to \$6,000; and (2) provide that the program shall be operable for Hawaii income tax purposes for wages paid after January 1, 2010 but before December 31, 2013.

The work opportunity tax credit (WOTC) is a federal tax credit that encourages employers to hire workers from targeted groups - Temporary Assistance for Needy Families (TANF) recipients, veterans, ex-felons, Supplemental Security Income (SSI) recipients, high-risk youth, vocational rehabilitation

referrals, youth employment program participants and food stamp recipients. The tax credit is designed to help job seekers gain on-the-job experience, move toward economic self-sufficiency, and help reduce employers' federal tax liability. For most target groups, the WOTC can be as much as \$2,400 based on qualified wages paid to the new employee for the first-year of employment. Generally, qualified wages are capped at \$6,000. The credit is 25% of qualified first-year wages for those employed at least 120 hours and 40% for those employed 400 hours or more. For disabled veterans, the WOTC can be as much as \$4,800 with qualified wages capped at \$12,000. For long-term TANF recipients, the tax credit can be as much as \$9,000, with qualified wages capped at \$10,000 for a combined two-year period. For summer youth the WOTC can be as much as \$750 during the 90-day period of employment with wages capped at \$3,000. On the federal level to be eligible for the credit, a new hire must be employed after December 31, 2005 and before September 1, 2011.

While this measure proposes to adopt a WOTC for Hawaii income tax purposes, it should be remembered that Hawaii generally does not adopt any of the credits on the federal level, except for the low-income housing tax credit, as Hawaii's income tax rates are not as onerous as those on the federal level. It should be remembered that this proposal, like many others, reflects the lack of understanding of the many challenges employers face in their attempt to stay in business and make a profit. It should be noted that these proposed credits are worthless to any business that is not making a profit as any excess credits over tax liability will not be refunded to the employer. Thus, unless the business is profitable, there will be no profits to tax and there will be no tax liability against which to apply the proposed credits.

Instead of parroting federal tax incentives such as the WOTC, lawmakers should instead look at state laws which impose barriers or additional costs to the creation of jobs in the states. For example, in recent years lawmakers have attempted to suspend the capital goods excise tax credit which recognizes the imposition of the state's general excise tax on the purchase of capital goods, capital goods that are imperative to the creation of new jobs. As a result of these vacillations, lawmakers have created uncertainty about the investment in capital equipment and, therefore, place one more barrier in the way of economic recovery. If there is anything lawmakers can do to encourage the creation of jobs it is to restore certainty to the availability of the capital goods excise tax credit.

While there is no limitation of the amount of credit that may be claimed by all employers, this measure could potentially result in a drain of state resources. It is questionable whether the state can afford this credit given its current financial crisis. In the state that the economy is right now, it is commendable that many businesses are still around as compared to those that have shuttered their doors recently. Thus, while the intent of this measure is commendable, it falls far short of recognizing the challenges facing business in this economic environment. Rising costs of unemployment insurance, the possibility of an increase in the general excise tax, and increases in fees, as well a new maze of regulations with which to comply, merely increases the cost of doing business in Hawaii. Until these issues are addressed, no amount of tax incentives will improve the outlook for business and the jobs they create.