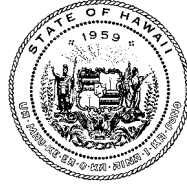


# SB2964

State Income Tax  
Deduction for Qualified  
Student Loan Interest; UH  
EDU, WAM

NEIL ABERCROMBIE  
GOVERNOR

BRIAN SCHATZ  
LT. GOVERNOR



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To: The Honorable Jill N. Tokuda, Chair,  
and members of the Senate Committee on Education

Date: Friday, February 10, 2012  
Time: 1:15 P.M.  
Place: Conference Room 225, State Capitol

From: Frederick D. Pablo, Director  
Department of Taxation

Re: S.B. No. 2964, Relating to Taxation

The Department of Taxation (Department) appreciates the intent of S. B. No. 2964, and offers the following information and comments for your consideration.

S.B. 2964 states that its intention is to create a deduction for qualified student loan interest paid on tuition expenses at the University of Hawaii system. However, as noted below, the bill as currently written also creates a deduction for student loan principal payments.

The Department notes that payments of student loan interest are already generally deductible under current law. Internal Revenue Code (IRC) section 221, incorporated into Hawaii Income Tax Law by HRS § 235-2.4, allows a deduction for interest paid on qualified education loans (the Student Loan Deduction).

However, the Student Loan Deduction contains a phase out provision, which limits the amount of the deduction for taxpayers with modified adjusted gross incomes (MAGI) above \$50,000 (\$100,000 in the case of joint filers), with taxpayers with modified MAGI above \$75,000 (\$150,000 for joint filers) being completely unable to take the deduction.

Thus, the effect of S.B. 2964 would be to create a deduction for student loan interest paid by taxpayers with MAGI above \$50,000 per year who paid tuition to the University of Hawaii, to the extent that those interest payments were not already deductible under IRC § 221.

In addition, S.B. 2964 defines "qualified student loan interest" to include "qualified education expenses," which could be broadly interpreted to allow for the deduction of principal, not just interest. If it is the Committee's intent to create a deduction for payments of student loan principal, in addition to student loan interest, the Department recommends the Committee amend the bill to clarify its intent in order to minimize any confusion.

The Department also recommends the following language be added to the definition of "qualified student loan interest": "...or an individual who was eligible to be claimed as the taxpayer's dependent for tax purposes when the loan was initiated..."

Thank you for the opportunity to provide comments.

# TAXBILLSERVICE

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SUBJECT: INCOME, Deduction for student loan interest

BILL NUMBER: SB 2964

INTRODUCED BY: Tsutsui, English, Tokuda and 7 Democrats

BRIEF SUMMARY: Adds a new section to HRS chapter 235 to allow a taxpayer to deduct from gross income, up to \$\_\_\_\_\_ in student loan interest, including required and voluntary interest payments on qualified education expenses. Defines “qualified education expenses” as tuition costs for a student who was enrolled in the University of Hawaii system at least half-time in a program leading to a degree, certificate, or other recognized educational credential.

Requires the director of taxation to prepare the necessary forms to claim the deduction, may require proof of the claim for the deduction, and adopt may rules pursuant to HRS chapter 91.

Defines “qualified student loan interest” for purposes of the measure.

EFFECTIVE DATE: Tax years beginning after December 31, 2011

STAFF COMMENTS: This measure proposes an income tax deduction of \$\_\_\_\_\_ for the amount of student loan interest paid on tuition expenses to the University of Hawaii system. This measure would grant a tax preference in the form of an income tax deduction for such student loan interest of a student who was enrolled at the UH. As such, it grants preferential tax treatment to a select group of taxpayers without regard to the taxpayer’s need for tax relief. Further, it is discriminatory in the sense that the deduction is limited only to UH students and does not even apply to students who attend another Hawaii institution of higher education let alone for students attending an out-of-state institution.

In addition, while the proposed tax deduction would only be applicable under the state income tax law and there is no similar deduction on the federal level, the adoption of this measure would be contrary to the state’s intent to conform to the federal law. It should be remembered that it has long been the intent of the state legislature to maintain conformity between Hawaii’s income tax law and the federal Code to insure that administration and compliance costs will be minimized.

Digested 2/9/12