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GOVERNOR

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DEPARTMENT OF TAXATION
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JOSHUA WISCH
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To: The Honorable Sylvia Luke, Chair
and Members of the House Committee on Finance

Date: Monday, April 1, 2013

Time: 2:00 p.m.

Place: Conference Room 309, State Capitol

From: Frederick D. Pablo, Director
Department of Taxation

Re: S.B. No. 573, S.D. 2, H.D. 1 Relating to Taxation

The Department of Taxation (Department) **appreciates the intent** of S.B. 573 S.D. 2, H.D. 1 and offers the following information and comments for your consideration.

This measure authorizes a state income tax credit of an unspecified amount for certain expenses paid or incurred by a school teacher during a taxable year. The measure has a defective effective date and applies to taxable years beginning after December 31, 2012.

Under the 2012 American Taxpayer Relief Act, the federal deduction for elementary and secondary school teachers, which had expired at the end of 2011, was extended for 2012 and 2013. Through conformity, the State will generally adopt changes made to the Internal Revenue Code.

While S.B. 573, S.D. 2, H.D. 1 provides that no other credit can be taken with the expenses claimed for this credit, it would not prevent a taxpayer from claiming both a deduction and the credit for the same expenses. When completing Hawaii income tax returns, taxpayers start by reporting their federal adjusted gross income (AGI). The federal AGI is an amount that is determined after income and above-the-line deductions, such as this deduction, are claimed on the taxpayer's federal income tax return. Since this amount is reflected on the federal return, the Hawaii return does not reflect whether the deduction was taken. Taxpayers would receive duplicate tax benefits as the amounts expended could be deducted in order to reach their federal AGI and then used to generate a tax credit that is used, dollar for dollar, to offset their tax liability.

The Department notes that, as written, the term "certain expenses" is extremely broad and should be more thoroughly defined to avoid potential compliance problems. The Department also notes that, due to technological and staffing constraints, the Department will have difficulty developing the required changes to forms and instructions in time for the 2013 tax filing season.

Should the proposal take effect upon its approval, the Department estimates that annual revenue loss would be \$3.5 million in FY 2014 and thereafter for a credit amount of \$250.

Thank you for the opportunity to provide comments.

TAXBILLSERVICE

126 Queen Street, Suite 304

TAX FOUNDATION OF HAWAII

Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: INCOME, Tax credit for expenses of school teachers

BILL NUMBER: SB 573, HD-1

INTRODUCED BY: House Committee on Education

BRIEF SUMMARY: Adds a new section to HRS chapter 235 to allow qualified taxpayers to claim a tax credit for “certain expenses” in a taxable year provided the credit shall not exceed \$_____ per taxable year and which shall be deductible from the taxpayer’s income tax liability for the taxable year the credit is properly claimed. Defines “qualified taxpayer” as a school teacher, special education teacher, school librarian, or counselor employed by the department of education, a charter school, or a private school in Hawaii that instructs students between junior kindergarten and twelfth grade. Defines “certain expenses” as expenses paid or incurred by a qualified taxpayer who incurs the expenses in connection with books, supplies (other than athletic supplies for courses of instruction in health or physical education), computer equipment (including related software and services) and supplementary materials used by the qualified taxpayer in the classroom. The credit shall be available for tax years beginning after 12/31/12.

Credits in excess of a taxpayer’s income tax liability shall be credited against a taxpayer’s subsequent income tax liability. Claims for the credit, including any amended claims, must be filed on or before the end of the 12th month following the close of the taxable year. Allows the director of taxation to adopt necessary rules and forms pursuant to HRS chapter 91 to carry out this section.

EFFECTIVE DATE: July 1, 2050; applicable to tax years beginning after December 31, 2012

STAFF COMMENTS: This measure proposes a tax credit of \$___ for out-of-pocket expenses incurred by a teacher. While the credit proposed in this measure would be granted without regard to a taxpayer’s need for tax relief or for that matter undertaking any specific action other than to be a teacher, it can be characterized as a backdoor pay increase for teachers as the credit is a dollar-for-dollar reduction of state income tax liability. It should be remembered that using the tax system to achieve social goals, as this measure proposes, is an inefficient means of accomplishing such goals. Credits are appropriate for alleviating an undue tax burden which certainly is not the case.

It should be noted that state income tax law already recognizes the federal “above the line” deduction for educator expenses. This deduction is taken before determining adjusted gross income and allows up to \$250 of qualified classroom expenses made by an educator (\$500 if the spouse is also an educator). This deduction was scheduled to expire at the end of 2012, but the American Taxpayer Relief Act, which was signed into law on January 2, 2013, extended the deduction. Should state lawmakers update the conformity statute, the deduction will again be available for state income tax purposes. While some have referred to the federal allowance as a “credit,” it is a “deduction” that reduces the amount of the taxpayer’s income that is subject to the federal income tax rates. The proposed credit on the other hand is a dollar-for-dollar reduction of the taxpayer’s liability and, therefore, far more generous.

While there is much empathy for the anecdotal reports of teachers using their own funds for classroom materials, the problem is with the bureaucratic system of requesting the funds and having the system take as much as six months to approve the money. The money has been appropriated, and it is the system that is frustrating. Thus, instead of using the tax system to “compensate” these teachers, first consideration should be given to “fixing the system.”

The suggestion has been made time and time again to give teachers debit like cards for the classroom supplies budget under EDN 100. The cards could be credited with a predetermined amount and could be encoded so that only defined classroom supplies could be purchased with that debit card. Such a system already has been employed to administer the state’s food stamp program, why can’t a similar system be established for classroom supplies rather than “mucking up” the tax system?

Instead of just throwing money at a problem, which in this case uses a tax credit, lawmakers should demand that the department fix the problem with the money that is there. Lawmakers, teachers and taxpayers should hold the bureaucracy of the department as well as the Board of Education responsible for not getting the resources allocated to classroom teachers. The legislature has continually funded resources for classroom teacher expenses, but the money goes unspent because teachers have little time to jump through the hoops to secure those funds. Perhaps an alternative might be to allocate the funds appropriated for classroom supplies to each school based on enrollment and economic circumstances of the community that school serves. If it is a poorer community, the per capita amount might be more than for a community which is more affluent. Approval and disbursement of the reimbursements could be located at the school level and overseen by the school administrator, e.g., the school principal or vice principal. Given that moneys are already being provided by the legislature for classroom supplies, the proposed credit is a redundancy. Thus, if lawmakers choose to go the route of the tax credit, then an amount equal to the loss of revenues incurred by the credit should be deleted from the department of education’s annual budget.

It is the bureaucracy that needs to be addressed. Since the tax credit is an indirect additional burden on all remaining taxpayers as it shifts the burden to those not so favored, this proposal amounts to a tax increase and steals money from other programs. Further, because the tax system is self-policing, one has to ask who will verify that the expenditures made do indeed qualify? If the teacher claims the credit and makes no expenditures, not only is it committing fraud, but it does amount to a backdoor salary increase. But then again, who is there to monitor whether or not the expenditure was made or for that matter whether or not the expenditure was a qualified expenditure.

The measure enumerates qualified expenditures as expenses in connection with books, supplies (other than athletic supplies for courses of instruction in health or physical education), computer equipment (including related software and services) and supplementary materials used by the qualified taxpayer in the classroom. However, anecdotal reports indicate that in some of the poorer neighborhoods, teachers have provided underwear and other articles of clothing so the students can attend school.

Should lawmakers adopt the proposed credit, then the federal deduction should be made inoperable for state income tax purposes, as having both would provide a double benefit for the same expenses.

**Testimony on SB573, SD2, HD1 (HSCR994) Relating to Taxation
Committee on Finance
Tuesday, April 2, 2013
2:00 PM, Conference Room 308, State Capitol**

By LYNN HAMMONDS, EXECUTIVE DIRECTOR, HAWAII TEACHER STANDARDS BOARD

April 1, 2013

Dear Chair Luke and Members of the Committee:

I am writing in support of SB573, SD2, HD1 (HSCR994) Relating to Taxation, which authorizes a state income tax credit for certain expenses paid or incurred by educators.

Hawaii teachers do not hesitate to spend out-of-pocket to ensure their students have supplies, even while contending with their own challenging financial constraints of pay cuts and rising health insurance costs. A dedicated teacher will always provide for their students, and I encourage you to provide tax relief for these selfless individuals.

Thank you for this opportunity to testify.



46-063 Emepela Pl. #U101 Kaneohe, HI 96744 · (808) 679-7454 · Kris Coffield · Co-founder/Legislative Director

**TESTIMONY FOR SENATE BILL 573, SENATE DRAFT 2, HOUSE DRAFT 1,
RELATING TO TAXATION**

**House Committee on Finance
Hon. Sylvia Luke, Chair
Hon. Scott Y. Nishimoto, Vice Chair
Hon. Aaron Ling Johanson, Vice Chair**

**Tuesday, April 2, 2013, 2:00 PM
State Capitol, Conference Room 308**

Honorable Chair Luke and committee members:

I am Kris Coffield, representing the IMUAlliance, a nonpartisan political advocacy organization that currently boasts over 150 local members. On behalf of our members, we offer this testimony in strong support of, with proposed amendments for SB 573, relating to taxation.

In 2011, the National School Supply and Equipment Association released a report stating that public school teachers spent \$1.33 billion of their discretionary income on supplementary school supplies and instructional materials during the 2009-2010 school year, an average of \$356 dollars per teacher. Though less than previous years in which a report was issued, that number, when broken down, nonetheless amounts to \$170 for supplies and \$186 on instructional materials not provided for by the Departments of Education. Moreover, NSSEA attributes the drop not to increased classroom funding, but the impact of the recent recession upon educators' discretionary income levels.

The trend is, if anything, worse in Hawaii, which has consistently ranked at or near the bottom in national cost-of-living studies and was recently ranked second-worst in a Center for Budget and Policy Priorities ranking of per-pupil spending cuts, with Hawaii cutting \$1,175 in per-pupil spending between FY 2008 and FY 2012, adjusted for inflation. Similarly, Hawaii has the highest ACCRA value in the country, typically hovering between 160 and 165, leading to our state being ranked last, year after year, in teacher salaries adjusted for cost-of-living,

with the average teacher making a COL-adjusted income of \$31,854 per year, roughly \$4,000 below the next-to-last state on the list (Maine), according to statistics compiled and released by the U.S. Census Bureau. Pay cuts (including teacher furloughs and DLWOP days), rising health care costs, adjusted insurance co-pays, and the loss of the state's \$1,690-per-special-education-teacher classroom supply fund have all aggravated the financial burden borne by teachers' pocketbooks. In a recent survey conducted by HSTA, 47 percent of respondents cited personal expenditures between \$250 and \$500 each year on classroom supplies, with many claiming expenditures in excess of \$1,000. Not surprisingly, these same teachers have called upon HSTA—and lawmakers—to take action to lighten their financial load.

In the past, opponents of this bill have argued that a tax credit for teachers amounts to a *de facto* pay increase for a selected class of citizens, one that would not rectify the structural barriers hindering the DOE's appropriation of funds for supplies. We agree with our opponents that it should not take up to six months for funding requests to be approved and facilitated. At the same time, though, we understand that structural inefficiencies result, in part and in a self-fulfilling fashion, from a lack of adequate funding. Mandatory budget cuts have crippled the DOE, in recent years, leading to reconsideration of whether or not to continue successful learning programs. Unfortunately, when budget cuts pose an existential threat to successful learning centers and categorical programs, the DOE's priorities shift from classroom support to programmatic savings. Put simply, in times of economic austerity, the DOE must spend more time accounting for basic, overarching programmatic needs, crowding out concerns about the efficient allocation of funds for individual teachers.

Additionally, it must be said that the “pay increase” contention cuts both ways. Granted, tax credits do lessen the individual tax burden of educators. Ensuring that educators have more money in their pocketbooks, however, effectively increases their purchasing power. Therefore, providing a tax credit for teachers incentivizes the teaching profession, at a time when our state's high cost-of-living and low adjusted-average income compel many would-be teachers to choose more highly compensated professions or, even worse, leave the state altogether—today, approximately 50 percent of teachers leave our state's classrooms every five years, giving Hawaii the distinction of having the highest turnover rate in the nation. If policymakers are truly interested in enhancing the DOE's ability to recruit highly effective teachers into our schools, providing fiscal incentives that

offset cost-of-living problems is a worthy path to take, whose longterm benefits are extremely likely to outweigh its immediate costs.

That said, we encourage the committee to extend this tax credit to cover librarians working within the Hawaii State Public Library System, who also spend personal money to expand educational resources and programs for Hawaii's schoolchildren. To enact this amendment (which has been considered as part of previous versions of this measure), we urge you to amend the definition of "qualified tax payer" to mean "a school teacher, special education teacher, school librarian, or counselor employed by the department of education, a charter school, ~~or~~ a private school in Hawaii that instructs students between junior kindergarten and twelfth grade, or a public service librarian employed by the Hawaii state public library system."

Again, we urge your committee to increase state educators' purchasing power by instituting tax credits for supplies, computer equipment, and supplementary materials, which will assist in the recruitment and retention of highly effective teachers who might otherwise leave the profession, or even the state, because of financial hurdles.

Mahalo for the opportunity to testify in strong support of this measure.

Sincerely,
Kris Coffield
Legislative Director
IMUAlliance

FINTestimony

From: mailinglist@capitol.hawaii.gov
Sent: Saturday, March 30, 2013 4:31 PM
To: FINTestimony
Cc: aicorrea@juno.com
Subject: Submitted testimony for SB573 on Apr 2, 2013 14:00PM

SB573

Submitted on: 3/30/2013

Testimony for FIN on Apr 2, 2013 14:00PM in Conference Room 308

Submitted By	Organization	Testifier Position	Present at Hearing
Aileen Correa	Individual	Support	No

Comments: I support this bill, but would like it to be effective for SY 2012-13, not 2050.

Please note that testimony submitted less than 24 hours prior to the hearing, improperly identified, or directed to the incorrect office, may not be posted online or distributed to the committee prior to the convening of the public hearing.

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FINTestimony

From: mailinglist@capitol.hawaii.gov
Sent: Saturday, March 30, 2013 11:13 AM
To: FINTestimony
Cc: cjpasco@gmail.com
Subject: Submitted testimony for SB573 on Apr 2, 2013 14:00PM

SB573

Submitted on: 3/30/2013

Testimony for FIN on Apr 2, 2013 14:00PM in Conference Room 308

Submitted By	Organization	Testifier Position	Present at Hearing
Colleen Pasco	Individual	Support	No

Comments: In encourage you to support SB 573 giving tax credits to teachers for educational purchases. Surveys repeatedly show teachers spend a great deal of money out of their own pockets (even during these furlough years) to provide necessary supplies for their classrooms. It is sad that this even occurs, but teachers should be able to recoup those expenditures in some way. Not all teachers need to itemize on tax returns. Having a tax credit would be very beneficial to all. Please support public school teachers and this measure. Thank you.

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FINTestimony

From: mailinglist@capitol.hawaii.gov
Sent: Sunday, March 31, 2013 7:38 PM
To: FINTestimony
Cc: tabraham08@gmail.com
Subject: Submitted testimony for SB573 on Apr 2, 2013 14:00PM

SB573

Submitted on: 3/31/2013

Testimony for FIN on Apr 2, 2013 14:00PM in Conference Room 308

Submitted By	Organization	Testifier Position	Present at Hearing
Troy Lopaka Abraham	Individual	Support	No

Comments: I support urgent passage of this bill to allows educators who pay things for their students tax insentives to receive bonuses for their tax return

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