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To: The Honorable Jill N. Tokuda, Chair  
and Members of the Senate Committee on Ways and Means

Date: Friday, February 6, 2015  
Time: 9:00 A.M.  
Place: Conference Room 211, State Capitol

From: Maria E. Zielinski, Director  
Department of Taxation

Re: S.B. 947, Relating to Conformance of State Personal Exemption to  
Federal Personal Exemption

The Department of Taxation (Department) appreciates the intent of S.B. 947 and provides the following comments for your consideration.

S.B. 947 conforms the Hawaii income tax law to the federal income tax law for personal exemptions. Conforming would increase the personal exemption from \$1,144 to \$2,000 for individual taxpayers and from \$400 to \$600 for estates. Conforming would increase the personal exemption from \$200 to \$300 for trusts required to distribute all income currently and from \$80 to \$100 for all other trusts. Hawaii does not conform to the Internal Revenue Code section which provides for the inflation adjustments, thus, the exemption amounts stated above are unadjusted.

Conforming to federal law would extend the phaseout of the personal exemption. Hawaii imposes its own phaseout of the personal exemption, separate from the federal phaseout. Hawaii's phaseout provision sunsets on June 30, 2015. This bill, by conforming to federal law, would impose the federal phaseout of the personal exemption, which is permanent.

S.B. 947 also repeals the \$7,000 personal exemption afforded to a blind, deaf, or totally disabled person, and the additional personal exemption afforded to taxpayers or spouses who are over 65 years old.

The Department is able to administer the changes made by S.B. 947, but notes that the bill does more than simply increase the personal exemption amounts. As drafted, the bill would

decrease the personal exemption for all taxpayers who are over 65 years old and who are blind, deaf, or totally disabled. The bill would also decrease the personal exemption for taxpayers with adjusted gross incomes exceeding the federal phaseout thresholds, which are currently \$250,000 for single taxpayers, and \$300,000 for married taxpayers filing jointly.

The estimated revenue loss is \$115 million in FY 2017, increasing by 2% annually thereafter.

Thank you for the opportunity to provide comments.

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SUBJECT: INCOME, Adopt federal personal exemption

BILL NUMBER: SB 947; HB 753 (Identical)

INTRODUCED BY: SB by Slom, Galuteria and 5 Democrats; HB by McDermott

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, 2016; applicable to tax years beginning after December 31, 2015

STAFF COMMENTS: The state personal exemption stands at \$1,144. This measure would replace the state's personal exemption amounts with the federal personal exemption amounts. Currently the federal personal exemption amount is \$3,950 for 2014. 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.

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.

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 2/4/15