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To: The Honorable Donovan M. Dela Cruz, Chair
and Members of the Senate Committee on Ways and Means

Date: Thursday, February 21, 2019
Time: 10:00 A.M.
Place: Conference Room 211, State Capitol

From: Linda Chu Takayama, Director
Department of Taxation

Re: S.B. 161, S.D. 1, Relating to Taxation

The Department of Taxation (Department) provides the following comments regarding S.B. 161, S.D. 1, for your consideration.

S.B. 161, S.D. 1, creates a nonrefundable income tax credit for businesses that hire individuals with a disability. The bill requires certification of disability from a qualified physician, and is claimed against the taxpayer's net income tax liability for the year in which it is earned with any excess carried forward until used. The Senate Committee on Human Services adopted the Department's recommendation to limit qualified wages to only that paid in cash, further clarified the term "individual with a disability", and made the credit 25% of the wages paid for the first 12 months rather than 50% of wages paid for the first six months as was in the original measure. The measure is effective upon approval and applies to taxable years beginning after December 31, 2018.

First, the Department notes that the proposed credit is similar to an already existing credit at Hawaii Revised Statutes (HRS) section 235-55.91. This credit is equal to twenty per cent of wages paid to vocational rehabilitation referrals during the first year of employment. To qualify for this credit, the employer must hire a person with a physical or mental disability who was referred to the employer by the Department of Human Services Vocational Rehabilitation and Services for the Blind Division. The Department believes that it may be more effective and efficient to amend or expand the current vocational income tax incentive rather than creating an entirely new credit.

Second, the Department notes that the term "individual with a disability" should be more clearly defined. As currently written, physicians will be unable to make consistent determinations of whether an individual would qualify for the credit because there is no set standard to make the determination by. The Department also notes that the definition could be interpreted to cover situations where the impairment is readily treatable with medications or

impairments from which one has fully recovered with no likelihood of relapse or reoccurrence.

Third, the Department notes that the wages allowed as the base of this credit are also allowed as a deduction as an expense to the employer. Thus, the employer would be provided a double tax benefit-claiming both an expense deduction and a tax credit for the same costs. In addition, a taxpayer could conceivably use the same expenditures to also claim the vocational rehabilitation credit. The Department suggests "qualified wages" be defined in the measure as follows:

"Qualified wages" means wages attributable to work rendered by an individual with a disability for the twelve-month period after the individual is initially hired, but does not include amounts for which another credit is claimed or for which a deduction is taken.

Fourth, the Department notes that the credit as currently written may be prone for abuse. While the measure attempts to prevent abuse by preventing the hiring of persons related to the taxpayer, it does not prevent the employers from hiring each other's disabled employees to qualify for the credit.

Fifth, the Department notes that there is no continuing requirement that the person remain in the employ of the taxpayer. After a year, the taxpayer could simply terminate employment, yet retain all of the credit. The Department strongly believes that there should be a minimum amount of time for which the employee must be retained, beyond the period in which the credit is calculated.

Finally, the Department requests that this new credit be made applicable to taxable years beginning after December 31, 2019 to allow the Department sufficient time to make the necessary form, instruction, and computer system changes.

Thank you for the opportunity to provide comments.

TAX FOUNDATION OF HAWAII

126 Queen Street, Suite 304

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SUBJECT: INCOME, Credit for Hiring Individual with a Disability

BILL NUMBER: SB 161, SD-1

INTRODUCED BY: Senate Committee on Human Services

EXECUTIVE SUMMARY: Provides a taxpayer who hires an individual with a disability a nonrefundable tax credit for the 6-month period after the individual is initially hired by the taxpayer. The adoption of this credit would provide tax relief to taxpayers regardless of their need for tax relief. It also would shift the burden of paying for government to the rest of us.

SYNOPSIS: Adds a new section to HRS chapter 235 to allow employers to claim an income tax credit for the hiring of an individual with a disability equal to 25% of the qualified wages for the first twelve months after the individual is hired.

To be treated as an individual with a disability, the employer must receive certification from a qualified physician before the individual begins work. If the certification is incorrect because it is based on false information provided by the individual, the certification shall be revoked and wages paid by the employer after the employer receives notice of revocation shall not be treated as qualified wages.

Payments between related parties are excluded, as are wages paid by any former employer.

Tax credits that exceed the taxpayer's income tax liability may be used as a credit against the taxpayer's income tax liability in subsequent years until exhausted. In no taxable year shall the total amount of tax credits claimed under this section exceed \$ _____ per taxpayer.

Requires claims for the credit, including any amended claims, to be filed on or before the end of the twelfth month following the taxable year for which the credit is claimed. Failure to comply with the foregoing provision shall constitute a waiver of the right to claim the tax credit.

Defines "individual with a disability" as an individual having a physical or intellectual impairment that is not temporary in nature and that substantially limits one or more major life activities, having a record of that impairment, or being regarded as having that impairment; provided that the disabling impairment is certified by a qualified physician.

Defines "wages" as wages, commissions, fees, salaries, bonuses, and all other kinds of remuneration for, or compensation attributable to, services performed by an employee for the employee's employer that are paid in cash, but excluding income excluded from gross income by section 235-7 or other provisions of the Income Tax Law. For example, employer funded pensions don't count.

If the taxpayer is a successor employer referred to in section 3306(b)(1) of the IRC, the determination of the amount of the credit shall be made in the same manner as if the wages were paid by the predecessor employer (as defined in IRC section 3306(b)(1)).

EFFECTIVE DATE: This Act, upon its approval, shall apply to taxable years beginning after December 31, 2018.

STAFF COMMENTS: This measure is proposed as an incentive to entice employers to hire an individual who is physically or intellectually disabled, but the tax system is a poor means of achieving such social goals. Providing such credits against the state income tax merely reduces state revenues, and if the size of government does not go down, then the tax burden shifts to other taxpayers who are not able to claim the credit.

The measure is like the existing income tax credit for the hiring of vocational rehabilitation referrals. If it is the intent of the legislature to encourage the hiring of individuals with a disability, it would be preferable to amend HRS-235-55.91 to include these individuals rather than to adopt a new credit which may have loopholes and technical issues.

Digested 2/19/2019

SB-161-SD-1

Submitted on: 2/20/2019 12:38:13 AM

Testimony for WAM on 2/21/2019 10:00:00 AM

Submitted By	Organization	Testifier Position	Present at Hearing
Melodie Aduja	Testifying for O`ahu County Committee on Legislative Priorities of the Democratic Party of Hawai`i	Support	No

Comments:

Hawai'i State Association of Counties (HSAC)

Counties of Kaua'i, Maui, Hawai'i and City & County of Honolulu

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February 19, 2019

To: The Honorable Donovan M. Dela Cruz, Chair
Senate Committee on Ways and Means

FROM: Valerie T. Poindexter
HSAC President



SUBJECT: **DECISION MAKING OF FEBRUARY 21, 2019; TESTIMONY IN SUPPORT OF SB161 SD1, RELATING TO TAXATION**

Thank you for the opportunity to testify on behalf of the Hawai'i State Association of Counties in full support of SB161 SD1 that encourages the hiring of individuals with a disability.

The purpose of this bill is to provide to a taxpayer who hires an individual with a disability a nonrefundable tax credit for the 12-month period after the individual is initially hired by the taxpayer and applies to taxable years beginning after 12/31/2018.

HSAC strongly supports and urges the enactment of SB161 SD1.

Mahalo for your time and consideration.

