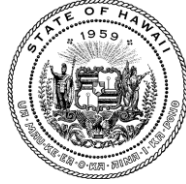


DAVID Y. IGE  
GOVERNOR

JOSH GREEN M.D.  
LT. GOVERNOR



STATE OF HAWAII  
**DEPARTMENT OF TAXATION**  
P.O. BOX 259  
HONOLULU, HAWAII 96809  
PHONE NO: (808) 587-1540  
FAX NO: (808) 587-1560

ISAAC W. CHOY  
DIRECTOR OF TAXATION

To: The Honorable Sean Quinlan, Chair;  
The Honorable Daniel Holt, Vice Chair;  
and Members of the House Committee on Economic Development

From: Isaac W. Choy, Director  
Department of Taxation

Date: February 12, 2021  
Time: 9:30 A.M.  
Place: Via Video Conference, State Capitol

**Re: H.B. 1388, Relating to Taxation**

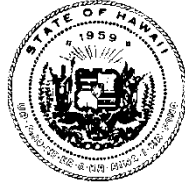
The Department of Taxation (Department) offers the following comments regarding H.B. 1388, for your consideration.

H.B. 1388 eliminates home mortgage interest deduction for second homes by de-conforming to the Internal Revenue Code sections 163(h)(4)(A)(i)(II) and 163(h)(4)(A)(ii)(II). H.B. 1388 also directs the revenue gains from the elimination of home mortgage interest deduction for second homes to be deposited into the rental housing revolving fund (RHRF). The bill is effective upon its approval and applies to taxable years beginning after December 31, 2020.

The Department can implement the elimination of home mortgage interest deduction for second homes for taxable years beginning after December 31, 2020. However, as a matter of policy, specific individual taxpayers' information should not be used to direct tax revenues to any specific funds. If the Legislature wishes to direct additional tax revenues to the RHRF, the Department suggests that it be done via appropriation of a specific amount from the general fund to the RHRF.

Thank you for the opportunity to provide comments.

DAVID Y. IGE  
GOVERNOR



DENISE ISERI-MATSUBARA  
EXECUTIVE DIRECTOR

**STATE OF HAWAII**

DEPARTMENT OF BUSINESS, ECONOMIC DEVELOPMENT AND TOURISM  
HAWAII HOUSING FINANCE AND DEVELOPMENT CORPORATION  
677 QUEEN STREET, SUITE 300  
Honolulu, Hawaii 96813  
FAX: (808) 587-0600

IN REPLY REFER TO:

Statement of  
**DENISE ISERI-MATSUBARA**  
Hawaii Housing Finance and Development Corporation  
Before the

**HOUSE COMMITTEE ON ECONOMIC DEVELOPMENT**

February 12, 2021 at 9:30 a.m.  
State Capitol, Room 312

In consideration of  
**H.B. 1388**  
**RELATING TO TAXATION.**

The HHFDC ***appreciates the intent*** of H.B. 1388, a bill that eliminates the mortgage interest deduction for second homes, and requires that revenue gained from its elimination be deposited in the Rental Housing Revolving Fund (RHRF).

HHFDC takes no position on the tax policy implications of this bill.

The RHRF provides equity gap low-interest financing to qualified owners and developers of affordable rental housing. We note that the Executive Biennium Budget request includes a request for infusion of General Obligation Bond funds into the RHRF of \$25,000,000 in FY2022-2023.

Thank you for the opportunity to provide written comments on this bill.

# TAX FOUNDATION OF HAWAII

126 Queen Street, Suite 304

Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: INCOME, Disallows Home Mortgage Interest Deduction for Second Homes

BILL NUMBER: SB 202; HB 1388

INTRODUCED BY: SB by RHOADS, CHANG; HB by GANADEN, HOLT, ILAGAN, KAPELA, LOPRESTI, MATAYOSHI, Marten, McKelvey, Mizuno

EXECUTIVE SUMMARY: Eliminates the home mortgage interest deduction for second homes under Hawaii income tax law. Requires the amount of state revenue gained by eliminating the deduction to be deposited into the rental housing revolving fund.

SYNOPSIS: Amends section 235-2.4, HRS, to eliminate the home mortgage interest deduction for second homes for Hawaii income tax purposes.

Directs the revenue gained by eliminating the above deduction to be deposited into the rental housing revolving fund.

EFFECTIVE DATE: Upon approval.

STAFF COMMENTS: There are likely to be practical issues with capturing the data needed even to come up with an estimate of revenue gain.

First, the Tax Cuts and Jobs Act of 2018 greatly increased the standard deduction allowable to individual taxpayers, so many taxpayers would no longer need to itemize the mortgage interest deduction for federal purposes. For state purposes, the standard deduction is smaller and taxpayers would itemize the deduction for mortgage interest, and if this bill were enacted they simply would not put down any deduction for mortgage interest on a second home. For taxpayers in this situation, it would be difficult or impossible to determine how much, if any, deduction was forgone.

Then, Hawaii requires certain deduction limits including the so-called Pease limitation in IRC section 68. (The section 68 limitations have been suspended for federal purposes, but Hawaii has decoupled from that suspension in HRS section 235-2.4(c)(2).) The IRC section 68 reductions are equal to 80% of the otherwise allowable itemized deductions or 3% of the excess of the taxpayer's AGI over the threshold, whichever is smaller. For Hawaii income tax purposes, HRS section 235-2.4(c) provides that the threshold is \$166,800 for all taxpayers except married taxpayers filing separately, for which it is \$83,400. For higher income taxpayers, against whom this provision is probably directed, the Pease limitation will be considerable. It is highly uncertain whether there would be significant, if any, revenue gain from this provision because the mortgage interest deduction may be reduced or denied because of the Pease limitations.

The Foundation is also concerned with earmarking of revenues away from the general fund. As with any earmarking of revenues, the legislature will be preapproving each of the programs fed by the fund into which the tax monies are diverted, expenses from the funds largely avoid

legislative scrutiny, and the effectiveness of the programs funded becomes harder to ascertain. It is also difficult to determine whether the fund has too little or too much revenue.

If the legislature deems the programs and purposes funded by this revolving fund to be a high priority, then it should maintain the accountability for these funds by appropriating the funds as it does with other programs. Earmarking revenues merely absolves elected officials from setting priorities. If the money were appropriated, lawmakers could then evaluate the real or actual needs of each program.

Digested 1/30/2021

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February 12, 2021

**The Honorable Sean Quinlan, Chair**  
House Committee on Economic Development  
Via Videoconference

Aloha Chair Quinlan, Vice Chair Holt, and Members of the Committee,

I am Ken Hiraki, Director of Government Affairs, testifying on behalf of the Hawai'i Association of REALTORS® (“HAR”), the voice of real estate in Hawai'i, and its over 10,000 members. HAR **opposes** House Bill 1388 which eliminates the home mortgage interest deduction for second homes under Hawaii income tax law. Requires the amount of state revenue gained by eliminating the deduction to be deposited into the Rental Housing Revolving Fund.

The Mortgage Interest Deduction (MID) on state and federal income taxes was introduced along with the income tax itself in 1913. The MID allows homeowners who itemize deductions on their taxes to deduct mortgage interest attributable to primary residence and second-home debt, and interest paid on home equity debt.

The Mortgage Interest Deduction encourages the American Dream of homeownership and gives people financial security through homeownership. The deduction helps home purchasers make their mortgage payments more affordable and is vital to the health and stability of housing markets.

In today's real estate environment, more homeowners are purchasing a second home for their elderly parents or their adult children who cannot otherwise afford to pay for a home.

HAR believes that the MID for second homes is an important opportunity for individuals to use to invest for retirement or to support their families with Hawaii's high cost of living and housing.

Mahalo for the opportunity to testify.



February 12, 2021

9:30 a.m.

VIA VIDEOCONFERENCE

Conference Room 312

**To: House Committee on Economic Development**

**Rep. Sean Quinlan, Chair**

**Rep. Daniel Holt, Vice Chair**

**From: Grassroot Institute of Hawaii**

**Joe Kent, Executive Vice President**

RE: HB1388 — RELATING TO TAXATION

***Comments Only***

Dear Chair and Committee Members:

The Grassroot Institute of Hawaii would like to offer its comments on [HB1388](#), which would eliminate the home mortgage interest deduction for second homes under Hawaii income tax law.

We are gravely concerned about the impact of this tax hike and the many tax increases and surcharges that have been proposed this legislative session. Hawaii residents are already among the most taxed in the country; the state has the [second highest overall tax burden](#) in the U.S.

That high tax burden contributes to Hawaii's cost of living and is one of the reasons why so many Hawaii residents have been leaving in search of greater opportunities elsewhere.

Given the state's already-high tax burden, there is never a good time to raise taxes. But this proposal comes at an especially bad time. The state is still in a state of emergency, tourism has slowed to a trickle, businesses are closing and unemployment is high. The economy will take years to recover from the pandemic and lockdowns. The last thing Hawaii residents and businesses need at this point is a tax hike.

There are myriad reasons policy makers should be wary of implementing tax hikes at this time. Here are just a few:

>> Hawaii cannot sustain a hike in taxes since its already-damaged economy was hit harder by the lockdowns than any other state in the nation.<sup>1</sup>

>> State lawmakers increased taxes and fees substantially following the Great Recession of 2007-2008,<sup>2</sup> despite a windfall in revenues from an economic boom over the past decade. Taxes and fees ballooned on motor vehicles, transient accommodations, estates, fuel, food, wealthy incomes, property, parking and businesses.

>> Hawaii's population reduction of 21,879 people since fiscal 2016<sup>3</sup> has left Hawaii's remaining taxpayers with a greater tax burden.

>> Hawaii businesses are already bracing for an automatic tripling, on average, of the state unemployment tax.<sup>4</sup> The UI tax rate depends not only on individual employer's claims experiences but also on the overall health of the state's unemployment insurance fund, which is hundreds of millions of dollars in the red.<sup>5</sup>

>> Hawaii already has a regressive general excise tax that disproportionately hits the poor.<sup>6</sup>

>> Hawaii has a progressive income tax that taxes high-income earners at 11%, second only to California at 13.3%.<sup>7</sup> Hawaii's top 1% already pays 23% of all income taxes in the state.<sup>8</sup>

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<sup>1</sup> Dave Segal, "[Hawaii's unemployment rate hit nation-high 15% in September](#)," Honolulu Star-Advertiser, Oct. 20, 2020.

<sup>2</sup> "[Tax Acts \(by Year\)](#)," Tax Foundation of Hawaii, accessed Feb. 8, 2021.

<sup>3</sup> "[Annual Estimates of the Resident Population for the United States, Regions, States, and the District of Columbia: April 1, 2010 to July 1, 2020 \(NST-EST2020\)](#)" U.S. Census Bureau, Population Division, December 2020.

<sup>4</sup> "[State unemployment tax slated to automatically triple in 2021](#)," Grassroot Institute of Hawaii, Nov. 16, 2020.

<sup>5</sup> "[UI Budget](#)," United States Department of Labor, Employment & Training Administration, Feb. 8, 2021.

<sup>6</sup> "Rich States, Poor States: ALEC-Laffer State Economic Competitiveness Index: "[Sales Tax Burden](#)," American Legislative Exchange Council, 2021. Note that Hawaii does not have a sales tax, but a state general excise tax that is levied on almost all goods and services, and imposed multiple times throughout the production chain.

<sup>7</sup> Katherine Loughhead, "[State Individual Income Tax Rates and Brackets for 2020](#)," Tax Foundation, Feb. 4, 2020.

<sup>8</sup> "[Hawaii Individual Income Tax Statistics](#)," Hawaii Department of Taxation, December 2020, Table 13A.

>> Closing tax exemptions would amount to a tax hike for Hawaii businesses already facing a steep spike in their unemployment insurance taxes.

>> Increasing Hawaii's lowest-in-the-nation property-tax rates<sup>9</sup> would result in a much higher overall tax bill compared to other states because Hawaii residents uniquely pay for public education through the general fund as opposed to property taxes.<sup>10</sup> Additionally, Hawaii's low property taxes are balanced out by the highest housing costs in the nation,<sup>11</sup> which results in a \$1,236 average annual property tax per capita, which is only slightly below the national average of \$1,617.<sup>12</sup>

Hawaii needs leadership that will stabilize the current financial crisis, reduce unsustainable long-term costs and lower the cost of living. Balancing the books without tax increases or future debt could send a message that Hawaii is a good place for businesses and future generations, and this could help the economy thrive while motivating people to return to the islands.

If the state needs more revenues, policymakers should focus on growing the economy. In our current condition, even small economic gains would have big effects.

If the purpose of the tax is to alter behavior, consider that the negative impact of a tax hike can far outweigh whatever policy goal is being pursued.

Hawaii's residents and businesses need a break from new taxes, fees, surcharges and tax hikes. This is not the time to make Hawaii a more expensive place to live and do business.

Thank you for the opportunity to submit our comments.

Sincerely,

Joe Kent  
Executive Vice President,  
Grassroot Institute of Hawaii

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<sup>9</sup> John Keirnan, "[Property Taxes by State](#)," WalletHub, Feb. 25, 2020.

<sup>10</sup> Janis Magin, "[Hawaii lawmakers seek to add new property tax to fund teacher pay](#)," Pacific Business News, Jan. 27, 2020.

<sup>11</sup> "[Average House Price by State in 2020](#)," The Ascent, Aug. 4, 2020.

<sup>12</sup> Janelle Cammenga, "[How Much Does Your State Collect in Property Taxes per Capita?](#)," Tax Foundation, March 11, 2020.