

**TESTIMONY OF
THE DEPARTMENT OF THE ATTORNEY GENERAL
KA 'OIHANA O KA LOIO KUHINA
THIRTY-SECOND LEGISLATURE, 2024**

ON THE FOLLOWING MEASURE:
H.B. NO. 1572, RELATING TO TAXATION.

BEFORE THE:
HOUSE COMMITTEE ON FINANCE

DATE: Wednesday, February 21, 2024 **TIME:** 2:00 p.m.

LOCATION: State Capitol, Room 308 and Videoconference

TESTIFIER(S): Anne E. Lopez, Attorney General, or
Janine R. Udoi, Deputy Attorney General

Chair Yamashita and Members of the Committee:

The Department of Attorney General (Department) has concerns regarding this bill and provides the following comments.

This bill proposes to amend section 235-7(a)(3), Hawaii Revised Statutes, to limit the exclusion from gross income received from pensions to only "compensation received in the form of a pension for past services performed in the State" when determining the taxability of pensions. See section 2, page 2, lines 7-8.

This bill could be subject to challenge as violating the Commerce Clause of the United States Constitution, which provides that Congress shall have the power to "regulate Commerce . . . among the several States." U.S. Const. art. I, § 8, cl. 3. "Though phrased as a grant of regulatory power to Congress, the Clause has long been understood to have a 'negative' aspect that denies the States the power unjustifiably to discriminate against or burden the interstate flow of articles in commerce." *Or. Waste Sys., Inc. v. Dep't of Env'tl. Quality*, 511 U.S. 93, 98 (1994). This negative aspect of the Commerce Clause is known as the dormant Commerce Clause.

Tax schemes that discriminate against interstate commerce may violate the dormant Commerce Clause. For example, in *Comptroller of Treasury of Maryland v. Wynne*, 575 U.S. 542 (2015), the United States Supreme Court struck down a tax scheme where resident taxpayers paid income tax to another jurisdiction for income earned in that state but were not allowed a tax credit for a portion of these taxes. The

Court noted that the dormant Commerce Clause prohibits states from "discriminat[ing] between transactions on the basis of some interstate element." See *Wynne*, 575 U.S. at 549. Further, the Court found, "[t]his means among other things, that a State "may not tax a transaction or incident more heavily when it crosses state lines than when it occurs entirely within the State." *Id.* (citations omitted). Because Maryland's law functioned as a tariff by discriminating against interstate commerce, it violated the dormant Commerce Clause. See *id.* at 567.

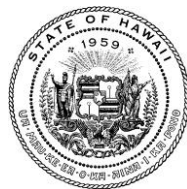
Here, this bill would result in the taxation of pension income Hawaii resident taxpayers earned for services performed in other states but not the taxation of pension income Hawaii resident taxpayers earned for services performed in the State. Like in *Wynne*, this tax scheme may be found to violate the dormant Commerce Clause because it could be construed as a tariff by discriminating against the earnings of Hawaii residents who receive compensation in the form of a pension for services performed outside of the State.

Based on the foregoing, we respectfully ask that these concerns be addressed by deleting the wording on section 2, page 2, line 8, "performed in the State" and including, instead, a nondiscriminatory tax mechanism to achieve the bill's intended goal set forth in section 1, page 1, lines 5-8, to "establish equity among taxpayers residing in Hawaii and help grow the State's economy."

Thank you for the opportunity to provide comments.

JOSH GREEN M.D.
GOVERNOR

SYLVIA LUKE
LT. GOVERNOR



STATE OF HAWAII
DEPARTMENT OF TAXATION

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DEPUTY DIRECTOR

**TESTIMONY OF
GARY S. SUGANUMA, DIRECTOR OF TAXATION**

TESTIMONY ON THE FOLLOWING MEASURE:

H.B. No. 1572, Relating to Taxation.

BEFORE THE:

House Committee on Finance

DATE: Wednesday, February 21, 2024

TIME: 2:00 p.m.

LOCATION: State Capitol, Room 308

Chair Yamashita, Vice-Chair Kitagawa, and Members of the Committee:

The Department of Taxation ("Department") offers the following comments regarding H.B. 1572 for your consideration.

H.B. 1572 would amend section 235-7, Hawaii Revised Statutes (HRS), by limiting the income tax exclusion for pensions only to those pensions earned for past services performed within Hawai'i. This would make all other pensions subject to State income tax. The measure would apply to taxable years beginning after December 31, 2023.

The Department requests that the effective date of this measure be postponed and made applicable to taxable years beginning after December 31, 2024. This will provide sufficient time to make the necessary form, instruction, and computer system changes, as well as to provide taxpayer education about the change in the law.

Thank you for the opportunity to provide comments on this measure.

TAX FOUNDATION OF HAWAII

126 Queen Street, Suite 305

Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: INCOME, Limit Pension Exclusion to In-State Payors

BILL NUMBER: HB 1572

INTRODUCED BY: KILA, BELATTI, COCHRAN, KITAGAWA, LAMOSAO, LOWEN, MARTEN, MARTINEZ, MATAYOSHI, MIYAKE, MORIKAWA, ONISHI, PERRUSO, TAKENOUCI, Amato, Sayama

EXECUTIVE SUMMARY: Limits the exclusion from gross income to pensions received for past services provided in the State.

SYNOPSIS: Amends section 235-7(a)(3), HRS, which currently provides an exclusion for a pension for past services, to limit the exclusion to pensions for past services performed in the State.

EFFECTIVE DATE: Applies to taxable years beginning after December 31, 2023.

STAFF COMMENTS: There is a constitutional issue. The restriction on pensions to those paid by Hawaii employers (for past services performed in Hawaii) could be unconstitutional under the Commerce Clause of the U.S. Constitution because the same preferential tax treatment is not allowed for pensions for work performed in other States. *In re Hawaiian Flour Mills, Inc.*, 76 Haw. 1, 868 P.2d 419 (1994); *Bacchus Imports, Inc. v. Dias*, 468 U.S. 263 (1984); Hawaii Tax Information Release No. 93-4.

Prof. Walter Hellerstein observed:

In *Boston Stock Exchange v. State Tax Commission*, 429 U.S. 318 (1977), the Court struck down a New York stock transfer tax scheme that provided reduced rates for stock transfers when the sale of the stock was made through a New York rather than out-of-state broker. The state contended that the tax break for local stock sales was merely an incentive designed to assist the New York brokerage industry. The Court acknowledged that states are free to “structur[e] their tax systems to encourage the growth and development of intrastate commerce and industry,” but held they may not do so by means that discriminate against interstate commerce. By providing a tax incentive for sellers to deal with New York rather than out-of-state brokers, the state had, in the Court's eyes, “foreclose[d] tax-neutral decisions.” Moreover, it had done so through the coercive use of its taxing authority. As the Court noted, “the State is using its power to tax an instate operation as a means of requiring other business operations to be performed in the home State.”

Hellerstein, *Commerce Clause Restraints on State Tax Incentives*, available at <https://www.minneapolisfed.org/article/1996/commerce-clause-restraints-on-state-tax-incentives>.

Re: HB 1572

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The bill gives employees an incentive to work for in-state employers as opposed to out-of-state employers, and thus may be seen as discriminating against interstate commerce.

Digested: 2/19/2024



HAWAII APPLESEED

CENTER FOR LAW & ECONOMIC JUSTICE

Dear Chair Yamashita, Vice Chair Kitagawa, and Members of the Committee,

Thank you for the opportunity to testify in **support** of HB 1572, which would look to only exempt pension-based gross income from taxation in the case of individuals who have provided services for the State. This would promote tax equity by ensuring that retirees who move to Hawai‘i pay their fair share towards the government programs and services that we all benefit from.

Many of Hawai‘i’s working families have been forced to move to the continental United States due to the high cost of living. In 2022 alone, over 15,000 local residents moved out of Hawai‘i, contributing to an overall decline in the state’s population. At the same time, thousands of residents of other states continue to move to Hawai‘i each year, where they benefit from the investments that our state and county governments have made in infrastructure, public spaces, and other essential services.

Currently, retirees who move to Hawai‘i do not have to pay state income tax on their pensions earned elsewhere in the US. Many of these retirees are also wealthy, as evidenced by their prevalence in affluent communities throughout the state. This means that the State is likely losing a considerable amount of tax revenue from a key demographic that—compared to the average local family that cannot dream of affording a home at median price—can more than afford to pay income taxes.

HB 1572 represents one common-sense path to increasing taxes on the wealthy, instead of shifting more of the burden to working families. In the process, it could generate revenue for desperately needed government investments.

Mahalo for your consideration.

HB-1572

Submitted on: 2/18/2024 3:38:42 PM

Testimony for FIN on 2/21/2024 2:00:00 PM

Submitted By	Organization	Testifier Position	Testify
Greg Misakian	Individual	Oppose	Written Testimony Only

Comments:

I oppose HB1572.

Fairness is allowing the voters to decide on major tax changes, not imposing the will of a group of legislators to make major changes to the Hawaii tax laws.

Greg Misakian

HB-1572

Submitted on: 2/20/2024 10:59:07 AM

Testimony for FIN on 2/21/2024 2:00:00 PM

Submitted By	Organization	Testifier Position	Testify
Gary Y.	Individual	Oppose	Written Testimony Only

Comments:

This bill would:

- Primarily affect lower to middle class residents who are on a fixed income or supplement their income from a mainland pension to afford to live here.
- Discourage locals that were born and raised in Hawaii and had to move to the mainland, from returning to Hawaii after vesting in a pension on the mainland.
- Discourage locals who had to move to the mainland from moving back to help their family members (kupuna and raising grandchildren).
- possibly result in the loss of tax revenue of people who moved to Hawaii to retire and will move away.
- possibly result in the loss of, or discourage, qualified and willing workers who can afford to live in Hawaii only because they have a pension as supplemental income, from staying or moving to Hawaii and addressing the staffing crisis throughout the state.