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LATE

SENATE COMMITTEE ON WAYS AND MEAN

COMMENTS OF THE DEPARTMENT OF TAXATION REGARDING HB 1092 HD1 SD1 RELATING TO TAXATION

COMMITTEE: WAM
DATE: APRIL 1, 2011
TIME: 9:00AM

POSITION: SUPPORT

This measure amends the current law that excludes employer-funded pension income from income tax. It treats employer-funded pension income like all other income, similar to that of the federal tax code. It starts in the 2011 tax year.

The Department of Taxation (Department) **supports** this measure.

PART I: TAXATION OF PENSION INCOME

FAIRNESS—This proposal makes taxation of pensioners more "even handed." Currently, retirees without employer-funded pensions are taxed on their retirement income, such as 401K, dividends, rental income, and other sources of income. It is a fair tax policy to treat the taxation of employer-funded retirement income similar to the self-funded retirement income.

The 1995-1997 and 2001-2003 Tax Review Commission recommended a phase in taxation of all pension income. Similarly, the 2005-2007 Tax Review Commission recommended conforming to the federal tax treatment of retirement income, excluding an annual base amount (*e.g.*: $50,000). Hawaii is one of only ten (or 20%) states that exclude all federal, state and local pension income from taxation[1]. Forty (or 80%) states taxed pension.

PRESERVE THE EXEMPTION FOR THOSE WITH MODEST INCOME—

This measure proposes to preserve the exemption of the pension income for those with a federal Adjusted Gross Income of less than:

- $100,000 for single or married filing separately;

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[1] The ten (10) states are as follows: Alabama, Hawaii, Illinois, Kansas, Louisiana, Massachusetts, Michigan, Mississippi, New York and Pennsylvania.

- $150,000 for head of household;
- $200,000 for joint returns or surviving spouse.

The Abercrombie-Schatz Administration proposes to preserve the exemption of the pension income for those with a federal Adjusted Gross Income of less than:

- $37,500 for single or married filing separately;
- $56,250 for head of household;
- $75,000 for joint returns or surviving spouse.

The thresholds chosen by the Administration took into consideration the average household income and average pension amount. According to the US Census Bureau, average Hawaii household income in 2008 was $66,701. According to the 2008 Federal Individual Income tax data, the average Hawaii residents' pensions and annuities taxed at the federal level was $22,686. According to the 2009 State Individual Income tax data, the amount of pensions taxed at the federal level but not by the State is $2.61 billion. This exemption currently benefits approximately 96,200 taxpayers, or only 18% of Hawaii resident taxpayers[2].

This measure will impact 3,988 taxpayers (or approximately 0.7% of Hawaii resident taxpayers), whereas the Administration's proposal will impact 43,520 taxpayers (or approximately 8.1% of Hawaii resident taxpayers).

REVENUE GAIN—This measure will result in an estimated revenue gain of $17.2 million per year for FY 2012 and thereafter, whereas the Administration's proposal will result in an estimated revenue gain of $112.3 million per year for FY 2012 and thereafter.

PART II: STATE TAX DEDUCTION

SOUND TAX POLICY—It is a fundamental tax policy to eliminate an absurd deduction allowed by the same source that is taxing the income. The current deduction is irrational and poor tax policy. It also simplifies the tax code. Only a handful (approximately 5) other states allow a state tax deduction for state income tax paid.

PRESERVES THE DEDUCTION FOR THOSE WITH MODEST INCOME—

This measure proposes to preserve the state tax deduction for those with a federal Adjusted Gross Income of less than:

- $75,000 for single or married filing separately;
- $112,500 for head of household;
- $150,000 for joint returns or surviving spouse.

[2] Total number of 2009 resident individual income tax returns is 535,996.

ABERCROMBIE-SCHATZ ADMINISTRATION'S PROPOSAL REPEAL THE DEDUCTION ENTIRELY BUT PHASES-OUT THE REPEAL FOR THOSE WITH MODEST INCOME—

Eliminates the deduction for the 2011 tax year for those earning:

- $75,000 or more for single or married filing separately;
- $112,500 or more for head of household or surviving spouse;
- $150,000 or more for joint returns.

Phases-out the deduction by reducing it over two taxable years for all others:

- 50% reduction for 2011
- 75% reduction for 2012
- 100% reduction for 2013.

This measure will impact 36,157 taxpayers (or approximately 6.7% of Hawaii resident taxpayers), whereas the Administration's proposal will impact 313,470 taxpayers (or approximately 58.5% of Hawaii resident taxpayers).

REVENUE GAIN—This measure will result in an estimated revenue gain of $33.2 million for FY 2012 and thereafter, whereas the Administration's proposal will result in an estimated revenue gain of $63.7 million for FY 2012, $79.0 million for FY 2013, $94.4 million for FY 2014 and thereafter.

TOTAL REVENUE GAIN FOR PART I AND II—This measure will result in an estimated total revenue gain of $50.4 million for FY 2012 and thereafter.

HAWAII GOVERNMENT EMPLOYEES ASSOCIATION
AFSCME Local 152, AFL-CIO

HGEA
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LATE

The Twenty-Sixth Legislature, State of Hawaii
The Senate
Committee on Ways and Means

Testimony by
Hawaii Government Employees Association
April 1, 2011

H.B. 1092, H.D. 1, S.D. 1 –
RELATING TO TAXATION

The Hawaii Government Employees Association, AFSCME Local 152, AFL-CIO opposes the purpose and intent of H.B. 1092, H.D. 1, S.D.1, which taxes the pension income with a federal adjusted gross income (AGI) of $100,000 for single filers, $150,000 for a head of household, $200,000 for joint filers, and makes the deduction for state taxes inoperable for corporate taxpayers and individual tax payers with a federal AGI of $75,000 for single filers, $112,500 for a head of household, and $150,000 for joint filers.

As this legislation is written, a pension tax and repeal of certain state deductions for individuals is unlikely to yield significant revenues. We implore the Legislature to consider a broad-based review of the tax code, in its entirety, instead of a piece meal approach to addressing the significant budget shortfall.

Respectfully submitted,

RyR

Randy Perreira
Executive Director