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STATE OF HAWAII DEPARTMENT OF TAXATION

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March 30, 2017

Colleen M. Takamura 2145 Wells Street, Suite 402 Wailuku, Hawaii 96793

Vaughn G.T. Cook 120 Pauahi Street, Suite 312 Hilo, Hawaii 96720

Re: Request for the Department of Taxation's Assistance

Dear Ms. Takamura and Mr. Cook:

We are responding to your letter dated February 27, 2017, requesting the Department of Taxation (Department) to assist the Tax Review Commission (TRC) with studies and statistics. The Department's responses to your requests are set forth below.

Studies Done for Prior Tax Review Commissions

The "Adequacy of Hawaii Tax Structure" and the "Study of the Progressive or Regressive Nature of Hawaii's Taxes" will be addressed by the Public Financial Management Group (PFM Group), the consultant retained by the TRC. To avoid duplication, the Department will not be updating these studies.

Due to limited data availability, the Department is not able to update the "Revenue Costs of Selected General Excise Tax and use Tax Exemptions and Deductions" in its entirety. However, it is able to update the costs for certain exemptions and deductions for activities where data is available.

The Department is able to update the following studies: (1) Study on the Question "Should Hawaii Replace Its Income and Franchise Taxes with an Increase in the General Excise Tax?" and (2) "Effect of Eliminating Income Tax for Those Below Poverty Level."

While the Department is able to update the study on "Effects of Eliminating Corporate Income Tax," as previously explained during the TRC meeting held on March 6, 2017, we will need to authorize staff overtime to update the study. The Department estimates that the necessary staff overtime will cost approximately \$10,000. Therefore, we would need authorization from the TRC to utilize its budget for this expenditure.

Information and Statistics

The Department is prepared to present an overview of the Tax System Modernization Program, including its progress and achievements, at the next TRC meeting to be held on April 24th.

The TSM program will be capturing information from forms such as the W-2 and 1099. The Department is aware of the identity theft and refund fraud threats and notes that it currently has procedures in place to address these issues. However, the Department is not able to provide any more detail regarding these procedures as it does not disclose specific details regarding audit, compliance, or security issues.

As the Department has previously explained, it does not have sufficient data on the General Excise Tax (GET) exemptions and deductions at present. The Department will update the TRC when it has complete and accurate data. The earliest that this data will be available is July 2017 as the tax year 2016 GET reconciliation returns (Form G-49) are due for calendar year taxpayers on April 20, 2017.

Under current law, the Department is required to report to the Legislature annually on GET exemptions for the: (1) wholesale rate, (2) retail rate, and (3) and foregone opportunities to export GET. Thus, your request for data on GET exemptions will also be published in this report.

The Department has reported corporate income tax revenues over the last ten years in its Annual Report, available on its website. For your convenience, we have attached Chart 1 from the report that shows corporate income tax revenues over the last ten years and have included a table showing corporate income tax as a percentage of total tax revenue.

The Department is able to provide the amount of deductions claimed by individuals for pensions exempt from Hawaii income tax for years 2012, 2013, and 2014. The statistics can be reported by year, filing status, and number of returns by the following federal adjusted gross income ranges:

- \$1 to \$50,000
- \$50,001 to \$75,000
- \$75,001 to \$100,000
- Over \$100,000

The Department is also able to provide the amount of taxes withheld on the disposition of real property by nonresident persons, which is commonly referred to as HARPTA, for the past ten years.

Department of Taxation Independent Study

Although not specifically requested in your letter, the Department is willing to provide a comprehensive study that examines the economic tradeoffs of major revenue sources for the State of Hawaii. The study will discuss the efficiency and the effects of the GET, individual income tax, corporate income tax, transient accommodation tax (TAT), and property tax. The study will also include a discussion of Hawaii's experience relative to other states. Lastly, it will include a list of different scenarios that show a range of tax rates amongst the different revenue sources that

are required to attain the current level of revenue collection relative to Total Personal Income and Gross State Product.

With its focus on issues related to efficiency and behavioral change, the proposed study will complement the work of PFM, which focuses on issues related to tax burden and incidence.

The Department proposes that the findings be shared in three presentations made to the TRC. The three tentative presentation topics would be 1) income tax, 2) GET, 3) and property tax and TAT. A final paper would be submitted to the TRC in August 2017 that would summarize the information shared in the presentation, providing additional information as needed.

The purpose of this study is to provide the TRC with information that will help it understand the inherent trade-offs of different tax scenarios for the State of Hawaii. The Department is able to make a formal proposal to the Committee in the April 24th meeting.

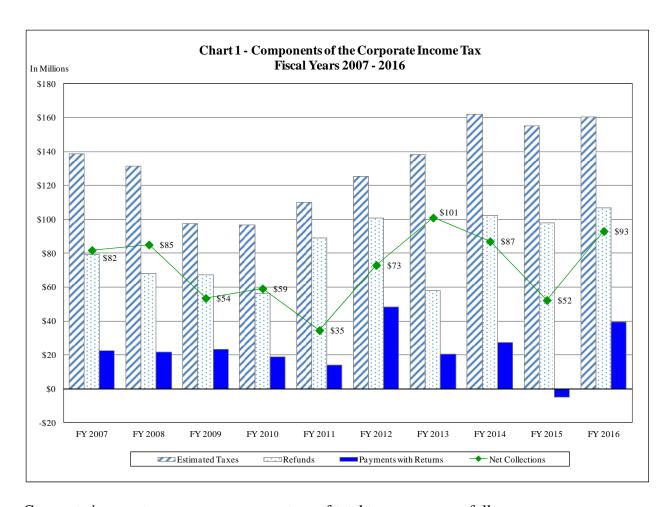
If you have any questions please contact Seth S. Colby, Tax Research and Planning Officer, at my office at (808) 587-1440.

Sincerely,

/s/

Maria E. Zielinski Director of Taxation

Attachment: Corporate Income Tax Revenues



Corporate income tax revenues as percentage of total tax revenues as follows:

| FY |
|------|------|------|------|------|------|------|------|------|------|
| 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 |
| 1.5% | 1.6% | 1.1% | 1.2% | 0.7% | 1.2% | 1.5% | 1.3% | 0.8% | 1.3% |