

Weekly Commentary

For The Week of September 18, 2011

SETTING THE AGENDA FOR TAX REFORM DEMANDS INFORMATION

By Lowell L. Kalapa

The eyes of lawmakers and legislative observers will turn to the deliberations of the latest Tax Review Commission which, after numerous delays, took up their work earlier this summer.

Fraught with the lack of interest or just plain unwillingness to serve on this constitutionally mandated study group, the Commission seems to be off to a rocky start basically putting the cart before the horse. With three meetings under their belt, the Commission is casting about looking to hire staff and a consultant to assist them.

Although that would sound logical, the Commission has yet to address what tax issues they would like to study. Their constitutional mandate is to review the state tax system with an eye on equity and efficiency. However, to date, they have yet to discuss anything about the state tax system. Some may argue that it is merely a process of getting organized and staffed so the Commission has the resources to conduct its review. The problem is that until the Commission knows where they will focus their review, it will be difficult to ascertain what sort of staff will be needed to help the Commission.

In its initial meeting some members called for a new tax structure “for the 21st Century.” Again, the problem with that is that until the Commission understands what the current tax structure looks like and how it works, they won’t be able to determine how to construct that new tax structure “for the 21st Century.” If nothing else, the Commission should start with the challenges that have faced the legislature and the state administration over the last five years since the previous Commission made its report to the governor and legislature.

One issue that should be very obvious to the Commission is the proposal to tax pension income. The department of taxation noted several times during the past legislative session that several of the previous Tax Review Commissions had recommended that the legislature address the issue. Will this Commission also address the issue of using tax incentives to encourage certain types of business activities such as the Act 221 tax credits for high technology investments?

How about all of those claims that Hawaii’s sales tax is too low or does Hawaii even, in fact, have a sales tax? Should the Commission look at the demands that Hawaii dump its general excise tax in favor of adopting a retail sales tax like those found on the mainland? And what about the proposals that attempt to tax Internet sales and the possibility of joining the effort to buy into the Streamline Sales Tax Project?

Although it has been more than twenty years since the issue of who pays Hawaii’s taxes has been studied, it might be time to do so again. Has the change in the economic base of the state altered who pays Hawaii’s taxes? In 1989 that Tax Review Commission was told that about 20% of the general excise tax is paid by visitors with roughly another 10% paid by nonresident owners of businesses and

properties in Hawaii. With the struggles of the visitor industry lately, has that number gone up or down for visitors?

And what about the changes made by this past session of the legislature? Of the dozen or so exemptions from the general excise tax that were suspended for the next two years, how many will have an impact on the cost of living and doing business in Hawaii? In fact, the Tax Review Commission needs to ask the question of how the state's tax structure affects the economic vitality of the state and how it will affect future growth.

Further, the Commission needs to address recent legislative action to eliminate the deductibility of state and local income and sales taxes for businesses and certain high-income individuals. Similarly, lawmakers imposed a temporary limitation on itemized deductions for certain high-income individuals over the next four years. Considering there is a policy set in law that directs conformity to the federal income tax Code to minimize differences between the federal and state laws, the Commission should address this divergence from that policy.

Finally, Hawaii has for years been known for having one of the lowest thresholds before people start paying income taxes. That means people who would otherwise be considered at poverty level are paying Hawaii state income taxes on what little taxable income they receive. One would think that the Tax Review Commission would be the perfect venue for a discussion of that anomaly. Yes, there is a lot for the Tax Review Commission to review without even looking to create a brand-new tax structure for the 21st Century and it starts with a review of the current system.

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