

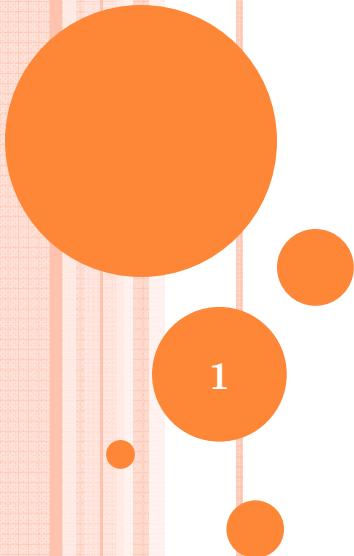


TAX ADEQUACY

**2010-2013 Hawaii Tax Review
Commission**

Presented by Dr. Donald Rousslang

August 29, 2012



SUMMARY OF THE METHOD

Similarities with the study by the PFM Group

- The study on tax adequacy by Joshua Fujino and me is similar to the study being done by the PFM Group.
- Both studies examine the General Fund budget and use Council on Revenues forecasts for the revenue side of the budget.
- Both studies use actuarial studies to project the future costs of pensions and health care benefits for retired State workers and both use State projections for the future cost of the Medicaid program.
- Both studies also look at the budget under the current payment system and under an accrual method of accounting.

SUMMARY OF THE METHOD

Differences from the study by the PFM Group

- The main difference between the studies is the method used to project future spending on current government services, excluding payments for pensions and health care benefits for retired State workers and the cost of the Medicaid program.
- The PFM Group examined spending by detailed line item and used projections by State agencies of the spending that would be needed to maintain the current level of services.
- Josh and I assumed that the current level of spending provided adequate government services and that future spending would be adequate if it grew in tandem with TPI. The approach is not as arbitrary as it may first appear. The bulk of the cost of current government services is for compensation of State workers. If their compensation is to be kept on a par with that of workers in the private sector, then we might reasonably expect the cost of maintaining a constant level of government services to grow with total personal income.

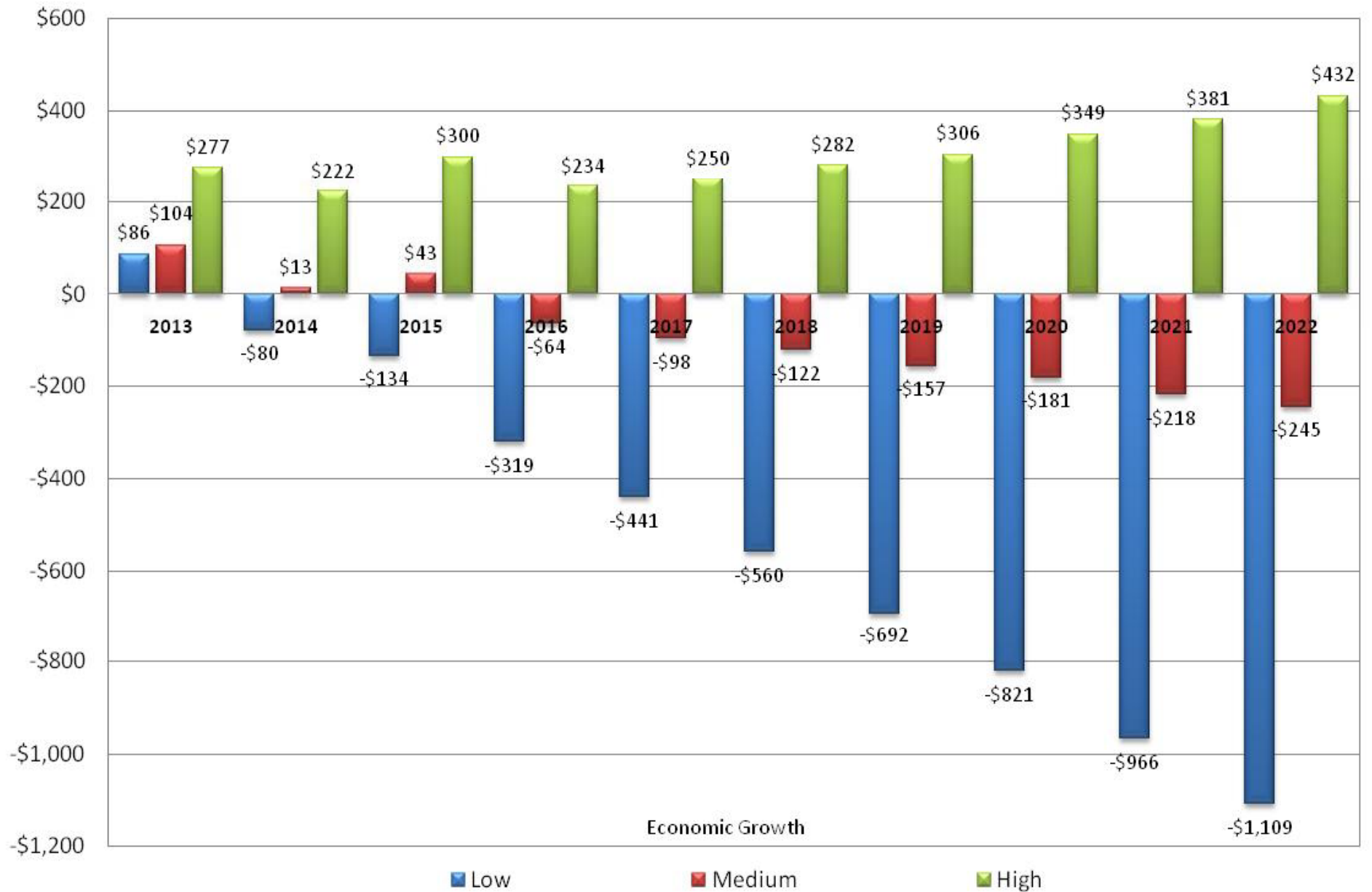
SUMMARY OF THE RESULTS

- The answer to the question "How much government services do we need?" is a matter of opinion.
- Both the study by the PFM Group and the one by Josh and me assume that the current level of government services is adequate.
- This view is not universal. During confirmation hearings for the Commission members, Senator Chun Oakland argued that current spending is too low and that we should go back to earlier, higher service levels.

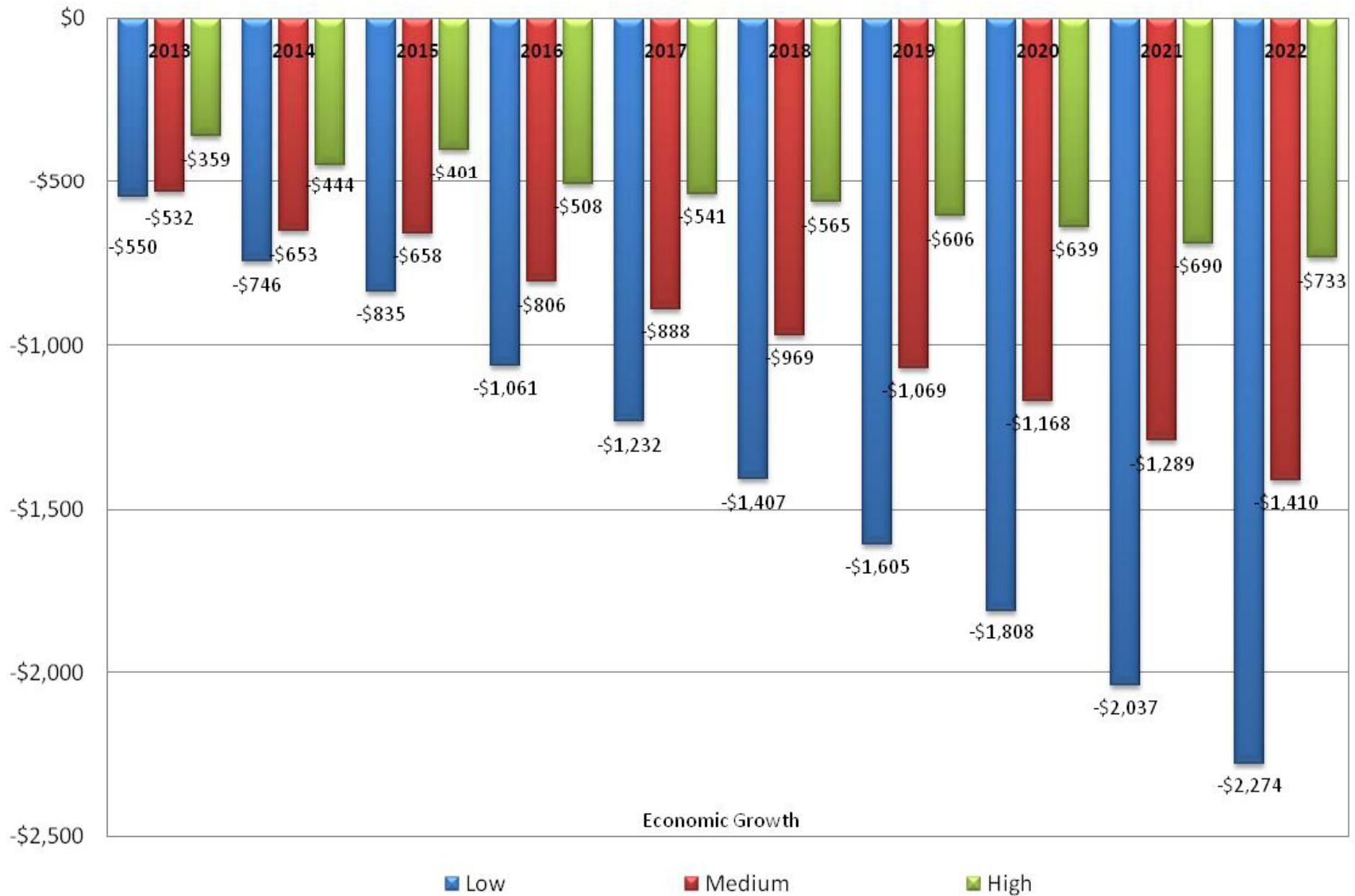
SUMMARY OF THE RESULTS

- We find that by our definition of adequate government spending, the current tax structure will be inadequate by 2016 under all but the most optimistic of our scenarios.
- If accrual accounting is used, the tax structure already falls badly short of providing enough revenue to cover present needs, and the annual shortfall may exceed \$2 billion by 2022.
- The results are summarized in Table 7 of our report (Figures 1 and 2 of this presentation).
- In producing the estimates, I updated revenue collections to fiscal year 2012, but the estimates for spending from the General Fund have not been updated since the draft we produced in February 2012.

**Figure 1. Estimates of the Annual Budget Surplus or Deficit:
Non-Accrual Method**



**Figure 2. Estimates of the Annual Budget Surplus or Deficit:
Accrual Method**



THANK YOU

