Who Pay’s Hawaii’s Taxes

TAX REVIEW COMMISSION

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DEPARTMENT OF TAXATION

What is Your Rationale for Taxes?

Spending money responsibly is much harder than raising money!

Preference for a market economy assumes that private actors are better at allocating capital than governments

- Imposing a tax implies that you are taking the spending power away from the individual *(hubris of taxation)*
  - Who would spend Bill Gates' fortune better? Bill Gates or U.S. Congress?

- Raise tax if,

ROI > cost of taxation

- Lower tax if,

ROI < cost of taxation

Three Questions

1) *What are you going to pay for? (depends on ROI: NOT purview of TRC)*
  - What are your assumptions in terms of ROI or needs?

2) *How much is the tax? (cost of taxation: Purview of TRC)*
  - What are your assumptions regarding behavior?

3) *Who is going to pay? (cost of taxation: Purview of TRC)*
  - What are your assumptions regarding behavior?
  - What are your assumptions about who should pay?

How is Hawaii's tax burden distributed between residents and non-residents?

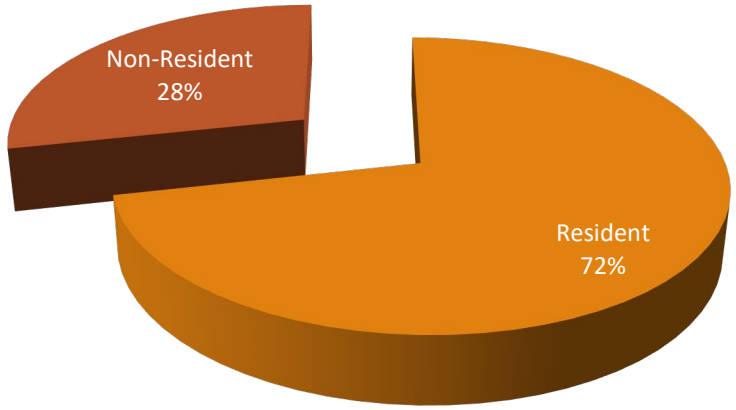
Non-Residents Pay a Roughly a Third of Hawaii's Tax Collections

Incidence of Residents and Non-Residents by Tax Type

	FY18 ($ mil)	Resident ($ mil)	Non-Resident ($ mil)	Resident (%)	Non-Resident (%)
State					
General Excise and Use Taxes	3,396	2,438	958	71.8%	28.2%
Individual Income Tax	2,492	2,315	177	92.9%	7.1%
Corporate Income Tax	69	28	41	40.7%	59.3%
Transient Accommodations Tax	555	44	510	8.0%	92.0%
Other Taxes	1,101	865	235	78.6%	21.4%
Sub-total	**7,613**	**5,691**	**1,921**	**74.8%**	**25.2%**
Local					
County Surcharge	282	202	79	71.8%	28.2%
Public Service Companies	112	104	8	92.8%	7.2%
County Fuel Tax	88	73	15	83.0%	17.0%
Property Tax (Residential)	1,003	714	289	71.2%	28.8%
Property Tax (non-Residential)	2,771.7	1,434	1,338	51.7%	48.3%
Sub-total	**4,256**	**2,526**	**1,730**	**59.4%**	**40.6%**
Total Tax Burden	**11,869**	**8,218**	**3,651**	**69.2%**	**30.8%**

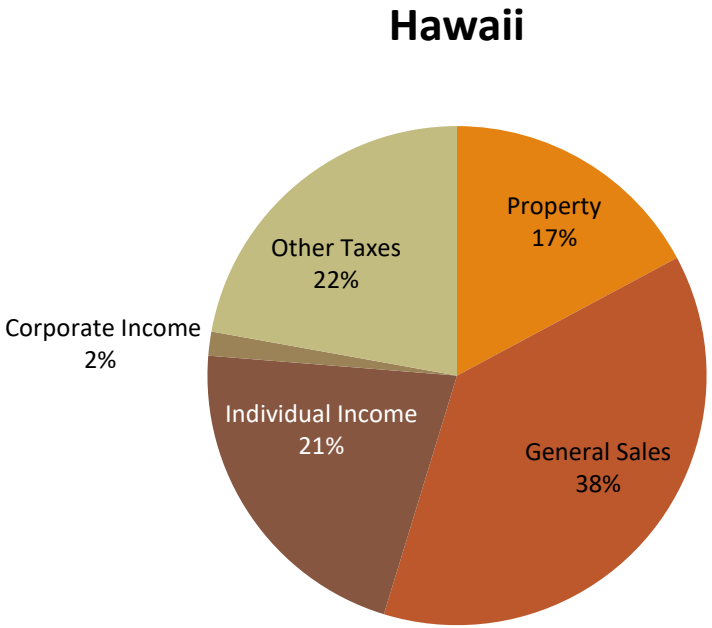
Exported taxes materially reduce the burden on residents

Tax Burden	Total	Per Capita
Total Tax	$9,918 M	$7,027
Tax/ Total Personal Income	13.1%	13.1%
Resident Total Tax	$7,145M	$5,029
Resident Tax/ Total Personal Income	9.3%	9.3%



How is Hawaii's tax burden distributed among income levels?

Revenue system highly reliant on GET and Individual Income Tax



Measuring Progressivity

Regressive – lower income people pay a higher percentage of their income in taxes

Neutral – everybody pays the same percentage of income in taxes

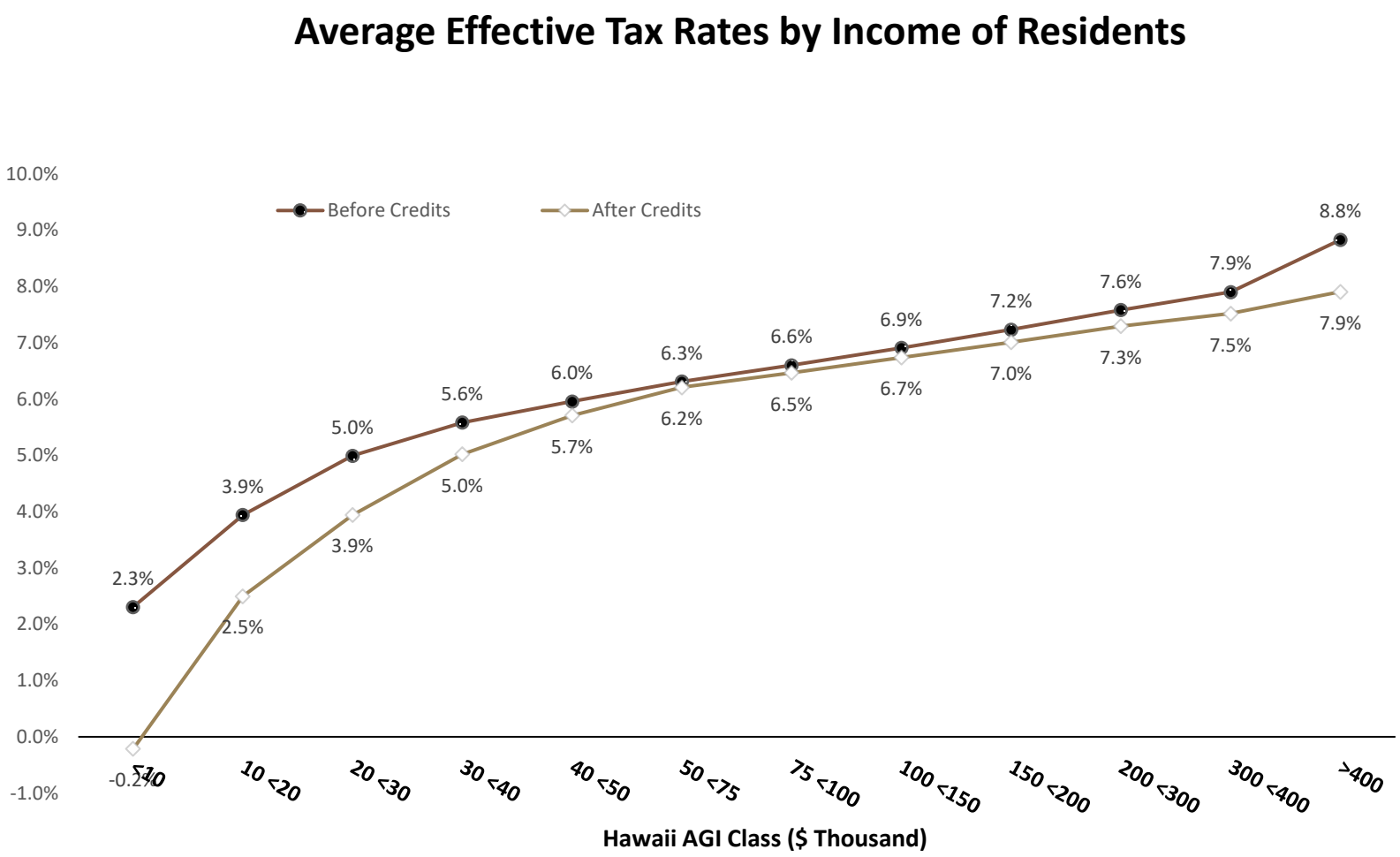
Progressive – higher income pay a larger percentage of their income in taxes

$$\% \text{ Tax Burden} = \frac{\text{Tax}}{\text{Income}}$$

Low Income

High Income

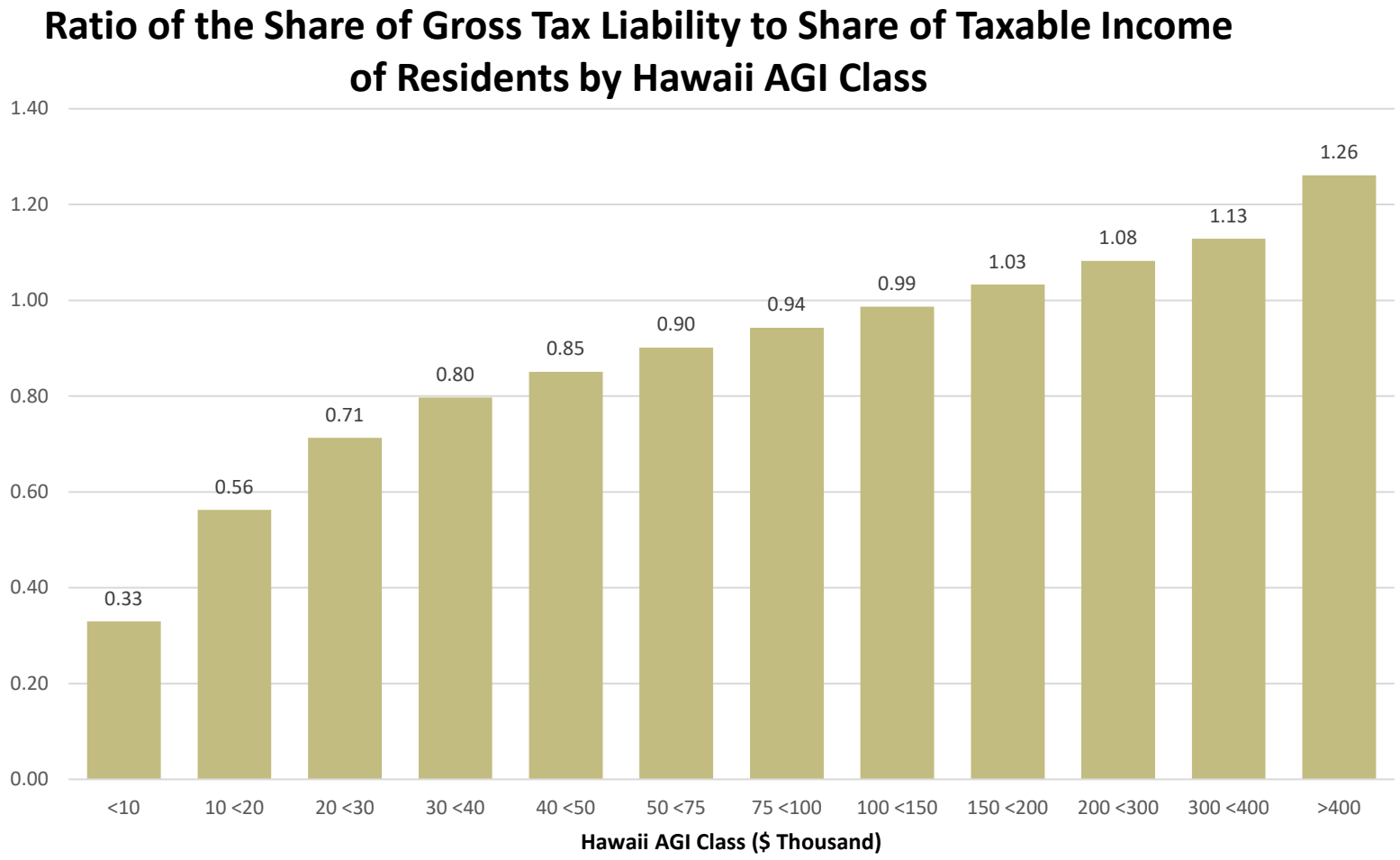
Individual Income Tax



Hawaii has a progressive individual income tax structure

Source: 2018 Income Tax Returns

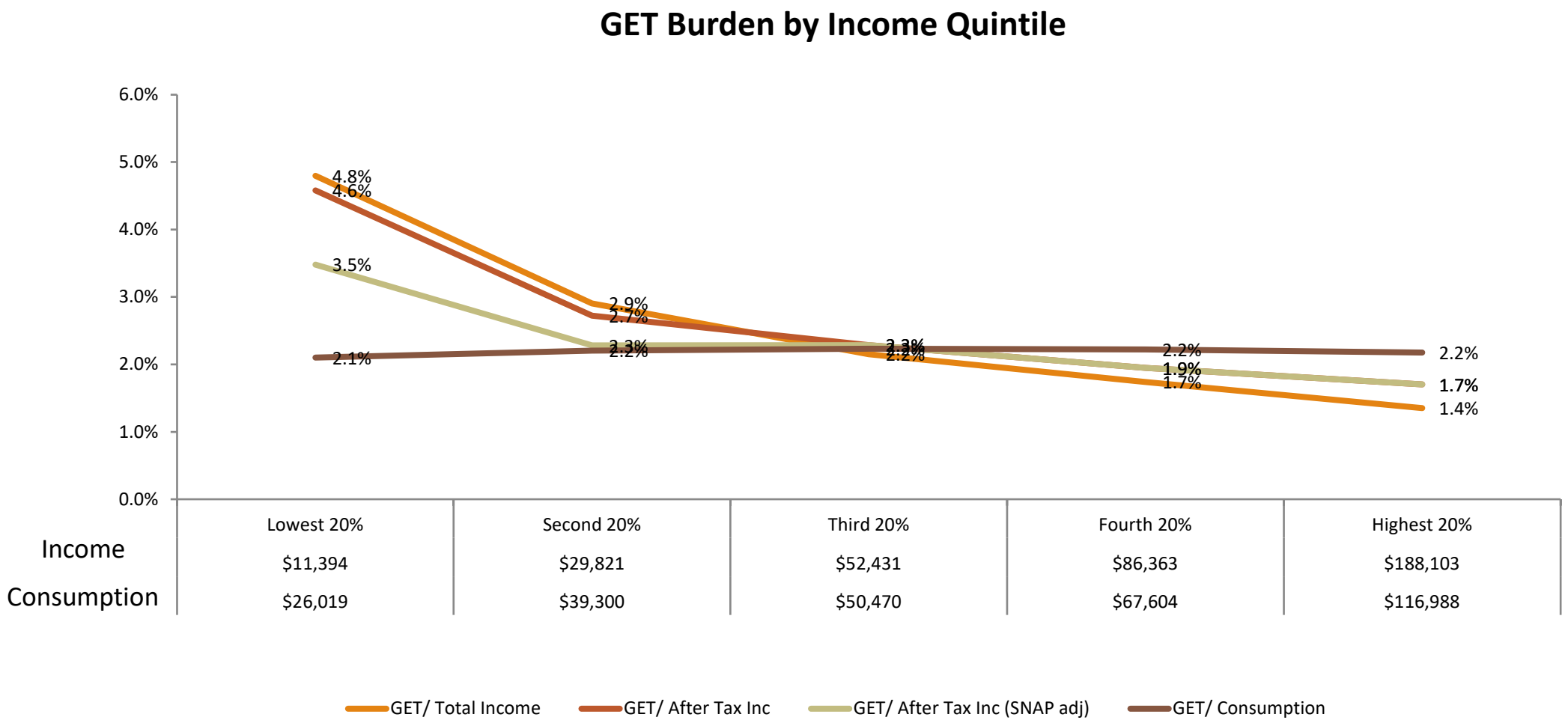
The highest income earners pay a higher share in taxes than their share of income



Source: 2018 Income Tax Returns

General Excise and Use Tax

GET is slightly regressive to neutral depending on the perspective



Source: Author's Calculations (Consumer Expenditure Survey)

Assumption: GET on rents is born by capital owner

Putting It All Together

Creating a comprehensive approach to measuring the state tax burden by quintile

Estimate taxes for median HH using micro simulations across income quintiles from CES

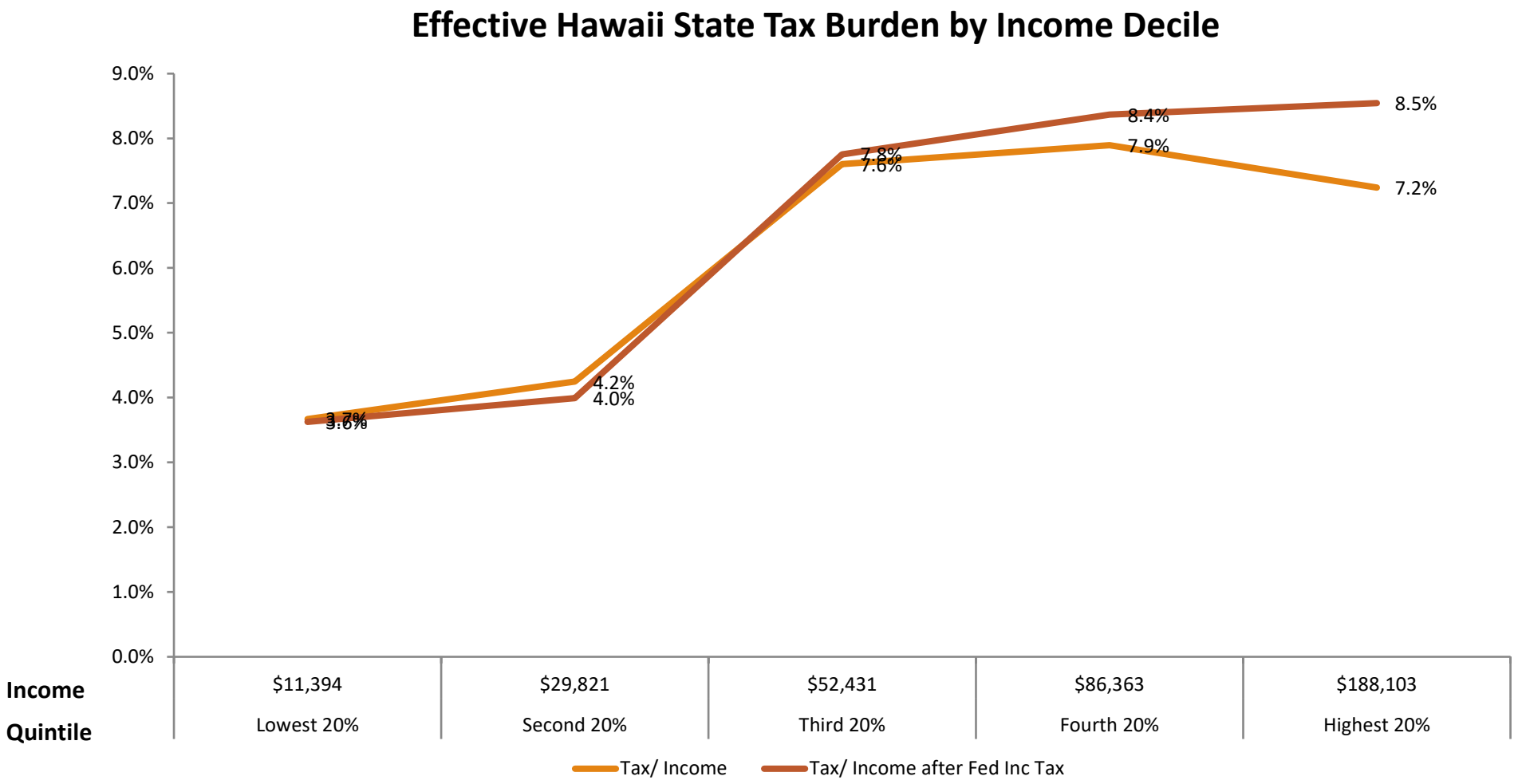
- Only include state taxes directly born by consumer (excise taxes, motor vehicle tax, personal income tax)
- Does not include CIT, PSC, Franchise, Estate, Unemployment, Insurance Prem, Conveyance (6.6% of collections)
- Assume GET on rent is born by capital owner

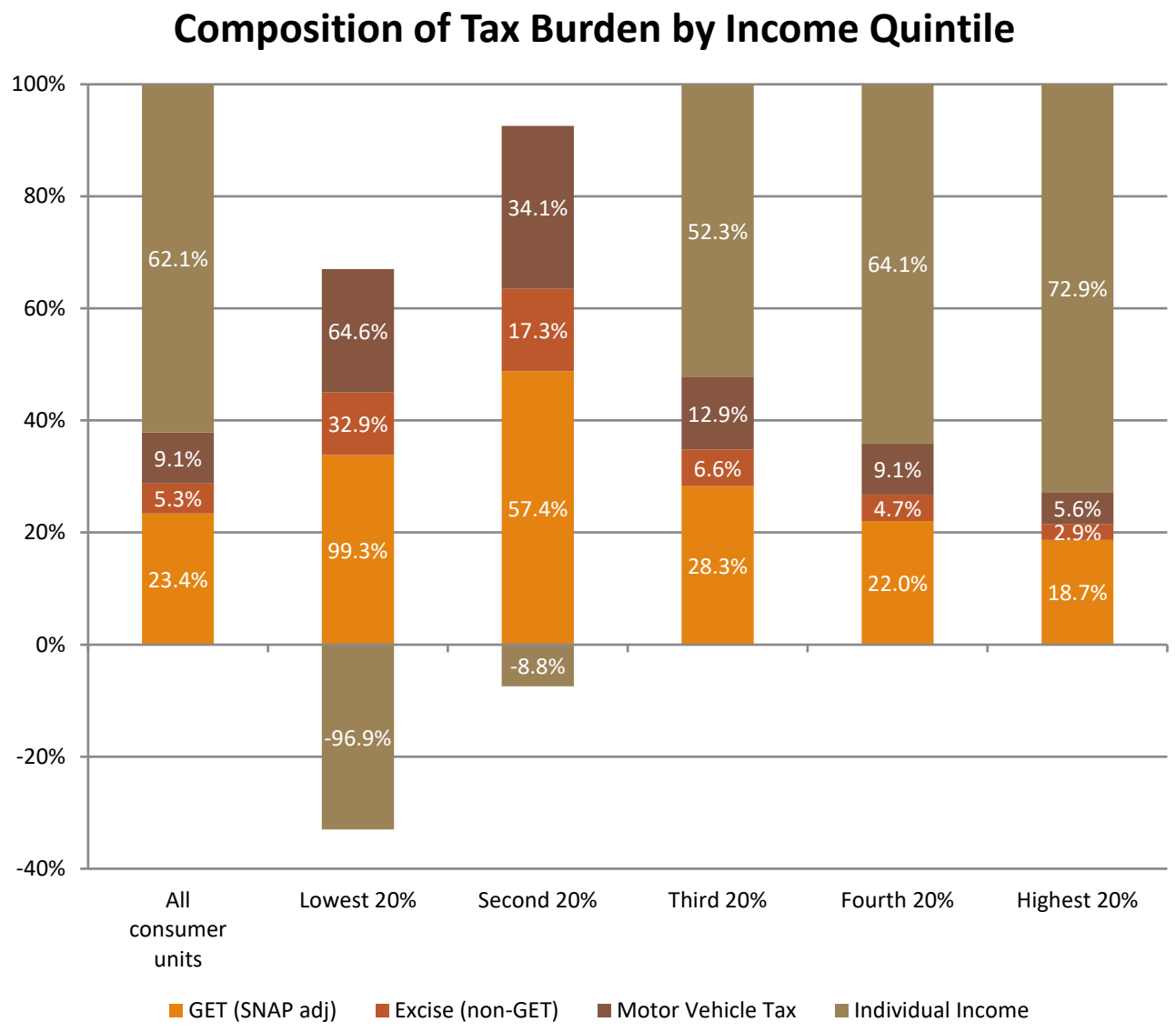
Tax Type	Estimation Methodology
GET (SNAP adj)	Consumer Expenditure Survey by quintile. Honolulu Adjusted
Liquor	Consumer Expenditure Survey by quintile. Honolulu Adjusted
Tobacco	Consumer Expenditure Survey by quintile. Honolulu Adjusted
Fuel	Consumer Expenditure Survey by quintile. Honolulu Adjusted
TAT	Consumer Expenditure Survey by quintile. Honolulu Adjusted
Motor Vehicle Tax	Consumer Expenditure Survey by quintile. Honolulu Adjusted
Personal Income Tax	Estimate state taxes for households (File Jointly, Standard deduction by HH size), Credits available: Refundable EITC, Food Credit, Low Income Rental Credit. Renters

Estimated tax burden by income quintile

	All consumer units	Lowest 20%	Second 20%	Third 20%	Fourth 20%	Highest 20%
Pre-Tax Income	$ 73,573	$ 11,394	$ 29,821	$ 52,431	$ 86,363	$ 188,103
Federal AGI	$ 66,951	$ 10,369	$ 27,137	$ 47,712	$ 78,590	$ 171,174
After Fed Tax Income	$ 67,102	$ 11,528	$ 30,316	$ 51,424	$ 81,474	$ 159,435
Consumption	$ 60,060	$ 26,019	$ 39,300	$ 50,470	$ 67,604	$ 116,988
People in HH	2.5	1.6	2.2	2.5	2.9	3.1
GET	$ 1,317	$ 415	$ 726	$ 1,128	$ 1,502	$ 2,545
Total Excise	$ 299	$ 138	$ 218	$ 261	$ 322	$ 389
Motor Vehicle Tax	$ 513	$ 270	$ 432	$ 513	$ 621	$ 756
Individual Income	$ 3,496	$ (405)	$ (111)	$ 2,085	$ 4,371	$ 9,931
Total Tax	$ 5,625	$ 418	$ 1,266	$ 3,987	$ 6,816	$ 13,621
GET/Total Tax	23.4%	99.3%	57.4%	28.3%	22.0%	18.7%
Other Excise/Total Tax	5.3%	32.9%	17.3%	6.6%	4.7%	2.9%
MVT/ Total Tax	9.1%	64.6%	34.1%	12.9%	9.1%	5.6%
PIT/ Total Tax	62.1%	-96.9%	-8.8%	52.3%	64.1%	72.9%
Total Tax	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Tax/ Income	**7.6%**	**3.7%**	**4.2%**	**7.6%**	**7.9%**	**7.2%**
Tax/ Income after Fed Inc Tax	8.4%	3.6%	4.0%	7.8%	8.4%	8.5%

Hawaii's state tax system is progressive measured directly





Excise and MVT comprise a large portion of the burden for low-income taxpayers

Taking a Closer Look at ITEP Study

- *Income should not be confused for consumption*
  - Use or pretax income has impact on metrics
  - Definition of income leaves out tax credits and in-kind transfers in the definition of income
- *Sales & excise on business over-stated compared to other studies*
- *Personal income tax rates lower than DOTAX findings*
- *With a strong social safety net, one might WANT the tax/ income rate to be highest for lower income individuals*

HAWAII State and Local Taxes (cont.)

TOTAL TAX

Share of Family Income

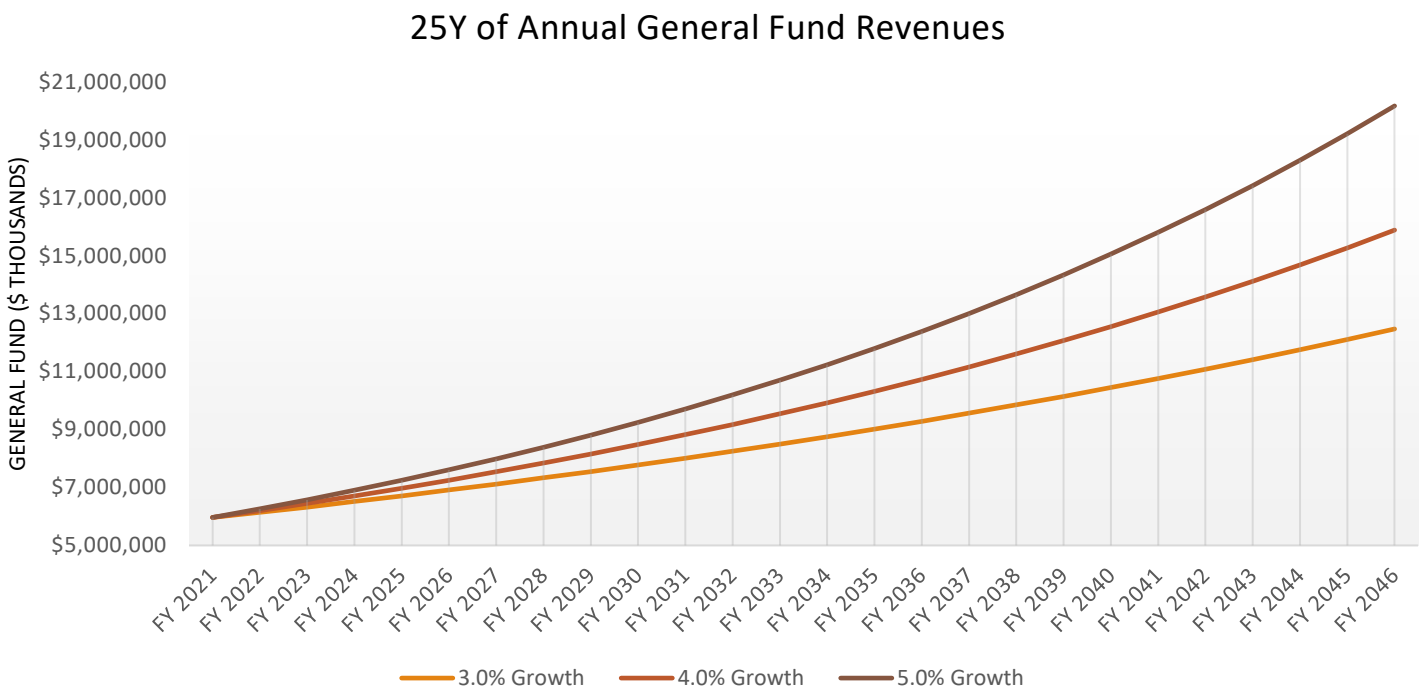
INCOME GROUP	LOWEST 20%	SECOND 20%	MIDDLE 20%	FOURTH 20%	NEXT 15% (TOP 20%)	NEXT 4% (TOP 20%)	TOP 1% (TOP 20%)
INCOME RANGE	Less than $20,000	$20,000 to $36,000	$36,000 to $55,700	$55,700 to $95,100	$95,100 to $213,800	$213,800 to $457,100	over $457,100
AVERAGE INCOME IN GROUP	$10,200	$26,700	$45,000	$72,500	$134,500	$299,700	$984,200
SALES & EXCISE TAXES	**10.5%**	**8.2%**	**6.2%**	**4.9%**	**3.6%**	**2.2%**	**1.2%**
General Sales—Individuals	4.7%	3.8%	2.9%	2.3%	1.6%	1.0%	0.5%
Other Sales & Excise—Ind.	2.1%	1.3%	0.9%	0.7%	0.5%	0.2%	0.1%
Sales & Excise on Business	3.8%	3.1%	2.4%	1.9%	1.5%	0.9%	0.6%
PROPERTY TAXES	**3.8%**	**2.2%**	**1.9%**	**1.9%**	**1.5%**	**1.5%**	**1.4%**
Home, Rent, Car—Individuals	3.8%	2.1%	1.9%	1.8%	1.3%	1.0%	0.4%
Other Property Taxes	0.1%	0.1%	0.1%	0.1%	0.2%	0.5%	1.0%
INCOME TAXES	**0.6%**	**2.6%**	**3.4%**	**4.2%**	**4.3%**	**5.5%**	**6.3%**
Personal Income Tax	0.6%	2.6%	3.4%	4.1%	4.3%	5.5%	6.2%
Corporate Income Tax	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.1%
TOTAL TAXES	**15.0%**	**13.0%**	**11.6%**	**11.0%**	**9.4%**	**9.2%**	**8.9%**

Individual figures may not sum to totals due to rounding.

ITEP TAX INEQUALITY INDEX

According to ITEP's Tax Inequality Index, which measures the impact of each state's tax system on income inequality, **Hawaii has the 15th most unfair state and local tax system** in the country. Incomes are more unequal in Hawaii after state and local taxes are collected than before. (See Appendix B for state-by-state rankings and the methodology section for additional detail on the index.)

Growth versus Taxation



The long-term average growth rate has a large effect on annual collections

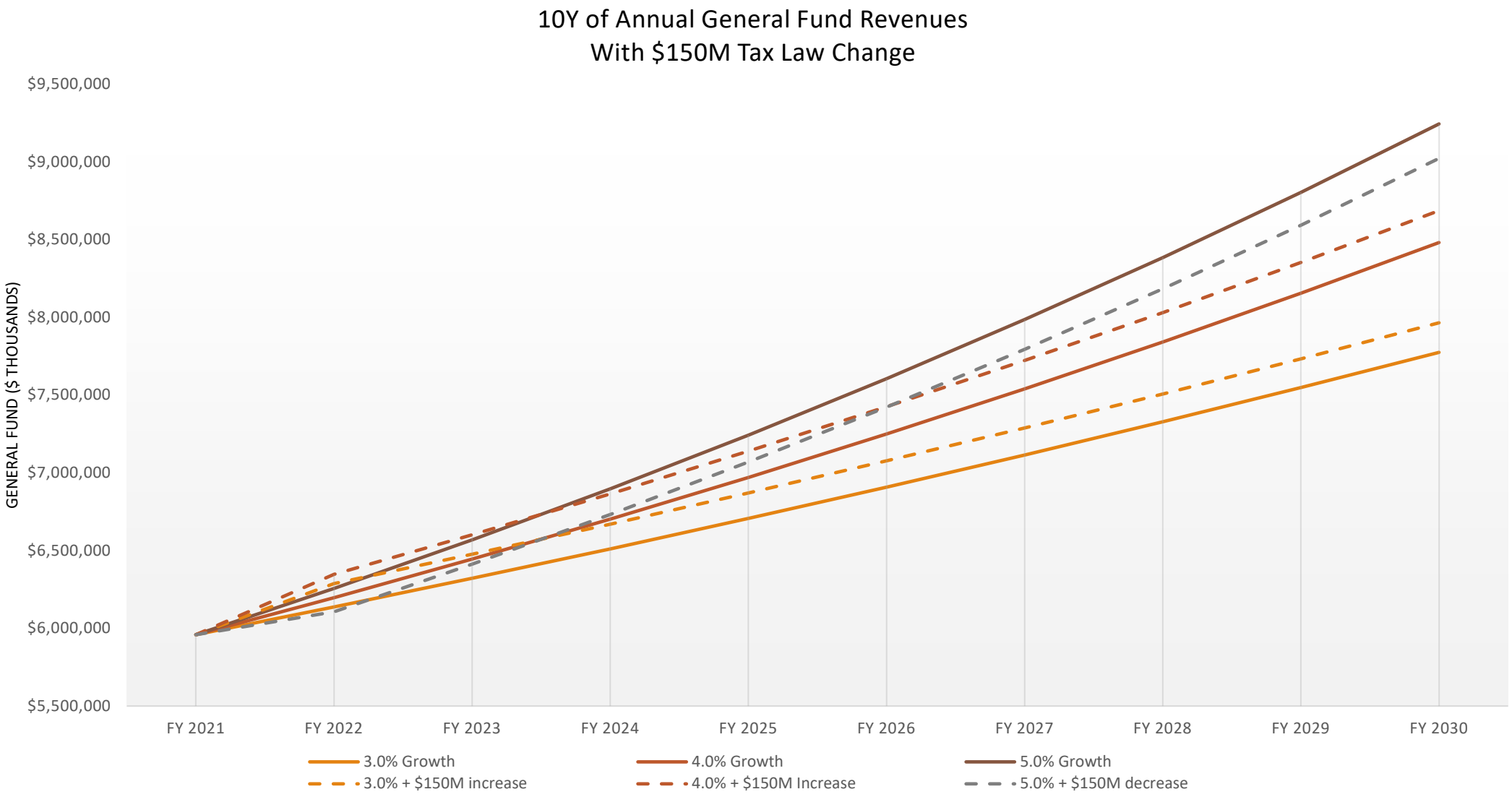
Average General Fund Growth Rate from 2001 to 2019

4.8%

Growth Rate Scenarios on General Fund Revenues ($ millions)

Growth Scenario	Cumulative			Estimated FY 2046 Annual	
	10 Year	20 Year	25 Year	1% of GF	Revenue
3.0%	$70,355,323	$154,145,499	$223,755,263	$124,755	$12,475,523
4.0%	$74,398,416	$171,470,702	$258,067,795	$158,841	$15,884,064
5.0%	$78,691,045	$191,061,111	$298,594,957	$201,772	$20,177,187
Differences					
3% vs 4%	$4,043,092	$17,325,203	$34,312,532	$34,085	$3,408,541
3% vs 5%	**$8,335,722**	**$36,915,612**	**$74,839,694**	**$77,017**	**$7,701,664**
4% vs 5%	$4,292,629	$19,590,409	$40,527,162	$42,931	$4,293,123

Over long term, growth is more important than tax law changes



Over long term, growth is more important than tax law changes

General Fund Scenarios with $150 million tax law change

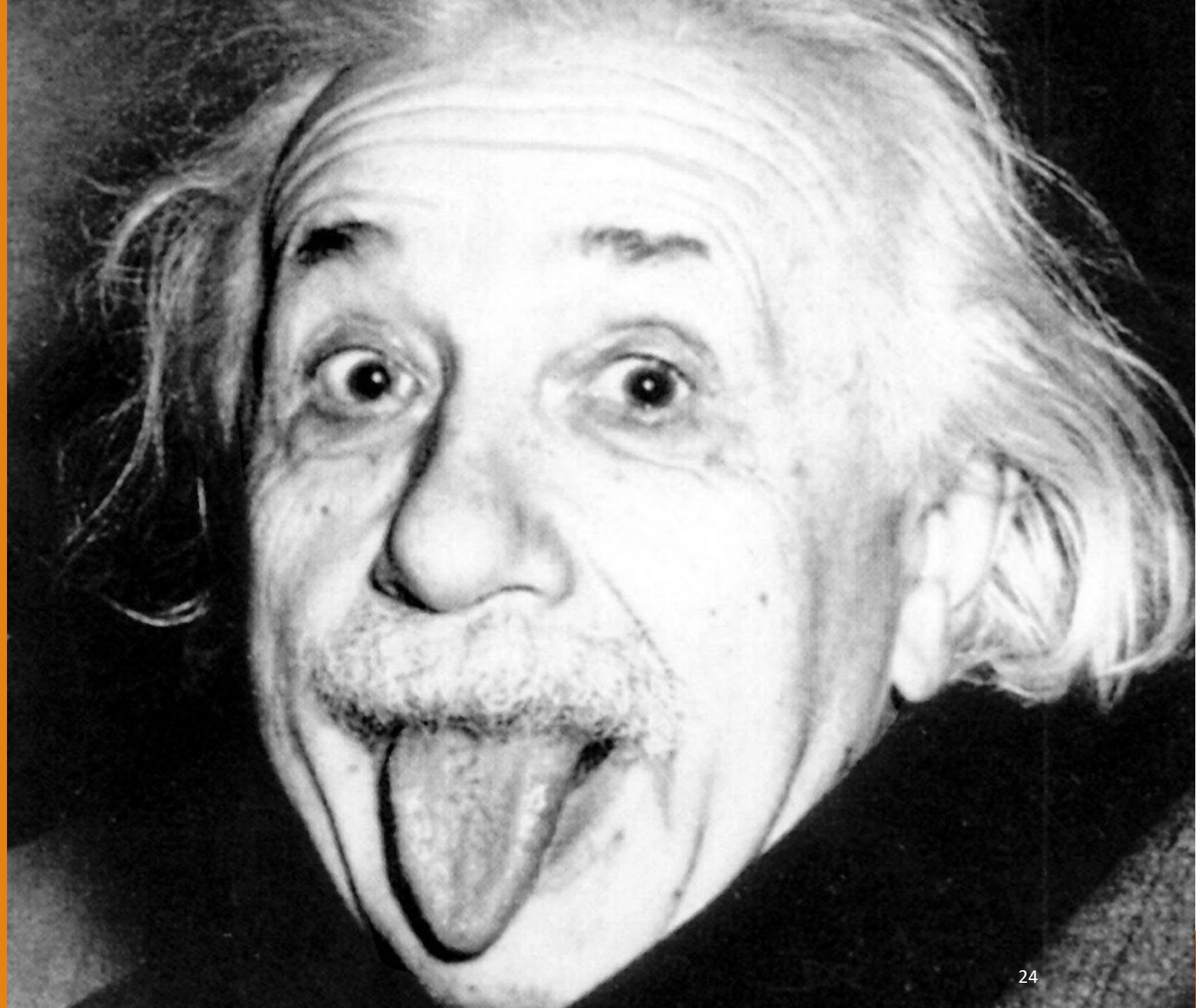
Growth Scenario	Cumulative			Estimated FY 2046 Annual	
	10 Year	20 Year	25 Year	1% of GF	FY 2046
3.0%	$70,355,323	$154,145,499	$223,755,263	$124,755	$12,475,523
4.0%	$74,398,416	$171,470,702	$258,067,795	$158,841	$15,884,064
5.0%	$78,691,045	$191,061,111	$298,594,957	$201,772	$20,177,187
$150M Tax Change					
3.0% + $150M increase	$72,074,905	$168,937,551	$229,224,152	$127,804	$12,780,442
4.0% + $150M Increase	$76,199,332	$188,992,957	$264,314,681	$162,686	$16,268,559
5.0% + $150M decrease	$76,804,361	$201,910,572	$291,435,892	$196,934	$19,693,422
Compared to 4.0% Growth					
3.0% + $150M increase	-$2,323,510	-$15,588,694	-$28,843,642		-$3,103,622
4.0% + $150M Increase	$1,800,916	$4,466,712	$6,246,886		$384,496
5.0% + $150M decrease	$2,405,945	$17,384,327	$33,368,097		$3,809,358

Potentially Apocryphal Quote of the Day:

Questioner: “What is the most powerful source in the universe?”

Albert Einstein: “Compound Interest”

Lesson: Add “thinking exponentially” thinking to your intellectual toolbox. Most people conceive the world arithmetically



Mahalo