

TAX REVIEW COMMISSION

MINUTES FOR THE SIXTEENTH MEETING OF THE
TAX REVIEW COMMISSION
HELD AT 830 PUNCHBOWL STREET
DEPARTMENT OF LABOR & INDUSTRIAL RELATIONS ROOM 310-313
IN THE CITY AND COUNTY OF HONOLULU
STATE OF HAWAII, ON TUESDAY, OCTOBER 3, 2017 AT 1:00 PM

The Commissioners of the Tax Review Commission (TRC) met at the Department of Labor & Industrial Relations Conference Rooms in the City and County of Honolulu, State of Hawaii, on October 3, 2017.

Members Present: Colleen Takamura, Chair
Vaughn Cook, Vice-Chair
John Knox
Nalani Kaina
Billy Pieper
Raymond Blouin

Members Absent: Dawn Lippert

Staff: Seth Colby, Titin Sakata and Noe Kaawa

Others: Randall Nishiyama, Department of the Attorney General
Randy Bauer, PFM Group Consulting LLC
Donald Rousslang, Department of Taxation
Wayne Yoshioka, KHPR
Tom Yamachika, Tax Foundation of Hawaii
Dane Wicker, State Senate Ways & Means
Robert Nishimoto, State Senate Ways & Means
Erin Conner, State Senate Ways & Means
Janos Palko, State Senate Ways & Means
Katarina Ruiz, CAN
Peter Fritz

CALL TO ORDER:

Chair Takamura called the meeting to order at 1:00 pm.

Chair Takamura said she was taking the meeting out of order and began with the presentation on the Principles of Sound Tax Policy by Dr. Rousslang.

PRESENTATION ON THE PRINCIPLES OF SOUND TAX POLICY BY DOTAX:

Dr. Rousslang said before he started, he wanted to ask rhetorical questions and wanted everyone to answer them quietly. He said an important purpose of the principles was to reduce costs of taxation, so which of the following cost of taxation was greater? Cost of tax administration including the department's budget, cost of tax compliance or cost of the economic distortions that were inevitably caused by taxes. The benefits principle says that those who get the benefits of a government service should be the ones that pay for it, was that principle meant to improve fairness or meant to improve efficiency? Last was the graduated tax rates like the individual income tax, the income was taxed at a graduated rate, was that efficient?

Principles of Sound Tax Policy presentation by Dr. Don Rousslang

https://tax.hawaii.gov/stats/a9_2trc

Chair Takamura said regarding the sound tax policy, there's also transparency and accountability, was that also included?

Dr. Rousslang said simplicity promotes transparency and in his view, it was another way of saying simplicity.

Chair Takamura asked what about accountability?

Dr. Rousslang said if people understood the tax code, they could hold accountable those who were responsible for it. What she was talking about was audit and that was part of tax administration.

Commissioner Knox said PFM also addressed those issues and he was concerned. He asked Dr. Rousslang if he saw any contradictions at all between his approach and PFM's or was it just a reworking of similar concepts.

Dr. Rousslang said he didn't think there was any contradiction between his list of principles of sound tax policy and any other list.

Mr. Bauer said there wasn't anything Dr. Rousslang said that he would necessarily disagree with except for the issue of volatility. He believed Dr. Rousslang recognized too from the discussion of tax adequacy was that there's a practical ramification to a tax structure. It's got to raise enough revenue to do the things that policymakers believe were necessary.

He said as he previously mentioned, there was no perfect tax and they all have some kind of burden on the economy but what states had found were some of the volatile tax structures were also those that could generate what would be considered sufficient revenues particularly when the economies started doing better. There's some ebb and flow that policymakers had to be able to deal with and got to put enough revenue aside when things were good for when things get bad, and tax structures can't necessarily do that that's up to the budget people.

Commissioner Knox said he was just concerned about clarities and consistencies, and appreciated the assurance.

Commissioner Cook asked if there were any trends in the U.S. towards emphasis of these tax policies, for example, trends more towards horizontal equity in the push towards a flat tax.

Dr. Rousslang said his understanding of flat taxes was primarily for efficiency but it made a sacrifice in what some people consider fairness. Although, when you talk about fairness to an economist, he's lost.

Mr. Bauer said if you benchmark both individual income tax systems, there hasn't been a change. The number of states that have a flat individual income tax was the significant minority and he didn't know if that was going to change. He said for the same kind of practical issues of what was discussed earlier in terms of what happens to a structure when things were going really good, a progressive structure would generate a lot more revenue as the people at the top end do really well.

Dr. Colby said he attended a conference of tax administrators and he thought there were a couple of trends that came up. One was the corporate income tax, people were moving away from that and it was generating less and less revenue from that which was a small tax for Hawaii in proportion to other states. The second was a push away from efficiency to simplicity. He said there was a lot more interest in gross receipts tax, a lot more interest in taxes like the GET that were just easier to collect and generates large amounts of revenue that was simple rather than taking it apart. He said there was a couple more states adopt bigger thing especially as the sales tax collected on the national level isn't developing sufficient levels of revenue.

He said in terms of all this which had nothing to do with sufficiency, but other things to take into consideration was what was going to happen at the national level and that would change for this TRC. It was hard to make any recommendations without knowing what was happening at the federal level. The federal level usually represents a larger portion of the tax burden, and states would have to react to that one way or another, and it would be very difficult to do tax planning and tax suggestions.

Mr. Bauer said had one more comment to add related to the corporate income tax. He said first of all, understanding that corporations, particularly large multi-state corporations were extremely adept at figuring out where and how they could structure a company to pay the least amount of corporation tax and states also contributed too. It used to be the classic three factor system for apportionment for multi-state corporations of sales, payroll and property. Now, the single largest method of apportionment was just a single factor, sales and the second most common apportionment was double weighted in sales and those were the kind of ways states decided they were going to structure their corporate income tax, but at the same time corporations pay a lot of taxes not just corporate income tax. He said he wasn't trying to minimize the fact they pay a lot of tax and in Hawaii because of the GET, it's even more so then in some other states.

Chair Takamura asked Mr. Bauer if he could tell her how many states had gone away from the three part allocation and were now using a single factor or double weighted sales factor.

Mr. Bauer said twenty-one states use a single sales factor, he thought eight or nine use the double weighted sales and the three factor apportionment was down to eight. There were states like North Carolina that used quadruple weights sales and others that could be referred to as stray cats.

Commissioner Knox said he would like to rise to the eighty thousand foot level and make a few observations and gear himself up to throw a few of them at Mr. Bauer later. He said he appreciated very much the presentation. His concern was the timing that the TRC was getting it at the end rather than the beginning and looking back on the whole progress of things, he did see a couple of reasons for that. One was timeframe and in combination with the fact that the whole rationale of the TRC had shifted as he had talked about very early on from being a comprehensive review by people with lots of expertise to being essentially a hopefully bright generalist, layman group that becomes a pass through for studies and so immediately the TRC's emphasis was getting the study going.

He said he really wished they had the time and the resources of DoTAX, but perhaps in the TRC's final report to the legislature, the TRC could reflect on recommendation for procedural changes for future TRCs. He wished the TRC had that at their very first meeting.

Mr. Bauer said he agreed that the presentation was really useful. If you went back to the 2012 TRC report, they had done several pages on tax principles. He said Dr. Rousslang's presentation was enlightening by he couldn't think of anything they did that contradicted what was said. He said it was complimentary.

Commissioner Knox said he wasn't speaking from their point of view but as a logical procedure for a TRC to begin to do its work because every report certainly starts with these principles as the basis so there work and thinking process, it would have been nice if they were able to do the same.

Mr. Bauer said he agreed that the TRC should have had this presentation earlier.

APPROVAL OF MINUTES:

Chair Takamura said the next order of business was the approval of the minutes from the August 10, 2017. She asked if there was any motion to amend or approve the minutes.

Commissioner Blouin moved the motion to approve the minutes from August 10, 2017 and Commissioner Pieper seconded the motion. The motion carried unanimously.

DISCUSSION AND ACTION REGARDING APPROVAL FOR TRAVEL EXPENSES OF TAX REVIEW COMMISSION MEMBERS ON RELATED TAX REVIEW COMMISSION BUSINESS:

Chair Takamura said the TRC has talked about this earlier and the expenses were for travel for outer island members that come to Oahu to do TRC business which may include meetings with DoTAX, legislators or community members. They try to schedule meetings when the TRC was having their regular meetings so it would be just one trip, but as the TRC gets nearer to the completion of their report and the presentation of that report, they may not be able to schedule meetings with committees, legislators, DoTAX during our meeting time. The budget that the TRC had for travel was just for TRC meetings.

Commissioner Kaina said she had a question related to that because Chair Takamura has mentioned different things. With respect to the travel expenses and understood it was difficult with the neighbor islands, but the meetings she was talking about, were they representing the TRC or representing themselves in those meetings as individuals. She felt it was important to have clarity as to how money was being spent and to understand what that was. She mentioned meetings with legislators and meetings with other committee members, was that information going to be provided to other TRC members to know that those things were happening.

Chair Takamura said it would be provided and they would discuss what happened. She said the WAM chair had requested to meet with one of them and that was going to be a meeting they would try to schedule and wasn't sure if it was an introductory meeting or follow up on what was going on with the report. They would try to schedule it during a meeting day but wasn't sure they could always do that and once they have to present the report, she didn't know that would be a meeting day also. That's what the travel costs were for.

Commissioner Knox said speaking of legislators, there would also be testimony that will have to happen next session, does the budget period extend into the next session.

Chair Takamura said yes it does and we would not be representing ourselves as individuals, this would be like representing the report to the legislators and if they wanted to meet the chair or vice-chair, which would be the types of meetings she was talking about.

Commissioner Knox said he would also say that he thought personally that it would be beneficial during the writing of the report, that they had the option of coming over here because sometimes it was useful to have face to face discussions with the writer

Commissioner Cook said from his perspective of a neighbor island commissioner and vice-chair, like his two other fellow commissioners, doesn't normally relish coming over for the day. He tries to normally schedule to stay the whole day for efficiency sake to minimize travel in the middle of the day and he would as much as possible preferred to meet by phone or Skype because it minimizes disruption. What was being talked about was sometimes it helps for the business acts of the TRC to be coming over in person.

Commissioner Pieper said he thought this was discussed like five times already and didn't think there was any disagreement with that. He thought where the TRC had left off last time was recommending a budget for that? He said he would be happy to get a motion to approve a budget for that and move on from this because there were no doubts commissioners should meet face to face when possible, so let propose a budget amount, make sure the TRC has enough money and do it.

Chair Takamura said she recommends from now through May, maybe a budget of \$5,000 for travel and if it's not spent, it's not spent.

Commissioner Pieper moved a motion to allocate \$5000 for travel related expenses of outer island TRC members.

Commissioner Kaina said she would ask as a friendly reminder it be for official business.

Commissioner Blouin seconded the motion. The motion was approved by Commissioner Pieper, Commissioner Blouin, Commissioner Knox and Commissioner Kaina. Chair Takamura and Commissioner Cook abstained.

DISCUSSION AND ACTION ON THE FINAL REPORT FROM THE PFM GROUP ON STUDIES OF HAWAII'S TAX SYSTEM:

Chair Takamura said next item on the agenda was the final report from the PFM Group and asked Mr. Bauer if he wanted to go through the changes.

Mr. Bauer said the TRC had received the report and it's not what he would consider to be substantially different from the draft report that was provided last time. They did add the edit definitely out of content related to what was expected state expenditure requirements related to the pension system and what the legislature had done in that area. The changes they made in 2011 were extensive in terms of changing the pension system's structure and went through kind of additional changes that had made a couple of downward revisions to what they now believed were going to be the return on investments that now aligns much more so with where pension systems were putting themselves in that area.

He said he had conversations with B & F, did use some of their expectations related to now the changes that were made in the last legislative session substantially increasing contribution rates for the pension system. That of course was going to mean additional general fund obligations for agencies, departments and state entities and reflected that in the numbers. From looking at that and getting an overall perspective from where their numbers were was fine and was not as big a number quite frankly as he expected them to be before delving into it.

He said they also included a discussion around the qualitative impacts for the state in terms of changes to a structure along the lines of what they had recommended. He took it back and didn't want to use the word recommended because what they were providing the TRC was alternatives and suggested those alternatives they thought were more optimal for the overall state budget and state economy as related to tax changes and has provided commentary then on those somewhat specific mostly around the types of taxes and how they impact on the Hawaii economy. Hawaii's economy was different than a lot of states and included a chart for example, of employment and wages in Hawaii, and it was much different then what was found in a lot of states they worked with. Manufacturing for example, was often the largest sector if not on employment, on wages in a state and that was nowhere near the case in Hawaii. They took those into consideration as they were working through parts of the economy and how they might be impacted to tax changes. They had pointed out on numerous times in the presentations and in their report that Hawaii was a unique state, every state was unique but Hawaii was probably the most unique state among the fifty so it definitely impacted the way they approached Hawaii's tax system and the analysis they've done.

He said they updated some of the information. Updated it for the special session with the vote on TAT and revised the numbers there because the legislature essentially did what we suggested they should do and essentially slightly more, and extended the GET for Oahu. Those were included in the recommendations and they also as Commissioner Knox pointed out weren't accurately reflecting the food excise refundable credit and would change that and send the TRC

rudiments for that. Otherwise from their perspective, there were things the TRC wanted them to further address and hopeful that would get the TRC closer to the comments that were made which were appreciated, answered most of them with a couple of exceptions that they didn't do.

Commissioner Knox said Mr. Bauer had a lot of changes to make and appreciate a whole lot of the changes you did make but his major concern has always been clarity because of that track record in Hawaii of the legislature often not moving on specific recommendations that the TRC has made but referring back to the reports as reference documents and so whatever recommendations the TRC makes or did not decide to make now, his concern was they had a really good reference document. Something that was really clear and really useful to legislators. He thought the TRC was moving towards it. The things he was concerned about may not have had sufficient progress from the last time and Mr. Bauer had pointed out himself that the same topics were sometimes addressed by different people from different sections, and sometimes there would be a need to better integrate and note not necessarily contradictions but things that didn't quite jive or quite sound the same.

He said of everything he sent to Mr. Bauer, he wanted to go over from his list number one and six. Number one had to do with basically the framework in which they assessed adequacy and sufficiency, and recommended the framework for alternative revenue strategies. He was confused, and we've added these statements as he mentioned on page 73 about the increases maybe managed with an existing revenue growth and Dr. Rousslang had pointed out to him that actually there may be some confusion between whether they were talking about the pension system or health benefits.

Mr. Bauer said they would be happy to make any of those kinds of little tweaks that were needed to be made if there was a lack of clarity and something easily corrected by adding words in that particular section. Yeah, now we're talking about specifics of the pension system and Commissioner Knox's point was well taken.

He said first of all, he read through the whole section and made edits himself as the last editor. They added in introductory and summary sections to each of the chapters to address the concerns that people could address individually or use, and would be happy to add clarity if there was specific areas the TRC thought was not clear.

Commissioner Knox said thank you and he would appreciate it especially that topic one and six, just a clear bottom line and simplest possible answer to whether our tax structure was fundamentally regressive or fundamentally progressive, and thought there would be three different answers Mr. Bauer would need to get.

Mr. Bauer said the issue of regressivity as Dr. Rousslang pointed out as well as they did, you could have individual taxes that were regressive and a tax system that was different from those individual taxes, and there was some that were regressive and that were progressive. He thought maybe they need to clarify that and thought among state tax systems, he would generally put Hawaii into the not regressive category, probably more maybe slightly progressive. If they hadn't made that clear they would be happy to entertain places where they thought had not been done well enough. He was under the impression that that's how it read now, but if they didn't think so, to please point it out.

Commissioner Knox said he thought it was clear about the state's tax structure alone being weakly progressive or mildly progressive. He thought it was clear if you add state, local and federal overall, then we become progressive and a whole lot comes from federal progressivity. It was gray and between state and local and various comments scattered throughout wasn't always clear at which of the three levels they were referring.

Mr. Bauer said it was hard because again, we talk about individual taxes and they were different in the system as a whole. He would be happy to look at the very end of it making a definitive statement about it because he thought the Commissioner Knox had identified what the definitive statement would be. He said he had said this before and not just here, there wasn't a single state tax structure as progressive as the federal structure. It was always going to make a system more progressive.

Commissioner Knox said to clarify; he was not talking about the distinction between specific taxes in the overall structure. He was talking about their conclusion about the overall structure when looking at state taxes among state plus local, state plus local plus federal.

Mr. Bauer said they would take a look at that to see if they could take another shot at that.

Commissioner Kaina said her understanding was at that meeting, since the TRC received the final draft the day before, there was not going to be a full discussion about the final draft, changes or requests. She appreciated that Commissioner Knox was able to read the report and put together his notes but other TRC member has not had the opportunity to dig through the report as deeply as that since we were told we didn't have to for that meeting.

She also said she didn't think Mr. Bauer should be making changes based on one commissioner's request without all commissioners having the opportunity to determine exactly what all the commissioners wanted to ask and asked Chair Takamura for clarification on that.

Chair Takamura said she guessed Commissioner Knox had the time but she didn't have the time to go through the report yet. She asked what the TRC would like to do and said the best thing was to read the report, send questions to Mrs. Sakata whom would send to Mr. Bauer.

Commissioner Kaina said that Mr. Bauer has been more than generous with his time and wanted to make sure that the concerns was that of the entire TRC and not just one.

Mr. Bauer said he agreed.

DISCUSSION AND ACTION ON THE ADDITIONAL STUDY TO BE DONE BY THE PFM GROUP REGARDING TAX BURDEN:

Mr. Bauer said he has talked with Dr. Wheeler and three other economic consultant firms that they use and in terms of his understanding of the TRC budget and time frame. None of them believe they could provide the additional study that the TRC was talking about. They think it was an important area for study and they also think DoTAX, B & F or some other entity that may have developed an input/output model for the state would be the best place to look for that

information. He was not sure if it would be cost effective to go outside those resources Hawaii may already have and may have already done what the TRC was asking them to do.

Chair Takamura said they left a number in there and asked if they were going to maybe note how they got that amount, percentage there.

Mr. Bauer said he didn't hear what Chair Takamura said.

Chair Takamura said on page 49, where PFM showed the percentage for tourist, the tax burden, and asked if they were going to put something in the report of how PFM got that percentage.

Mr. Bauer said sure and that Chair Takamura was looking for methodology about how they got any of those numbers. He was sure Dr. Wheeler would put them in the appendices, if that's what she was asking for.

DISCUSSION AND APPROPRIATE ACTION RELATING TO THE TAX REVIEW COMMISSION'S REPORT AND ITS EVALUATION OF THE STATE'S TAX STRUCTURE AND RECOMMENDATION ON TAX REVENUES AND POLICY:

Chair Takamura said the TRC wasn't ready to do that part yet, but she thought going through the report from PFM and all the reports from DoTAX that was received, wanted the TRC to start formulating their own thoughts of what was important to be shown in the recommendations. She said another thing she would like the TRC to look at was what Mrs. Sakata provided a while ago, the list of all the recommendations from previous TRCs. Some of them haven't been adopted and some were very good, and to see what they thought of those too.

She said everyone has vast knowledge on this TRC and think about what they thought even if it was not on a study or prior study, what they thought would be a good recommendation for Hawaii's tax structure. She said it didn't have to be a study, it could be from experience.

WRITTEN COMMENTS ON HAWAII'S TAX STRUCTURE OR ITEMS LISTED ON THE AGENDA:

Chair Takamura said the TRC received a letter from Tom Yamachika of the Tax Foundation of Hawaii with comments on the draft report by the PFM Group Consulting LLC.

Commissioner Knox said Mr. Yamachika consistent with his predecessor points out concerns about adequacy or sufficiency, and he wondered, it does lead into this sort of issue on one hand the TRC has consistently been told adequacy and sufficiency were key principles of tax policy. On the other hand, clearly know recommending to the legislature at least specifically expenditures was not what the TRC was supposed to do, but it was also a signal if we venture into those waters again, at least the Tax Foundation would be concerned about it again. He said he wondered if the TRC had asked their attorney and did this come up before as to whether or not there would be constraints on looking at the whole issue of tax adequacy.

Mr. Nishiyama said not that he was aware of and he didn't believe that that was formally posed.

Commissioner Knox said perhaps it would be of some value to the legislature to get a legal ruling on that.

Mr. Bauer said back in 2012, PFM was very involved in that discussion. The statute that established the TRC doesn't say only to look at equity and efficiency, but it said those were tax principles such as equity and efficiency. He said they had a survey and a variety of principles from different groups that would be considered subject matter experts mentioned adequacy or sufficiency and was not something the TRC cooked up at any particular point in time. So if the TRC was talking tax principles, you were not limited to equity and efficiency. He didn't see how one could argue that sufficiency was not an issue the TRC should be mindful of.

Commissioner Knox said yet it was being argued here and would it be appropriate to get some guidance because he thought it would be useful in doing the contemplation.

Mr. Nishiyama said the request should be made in writing to the Attorney General.

Commissioner Know motioned to request that the Attorney General provide guidance to the TRC on legalist and appropriateness of considering adequacy in their recommendation process and Commissioner Cook seconded the motion.

Mrs. Sakata said it was specific to the expenditure portion not revenue portion.

Commissioner Knox said what he really wanted to do was get resolution on the issue that Mr. Yamachika had raised and see how it affects or should affect the TRC contemplation about what they recommend. He said he understood the TRC had constraints about getting into expenditures and did understand that adequacy seemed, was something the TRC should be looking at but there seemed to be a question, some gray area.\

Commissioner Cook said he has had some concern the he expressed in the past when they looked at potential options for adequacy on the tax side, increasing revenues and the other side of that seemed the TRC was out of balance. We were just looking at tax options of dealing with the unfunded liabilities but weren't looking at the other side of expenditures. His assumption was that was off limits and that was a political discussion, but if his understanding of the objections raised by the Tax Foundation of Hawaii was correct that could be problematic as well looking at the revenue side and might be impermissible. He supported getting an opinion and guidance from the AGs Office on the scope of the TRCs authority on that matter.

Mrs. Sakata said she was going to read the statute. The statute says that the TRC would do a systemic review of the state tax structure using such standards as equity and efficiency, 30 days prior to the convening of the second regular session of the legislature after the members of the commission has been appointed, the commission shall submit to the legislature an evaluation of the state tax structure and recommend revenue and tax policy.

Chair Takamura asked for approval of the motion. Motion carried unanimously.

PUBLIC COMMENTS ON HAWAII'S TAX STRUCTURE OR ITEMS LISTED ON THE AGENDA:

Mr. Yamachika thanked the TRC for the floor and for discussing the first issue that was referred to on the first page and was there the last time the foundation submitted comments through its predecessor, and wanted to make sure that discussion was considered. He said it may not be a legal matter in so much as what was the proper sphere of the TRC as opposed to what the legislature's kuleana was. They were supposed to be the ones who make those tough decisions about what was spent and how much was spent, and how many feathers was plucked from the goose, for those who read the report and found that great analogy from that French taxation administrator that basically said that taxation was a science of plucking the goose to get the most feathers and minimize the hissing. He said that that's what we're trying to do here and thought the TRC should be more concerned about the fairness and efficiency aspect opposed to how they could they raise money. They weren't there to give the legislators a menu of you could raise this much money, this much money and if you want extra large fries or big coke, this was what you do. He thought it was more of a question of making the system fairer and more efficient, that kind of stuff consistent with the principles Dr. Rousslang mentioned.

He said specifically with regards to the recommendations that were in the draft report, he didn't get to read that far to the end, but wanted to make more observations on the pension exemptions and that the way pension exemptions were structured right now, doesn't only apply to government plans. It applied to government and government defined benefit plans and any plan where the employer contributed to the pension fund independently of the employee's contribution. A fairly general question to ask was why there was a distinction between employer funded amounts and employee funded amounts.

He said back when he was with the department, he was tasked with writing the regs for that exemption and one of the big objections that came out from the public was why was there a huge distinction between employer funded and employee funded plans in the first place and his question was its there, deal with it. There were several TIRs and prior rules already and not being able to change the law, he eventually had to figure out how to deal with what was already there, but the TRC could deal with that.

Mr. Bauer said he reviewed the Tax Foundation's comments and they had differences on a few issues, some of which reflects the fact that one of their charges was to identify revenue options for consideration. A few of them they made exceptions to and wouldn't necessarily dramatically disagree on some of their exceptions. In general, he thought as they often find with the Tax Foundation, they were cognizant of it being a very fine organization that did a lot of good research.

Chair Takamura thanked Mr. Yamachika for his comments and the TRC always appreciated another view and another consideration for when they make recommendations. She appreciated that he took the time to read the draft report and made comments on it.

Dr. Colby said in light of Mr. Yamachika's comments on pension exemption, what was his view on taxes on employee contributions to pensions. For example, at the federal level if a person contributes to pension in the state of Hawaii, it was taxable.

Mr. Yamachika said the feds already had their own system where they had different choices. A person could take the deduction out now and get taxed when it came out or pay taxes now and get no tax when it came out. The system was already there. We were distorting the picture by saying if you had money coming out of a defined benefit plan even though the feds were going to tax it, we won't or if you had an employer match, we won't tax the employer match. The question was there a coherent rationale for saying why we don't tax the employer match but we would tax the individual contribution. Should we be following the feds or would we be exempting all of them as opposed to that distinction created between employer and employee contributions. He said a practitioner, when he was with the department tried to impress upon him that was not a viable distinction but he had to deal with it because it was there.

Chair Takamura said maybe his perspective was its time for a change and she agreed, like 401Ks were taxable and that was for retirement plan also. She questioned why was that taxed versus other pensions, it wasn't fair and that was her question to Mr. Bauer. If everything was a retirement plan, why doesn't \$25,000 of all retirement plans be non-taxed and anything over that taxed including 401Ks.

Mr. Yamachika said right now with the exemption we now had, if you had \$1,000,000 coming out of a defined benefit plan and no taxes.

Commissioner Pieper said as Mr. Yamachika pointed out, it was a tough situation to get people to accept that and usually always met with much resistance.

Chair Takamura said maybe if it was packaged enlight of being fair that all retirement plans were exempt.

Commissioner Pieper said do like the feds or exempt it all.

Dr. Colby said with defined contribution plans the employee has not elected how much to put into a defined contribution plan, you have to have a portion that was taxed, was a strange concept as well.

Mr. Yamachika said if the employee doesn't elect then a portion was exempt.

Dr. Colby said yes, it was exempt but in some cases, a defined contribution as with the state, employees don't have the option.

Dr. Rousslang asked was there any problem exempting only state pensions and not the other ones that were similar like the employer provided or federal government provided.

Mr. Yamachika asked Dr. Rousslang if his question was whether it would be acceptable to exempt just state pensions. He said he hasn't researched the legalities of that. It was probably something that could be done and thinks there would be arguments you must do it.

Mr. Bauer said there were a variety of states that do provide some of partial exemption for public pensions and not private pensions, and was deemed acceptable. On tax policy it was a rational basis was the general standard and there was various arguments made t that rational basis in taxation.

Mr. Yamachika said even within the state, there were different kinds of pension vehicles. When he was with the state, he contributed to the states equivalent of a 401K.

Commissioner Knox said he was going back to what was on the first page, did think a little light would help the TRC with legal perspective but last time the previous TRC went to the statement that the TRC could only affect revenue sorts of things not expenditures, and therefore any recommendations wasn't ordered to look at the expenditures, and the Simpson-Bowles Commission be created. He asked Mr. Yamachika if he was still feeling that that sort of recommendation would not be appropriate for a TRC to make.

Mr. Yamachika said he thought what the people had in mind when the enacted such a provision in the constitution was once in a while we had to take a look at our system to make sure it was fair and consistent with what people wanted. He thought there was a potential for lawmakers to use if for the purpose of gaining political coverage and was not what the TRC was for.

Commissioner Knox said early TRC studies of adequacy were in situations where the recent past appeared to be a pretty good predictor of the upcoming future in terms of need for evidence. We had entered a period where that was no longer the case, more secondarily, pointed out in some of the additional material provided by the PFM report, entered a period where states in general were finding revenue were not coming up to their forecasts and seemed to be a national issue.

Mr. Yamachika said the issue of need was necessarily a political question and if he was Commissioner Knox, he wouldn't go there.

NEXT MEETING:

The next meeting was scheduled for Tuesday, October 24, 2017 at 1:00 PM.

TRC tentatively scheduled meetings for: Wednesday, November 8, 2017 at 1:00 PM
Monday, December 11, 2017 at 1:00 PM

ADJOURNMENT:

The meeting was adjourned at 2:40 PM.