HAWAIʻI APPLESEED
CENTER FOR LAW & ECONOMIC JUSTICE

FOR IMMEDIATE RELEASE

January 9, 2024

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Hawaiʻi's tax system makes inequality worse, national study finds

Hawaiʻi lawmakers can improve the economic health of our communities by re-balancing the state's upside-down tax code.

HONOLULU, Hawaiʻi — Hawaiʻi's tax system is upside-down, with the wealthy paying a smaller share of their income in taxes than low- and middle-income families. That's according to the latest edition of the Institute on Taxation and Economic Policy (ITEP)'s *Who Pays?* report, the only distributional analysis of tax systems in all 50 states and the District of Columbia.

The report finds Hawaiʻi has the 22nd most regressive tax system in the nation. Regressivity means the tax system takes a larger share of income from those further down the income scale than from those at the top.

This regressivity in our state's tax code is driven by factors such as our comparatively high reliance on sales and excise taxes for funding, preferential tax rates on capital gains, and the absence of a state child tax credit, among other things. Lawmakers could help address this imbalance by creating a state child tax credit, taxing capital gains the same as income from regular work, and looking for other ways to better tax wealth while reducing our reliance on the General Excise Tax.

"Hawaiʻi's high cost of living and low wages continue to force local families to live paycheck to paycheck or leave the state," said Will White, deputy director of Hawaiʻi Appleseed. "That's bad for the entire economy. Fortunately, the state tax code is a powerful tool lawmakers can use to address the economic health of our communities."

"There are multiple policy changes the legislature could enact in 2024 to reduce the burden on working families, while increasing revenue for anti-poverty programs, affordable housing, and other things Hawaiʻi's people need, through fairer taxes on wealth," said Devin Thomas, Appleseed senior policy analyst.

The report’s key findings for Hawai‘i:

- The average effective state and local tax rate is 14.1% for the lowest-income 20% of individuals and families; 14.2% for the middle 20%, and 10.1% for the top 1%.
- Hawai‘i has the 22nd most regressive tax system in the nation.
- Hawai‘i is one of 42 states that tax the top 1% less than every other income group.

Nationally, tax systems in 44 states exacerbate inequality by making incomes more unequal after collecting state and local taxes. Only six states plus D.C. reduce inequality, the report finds. On average across the country, the lowest-income 20 percent of taxpayers face a state and local tax rate nearly 60 percent higher than the top 1 percent of households. The nationwide average effective state and local tax rate is 11.3 percent for the lowest-income 20 percent of individuals and families, 10.5 percent for the middle 20 percent, and 7.2 percent for the top 1 percent.

“When you ask people what they think a fair tax code looks like, almost nobody says we should have the richest pay the least. And yet when we look around the country, the vast majority of states have tax systems that do just that,” says Carl Davis, ITEP’s Research Director. “There’s an alarming gap here between what the public wants and what state lawmakers have delivered.”

Recent policy changes have exacerbated or lessened regressivity in state tax systems, depending on the choices made by lawmakers.

Many states with tax codes that already increase inequality have doubled down on regressive tax policies in recent years. Arkansas, Idaho, Iowa, Kentucky, Nebraska, and West Virginia, for instance, have taken steps to deeply cut taxes on more affluent households and wealthy corporations.

On the other hand, many of the states with tax codes that reduce inequality, or at least do less than average to widen inequality, have made strides toward more progressive tax policies in recent years. Massachusetts, Minnesota, New Jersey, New Mexico, New York, and the District of Columbia, for instance, have taken steps both to raise taxes on more affluent households and lower them for low- and moderate-income families.

“We’ve seen a lot of states shift their tax systems to become even more regressive in recent years by enacting deep tax cuts for the wealthiest. But we know it doesn’t have to be like this. There is a clear path forward for flipping upside-down tax systems and we’ve seen a handful of states come pretty close to pulling it off,” said Aidan Davis, ITEP’s State Policy Director. “The regressive state tax laws we see today are a policy choice, and it’s clear there are better choices available to lawmakers.”

About

Who Pays? is the only distributional analysis of tax systems in all 50 states and the District of Columbia. The comprehensive 7th edition of the report assesses the progressivity and regressivity of state tax systems by measuring effective state and local tax rates paid by all income groups. No two state tax systems are the same; this report provides detailed analyses of the features of every state tax code. It includes state-by-state profiles that provide baseline data to help lawmakers and the public understand how current tax policies affect taxpayers at all income levels. Over 99 percent of all state and local taxes, measured by their revenue contribution, are included in the analysis.

ITEP is a non-profit, non-partisan tax policy organization. We conduct rigorous analyses of tax and economic proposals and provide data-driven recommendations on how to shape equitable and sustainable tax systems. ITEP's expertise and data uniquely enhance federal, state, and local policy debates by revealing how taxes affect people at various levels of income and wealth, and people of different races and ethnicities.

Hawai‘i Appleseed is committed to a more socially and economically just Hawai‘i, where everyone has genuine opportunities to achieve economic security and fulfill their potential. We change systems to address inequity and foster greater opportunity by conducting data analysis and research to address income inequality, educating policymakers and the public, engaging in collaborative problem solving and coalition building, and advocating for policy and systems change.