Hawai‘i's Tax Credits: Key Findings

TAX CREDITS are among the tools the state uses to invest in people, businesses and the environment. Instead of appropriating state funds for these investments through the budget process, tax credits meet the state's objectives by reducing the tax liability of qualified individuals and businesses in order to:

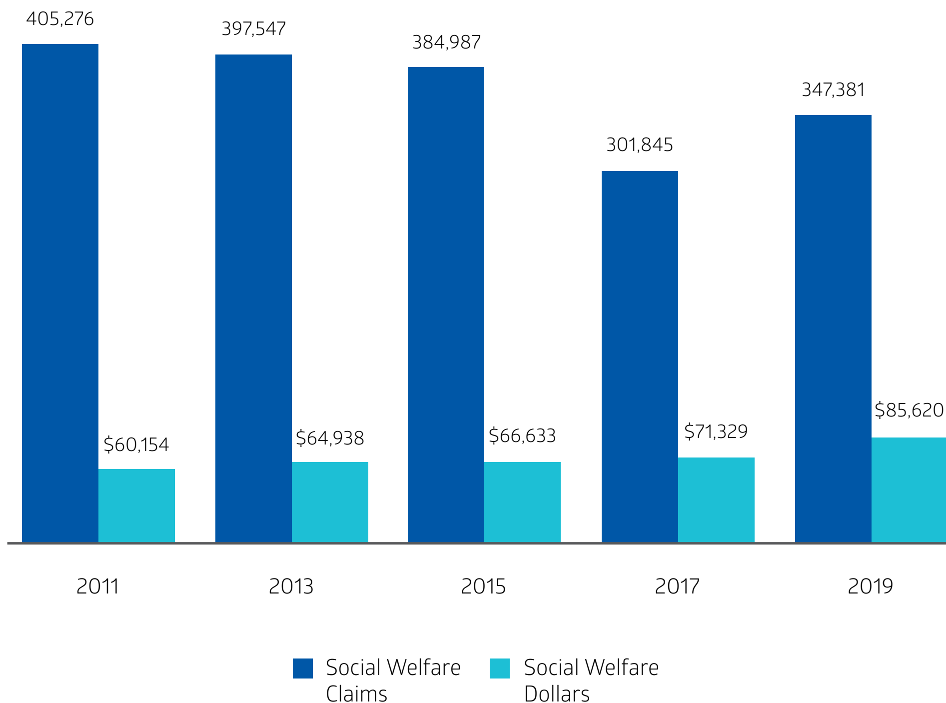
- Promote social welfare;
- Encourage certain industries or economic activities; or
-
- Avoid double taxation or pyramiding of Hawai‘i taxes.

In 2019, Hawai‘i granted more than $300 million in tax credits, a sum equal to 10 percent of all individual and corporate income taxes collected that year.

In 2000, Hawai‘i's tax credits amounted to a total of $154 million. This figure more than doubled by 2015 when it totaled $339 million. It has since declined, totaling $310 in 2019. (**All amounts are in 2021 dollars.**)

- Tax credits for social welfare accounted for 28 percent of total tax credit dollars in 2000, but dipped to just 14 percent in 2005. By 2011, dollars for social welfare tax credits had rebounded due to changes in the food/excise tax credit. By 2019, social welfare tax credits again made up 28 percent of the total, reflecting the implementation of the Earned Income Tax Credit in 2018.
- In 2000, 54 percent of tax credit dollars went to avoid duplicating and pyramiding tax payments. By 2019, they accounted for just 31 percent of all tax credits.

Social Welfare Tax Credits Total Claims & Dollars, 2011–19 (2021 Dollars)



More than 90 percent of claims for social welfare tax credits go to low-income households for General Excise Taxes on food, for low-income renters and, starting in 2018, for the EITC. Despite the new EITC, the number of tax credits claimed by low-income households decreased by nearly 53,000 between 2011 and 2019, due largely to the failure to adjust eligibility levels for inflation.

Download the full brief at https://www.hibudget.org/publications/tax-credits-tools-advance-prosperity

HAWAI‘I **KIDS COUNT**
Hawai‘i Children's Action Network

Recommendations

1. Weigh Costs and Benefits of Tax Credits

Tax credits are as important to the overall resources of the state as revenue-producing measures. Once put in place, they reduce future revenues or provide taxpayer refunds, both of which affect the amount of funds available to support the state budget. We recommend that the legislature require that all measures introduced to create new tax credits or amend existing ones should include:

- An estimate of cost to the state associated with implementing the tax credit;
- A clear description of the public benefits the tax credit will produce; and
- The process and data that will be used to evaluate the actual benefits and costs that result from the tax credit.

This will help lawmakers decide in advance whether a tax credit, budget appropriation, or other strategy will best achieve the public purpose in question.

2. Increase Transparency and Accountability

When the state gives money to individuals and businesses through grants and contracts, the information is made public. This is not the case for taxpayers who derive substantial economic benefits from tax credits.

We recommend that the legislature impose more transparency and accountability for tax credits that provide large tax breaks and refunds to a small number of taxpayers. Legislative authorization for both existing tax credits and any created in the future should require that the following information be disclosed to the public:

- The identity of the taxpayer;
- The amount of the tax credit claimed; and
- Summary data provided by the claimant that verifies that the public good is being served.

3. Justify Refundability vs Nonrefundability

Refundable tax credits like those temporarily created to help victims of flooding, are also the most helpful strategies to reduce taxes or provide cash aid to targeted taxpayers. Nonrefundable tax credits are most appropriate for taxpayers with larger tax liabilities in amounts that can be used in a short time frame.

The lowest income taxpayers often cannot access the full benefit of nonrefundable tax credits because the credit is often larger than their total liability. This weakens the effectiveness of credits like the state's Earned Income Tax Credit (EITC).

Lawmakers should consider including in legislative language the reasons why each new tax credit is made refundable or nonrefundable. As nonrefundable tax credits may be an unexpected drain on resources even after they've expired, legislators should also consider parameters that may limit the amount and time period over which benefits may be used.

4. Index to Inflation

Many of Hawai'i's tax credits that promote social welfare have not been adjusted regularly to reflect inflation. Most of these tax credits are available to lower-income taxpayers, so over time fewer claimants are eligible because their wages have risen with inflation. In addition, if the dollar value of the benefit is not increased to keep up with costs, it no longer meets its intended purpose.

The tax credit for low-income renters, which was last adjusted for inflation in 1989, is a good example of this concern. If updated to 2021 dollars, income eligibility would increase from $30,000 per year to $68,100 and its value for every personal exemption would be $159 instead of $50.

We recommend that lawmakers review and update tax credits where eligibility is based on restricted incomes, and dollar amounts are intended to offer economic assistance. Once adjusted to current dollars, legislation should ensure that these tax credits are adjusted annually for inflation.