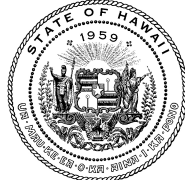


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**TESTIMONY OF
GARY S. SUGANUMA, DIRECTOR OF TAXATION**

TESTIMONY ON THE FOLLOWING MEASURE:

H.B. No. 1147, Relating to the Earned Income Tax Credit

BEFORE THE:

House Committee on Finance

DATE: Wednesday, February 19, 2025

TIME: 2:00 p.m.

LOCATION: State Capitol, Room 308

Chair Yamashita, Vice-Chair Takenouchi, and Members of the Committee:

The Department of Taxation (DOTAX) offers the following testimony in support of H.B. 1147, an Administration measure, for your consideration.

H.B. 1147 amends section 235-55.75, Hawaii Revised Statutes (HRS), relating to the Earned Income Tax Credit (EITC) to address two issues: (1) Nonresident claims of the EITC; and (2) Carryforward of the nonrefundable EITC claimed for tax year 2022. The bill is effective upon approval and applies to taxable years beginning after December 31, 2024.

Nonresident Claims of the EITC

Under current law, the EITC is equal to 40 percent of the federal EITC allowed and properly claimed on an individual taxpayer's federal income tax return. A part-year resident is required to adjust that amount by multiplying it by the ratio of their Hawai'i Adjusted Gross Income (AGI) to federal AGI. For individuals who resided outside of the State for part of the year, this adjustment ensures that the amount of the EITC claimed is proportionate to income the individual earned in the State. Section 235-55.75, HRS, is silent, however, as to whether nonresidents are required to adjust the EITC amount.

This bill clarifies that nonresidents must also adjust the amount of the EITC using

the ratio of their Hawai'i AGI to federal AGI, thereby ensuring equitable treatment between part-year residents and nonresidents.

Carryforward of the Nonrefundable EITC for Tax Year 2022

The nonrefundable EITC was established by Act 107, Session Laws of Hawaii (SLH) 2017, for tax years 2018 through 2022. Pursuant to Act 107, the nonrefundable EITC could be carried forward indefinitely until exhausted.

Act 114, SLH 2022, established a refundable EITC, beginning for tax year 2023, and also imposed a deadline for carryforwards of the nonrefundable EITC. Specifically, Act 114 provides that claims for the nonrefundable EITC for tax years 2018 through 2021 cannot be carried forward after tax year 2024. The carryforward for tax year 2022, however, appears to have been inadvertently omitted. Accordingly, under current law, a taxpayer who claimed the nonrefundable EITC for tax year 2022 may carry forward any unused credit indefinitely until exhausted.

This bill imposes a deadline such that any carryforward of the nonrefundable EITC for tax year 2022 cannot be claimed after tax year 2025. DOTAX notes that this amendment will promote taxpayer equity and discourage potential abuse and fraud. Setting an expiration date for unused nonrefundable credits eliminates the difficulty of tracking unused credits years after they were claimed, easing administration of the tax system. This also removes incentives for fraudulent claims and abuse, which are more difficult to identify when credits are used farther from the original claim.

Revenue Impact

DOTAX estimates a revenue gain as follows:

General Fund Impact (\$ millions)

FY 2026	FY 2027	FY 2028	FY 2029	FY 2030	FY 2031
-	2.4	2.4	2.4	1.7	-

Thank you for the opportunity to provide testimony in support of this measure.

TAX FOUNDATION OF HAWAII

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SUBJECT: INCOME, Limit EITC for Nonresidents; Expire 2022 Credits in 2026

BILL NUMBER: SB 1466, HB 1147

INTRODUCED BY: SB by KOUCHI by request; HB by NAKAMURA by request (Governor's Package)

EXECUTIVE SUMMARY: Clarifies that nonresidents who claim the refundable earned income tax credit are required to adjust the amount claimed using the ratio of their Hawai'i adjusted gross income to federal adjusted gross income. Eliminates the unlimited carryforward on nonrefundable earned income tax credits for tax year 2022.

SYNOPSIS: Amends HRS section 235-55.75 to provide that for a part-year resident or a nonresident, the state earned income tax credit (EITC) shall equal 40% of the amount of the federal EITC multiplied by the ratio of Hawaii AGI to federal AGI.

Provides that nonrefundable EITC for the year 2022 expires on December 31, 2025.

EFFECTIVE DATE: Taxable years beginning after December 31, 2024.

STAFF COMMENTS: This is an Administration bill sponsored by the Department of Taxation and designated TAX-03 (25).

The current Hawaii EITC statute currently requires part-year residents to multiply 40% of the federal EITC, which is the amount a resident would be entitled to, by the ratio of Hawaii AGI to federal AGI. The bill also requires that adjustment for nonresidents, which makes sense because nonresidents are in effect part-year residents with no period of Hawaii residency.

Apparently, there is a loophole in the law that the Department seeks to plug. The EITC was enacted by Act 107, SLH 2017, as 20% of the federal EITC. It was nonrefundable but the law stated that it may be used as a credit against the taxpayer's net income tax liability in subsequent years until exhausted. The law was amended by Act 114, SLH 2022, to make the credit refundable for taxable years starting in calendar 2023, and to make any credit being carried forward from years 2018 through 2021 expire on December 31, 2024. Nonrefundable tax credits earned in 2022 escaped the net and would last forever absent this bill.

Digested: 2/9/2025