

*For Immediate Release*

Wednesday, February 14, 2007

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**HAWAII'S TAX BURDENS ON POOR AMONG THE NATION'S LARGEST; STATE EITC WOULD PROVIDE TARGETED RELIEF**

Hawaii levies among the nation's highest income taxes on low-income working families and its national ranking is worsening by some measures, according to a report from the Center on Budget and Policy Priorities. Creation of a state Earned Income Tax Credit, one of two policy responses the Hawaii legislature is considering this year, would bring meaningful tax relief to low-income families at moderate cost, the report states.

"An EITC would bring more tax relief to low-income families — and at less cost — than the tax proposal by Governor Lingle because an EITC would be targeted on the families who need it," said Jason Levitis, an analyst at the Center and author of the report.

<b>Table 1: HAWAII IMPOSES SIGNIFICANT INCOME TAXES ON POOR AND NEAR-POOR WORKING FAMILIES</b>		
<b>Measure of Tax Burden</b>	<b>Amount*</b>	<b>HI Rank* (out of 42)</b>
<b>Income Tax at the Federal Poverty Line for:</b>		
One-Parent Families of Three (income = \$16,122)	\$294	<b>1</b>
Two-Parent Families of Four (income = \$20,670)	\$382	<b>3</b>
<b>Income Tax at 125% of the Federal Poverty Line for:</b>		
One-Parent Families of Three (income = \$20,153)	\$546	<b>1</b>
Two-Parent Families of Four (income = \$25,838)	\$665	<b>4</b>
<b>Income Tax Threshold for:</b>		
One-Parent Families of Three	\$10,400	<b>3</b>
Two-Parent Families of Four	\$14,000	<b>3</b>

\* Reflects tax year 2006 as if legislated changes affecting future years were in effect.

Of the 42 states with income taxes, Hawaii levies the nation's highest taxes on families of three with incomes at the poverty line and at 125 percent of the poverty line, as Table 1 shows. And Hawaii's tax thresholds (the level of income at which families begin to owe income tax) are among the nation's lowest, thousands of dollars below the poverty line.

Taxing the incomes of working-poor families undermines the efforts by policymakers across the political spectrum to help families work their way out of poverty, the report notes. The federal government has exempted working-poor families from the income tax since the mid-1980s, and most states now do so as well.

Last year, Hawaii and several other states that continue to levy high income taxes on low-income families (such as Alabama and West Virginia) enacted major tax cuts. But those other states generally did a better job than Hawaii of targeting tax relief on low-income families. As a result, while Hawaii's tax cut has modestly reduced taxes for the working poor, the state's *ranking* has actually worsened by some measures in the past year.

## EITC More Effective, Less Costly Than Governor's Proposal

The Hawaii legislature is considering two primary proposals for low-income tax relief: a package of permanent tax cuts proposed by Governor Lingle and a state EITC proposed by leaders of the legislature. While both approaches would provide significant tax relief to low-income families, an EITC would provide greater benefit at less cost because it is targeted on those families. (The benefits of the governor's proposal, in contrast, are distributed more broadly.)

Table 2 compares the governor's proposal to a leading EITC proposal (SB1919), which would create a state EITC set at 20 percent of the federal EITC. The credit would be "refundable"; that is, households whose EITC exceeds their state income tax liability would receive a refund check for the difference. The refund would partially offset the other state taxes these households pay.

<b>Table 2. Comparison of Governor's Income Tax Proposal and a 20% EITC: Cost to the State and Impact on Low-Income Families</b>			
Measure of Cost or Tax Burden	Current Law	Governor's Proposal	20% EITC
Cost in 2007 (millions of \$)	0	\$60 million	\$24 million
Bills	None	SB1493, SB1494, SB1495	SB1919/ HB1799
<b>Income Tax at the Federal Poverty Line for:</b>			
One-Parent Families of Three (income = \$16,122)	\$294	\$82	-\$558
Two-Parent Families of Four (income = \$20,670)	382	138	-\$363
<b>Income Tax at 125% of the Federal Poverty Line for:</b>			
One-Parent Families of Three (income = \$20,153)	546	296	-\$135
Two-Parent Families of Four (income = \$25,838)	665	362	\$138
<b>Income Tax Threshold for:</b>			
One-Parent Families of Three	10,400	15,000	\$21,500
Two-Parent Families of Four	14,000	16,600	\$24,400
Source: Center on Budget and Policy Priorities			
All calculations reflect tax year 2006 if changes affecting future years were in effect.			

The governor's proposal would cost about \$60 million per year and yet would leave Hawaii among the worst states in the nation in terms of its income-tax burden on low-income families. An EITC set at 20 percent of the federal would cost less than half as much — about \$26 million per year — and would make Hawaii above average in this area.

"With an EITC, Hawaii's income tax would no longer be one of the nation's most burdensome on low-income families. That would be an important step forward, especially given Hawaii's high cost of living," said Levitis.

A state EITC also would moderate the imbalance in Hawaii's tax system, under which low-income residents pay a higher share of their income in taxes than wealthier residents do, Levitis noted.

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**The Center on Budget and Policy Priorities** is a nonprofit, nonpartisan research organization and policy institute that conducts research and analysis on a range of government policies and programs. It is supported primarily by foundation grants.