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THE IMPACT OF HAWAII'S INCOME TAX ON LOW-INCOME FAMILIES: AN UPDATE

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In the next few days, Hawaii's legislature will consider the conference agreement on changes to Hawaii's income tax, HB957. This agreement, which appears to have the support of legislative leadership and the governor, increases the standard deductions and expands the tax brackets beginning in tax year 2007.[1]

The bill fails to remedy a well-documented problem in Hawaii's tax system: the high income tax Hawaii levies on poor working families. A Center on Budget and Policy Priorities report earlier this year found that in tax year 2005, Hawaii was one of the states with the very highest income taxes on families with poverty-level earnings.[2] Despite its substantial cost, HB 957 provides relatively little tax reduction for working-poor families and does little to improve Hawaii's standing relative to other states.

- Of the 42 states with income taxes, Hawaii in 2005 imposed the second-highest income tax in the nation on one-parent families of three with income at the federal poverty line. Under HB957 and other tax changes passed this year, Hawaii will still impose the second-highest income tax on these families.[3] See Table 1.

Table 1. Impact of Tax Cuts in HB957 on Hawaii's Income-Tax Treatment of Poor Working Families, and on Hawaii's Rankings Compared to Other States with Income Taxes

Measure of Tax Burden	Under Current Law	Under HB957	2005 Rank under Current Law (out of 42)	Rank under HB957 and Other New Law* (out of 42)
Income Tax on:				
One-Parent Families of Three at Poverty Line ($15,577)	$373	$263	2	**2**
Two-Parent Families of Four at Poverty Line ($19,961)	470	303	2	**5**
Income at which Income Tax begins to be Levied on:				
One-Parent Families of Three	9,800	10,400	3	**4**
Two-Parent Families of Four	11,500	14,000	4	**4**
* Reflects tax year 2005 rankings if HB957 and new Alabama law had been in effect.				
Source: Center on Budget and Policy Priorities				

[1] The bill also includes temporary flood relief provisions which are not considered here.
[2] Jason A. Levitis and Nicholas Johnson, "The Impact of State Income Taxes on Low-Income Families in 2005," Center on Budget and Policy Priorities, February, 2006.
[3] On April 12, Alabama Governor Bob signed legislature providing major income tax relief to poor working families beginning in tax year 2007. See www.cbpp.org/4-17-06sfp.htm.

- Under HB957, Hawaii's tax thresholds, the lowest income at which families are required to pay income tax, will be the fourth lowest in the nation, and still well below the federal poverty line.

- A separate analysis by the Institute on Taxation and Economic Policy finds that the poorest 40 percent of Hawaii residents — those with income under $31,000 — will receive only 20 percent of the benefits of the bill. See Table 2.

Table 2. Distribution of the Benefit of Tax Cuts in HB957

Income Quintile	Income Range	Average Tax Cut	Share of Total Benefit of Tax Cuts
Highest 20%	More than $81,000	$188	32%
Fourth 20%	$50,000 to $81,000	149	26%
Third 20%	$31,000 to $50,000	133	22%
Second 20%	$17,000 to $31,000	89	15%
Lowest 20%	Less than $17,000	27	5%

Source: Institute on Taxation and Economic Policy, May 2006

Hawaii's income tax imposes a major burden on poor and near-poor working families. The Center study of state income tax systems found that, overall, Hawaii's income tax in 2005 was second only to Alabama's in the burden it imposed on low-income families, and it was far outside the national mainstream. Alabama has since significantly reduced its taxes on the poor. HB957 directs only a fraction of its benefit to low-income families, and so leaves Hawaii's income tax system well outside the national mainstream in its tax treatment of the working poor.