

**TESTIMONY**

**SB 272**

LINDA LINGLE  
GOVERNOR



DARWIN L.D. CHING  
DIRECTOR

COLLEEN Y. LaCLAIR  
DEPUTY DIRECTOR

**STATE OF HAWAII  
DEPARTMENT OF LABOR AND INDUSTRIAL RELATIONS**

830 PUNCHBOWL STREET, ROOM 321  
HONOLULU, HAWAII 96813  
www.hawaii.gov/labor  
Phone: (808) 586-8842 / Fax: (808) 586-9099  
Email: dlir.director@hawaii.gov

February 4, 2009

To: The Honorable Dwight Y. Takamine, Chair  
and Members of the Senate Committee on Labor

Date: Thursday, February 5, 2009

Time: 2:45 p.m.

Place: Conference Room 224, State Capitol

From: Darwin L.D. Ching, Director  
Department of Labor and Industrial Relations

**S.B. 272 - Relating to the Income Tax Law**

**I. OVERVIEW OF PROPOSED LEGISLATION**

S.B. 272 proposes to amend section 235-7, HRS, to exclude unemployment insurance benefits as income under the state income tax law.

**II. CURRENT LAW**

Currently, the state law provides for taxation of unemployment benefits under section 235-2.3, HRS, Conformance to the federal Internal Revenue Code; general application.

Unemployment compensation first became taxable for IRS purposes under Public Law 95-600, The Revenue Act of 1978, which designated specific income levels at which unemployment benefits were taxable (\$25,000 for joint returns or \$20,000 for single returns). The Tax Equity and Fiscal Responsibility Act of 1982 lowered the applicable income levels to \$18,000 for joint returns or \$12,000 for single returns. Public Law 99-514, Section 121 of the Tax Reform Act of 1986, amended the law to provide that gross income shall include all unemployment benefits.

Although these federal laws did not require states to amend their laws to tax unemployment insurance benefits, Hawaii adopted provisions identical to federal

statutory provisions.

### **III. SENATE BILL**

The Department opposes this bill for the following reason:

1. The unemployment benefits system is setup as a wage replacement program to assist the insured unemployed while they seek new employment. The weekly benefit amount is determined by the claimant's prior wages. The State should continue to tax unemployment benefits just as they would the claimant's prior wages.

LINDA LINGLE  
GOVERNOR

JAMES R. AIONA, JR.  
LT. GOVERNOR



KURT KAWAFUCHI  
DIRECTOR OF TAXATION

SANDRA L. YAHIRO  
DEPUTY DIRECTOR

STATE OF HAWAII  
DEPARTMENT OF TAXATION  
P.O. BOX 259  
HONOLULU, HAWAII 96809

PHONE NO: (808) 587-1510  
FAX NO: (808) 587-1560

**SENATE COMMITTEE ON LABOR  
TESTIMONY REGARDING SB 272  
RELATING TO THE INCOME TAX LAW**

**TESTIFIER: KURT KAWAFUCHI, DIRECTOR OF TAXATION (OR DESIGNEE)**

**DATE: FEBRUARY 5, 2009**

**TIME: 2:45PM**

**ROOM: 224**

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This measure excludes unemployment insurance benefits from gross income that is subject to tax for taxable years beginning after December 31, 2008.

The Department of Taxation (the "Department") **opposes** this legislation due to the reasons enumerated below.

**RATIONALE FOR TAXING UNEMPLOYMENT INSURANCE BENEFITS—**

Unemployment insurance benefits are generally viewed as a substitute for wages and thus, subject to income tax under both Hawaii's tax laws and the Internal Revenue Code. This measure would decouple Hawaii's tax treatment of unemployment insurance benefits from the Internal Revenue Code.

**FISCAL CONSTRAINTS—**While the Department is sympathetic to the growing number of unemployed individuals, budgetary constraints require that the Department oppose this legislation. Even if this measure had a sunset date, the annual fiscal impact alone is significant.

**REVENUE LOSS—**If this measure is passed, the resulting revenue loss is estimated to be \$12.6 million annually.

# TAXBILLSERVICE

126 Queen Street, Suite 304

TAX FOUNDATION OF HAWAII

Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: INCOME, Exclude unemployment benefits

BILL NUMBER: SB 272

INTRODUCED BY: Nishihara

BRIEF SUMMARY: Amends HRS section 235-7 to exclude from state income taxation, unemployment benefits.

The amendment made by this act shall not be repealed when this section is reenacted on January 1, 2013, pursuant to section 3 of Act 166, SLH 2007.

EFFECTIVE DATE: Tax years beginning after December 31, 2008

STAFF COMMENTS: Currently, unemployment insurance benefits are taxable under both the state and federal income tax laws. The proposed exclusion would represent a digression from the state's efforts to maintain conformity between the state and federal income tax laws as no exclusion is available at the federal level. Further, the lack of any federal tax preference would actually create a heavier burden of taxes for the unemployed.

Because this measure would reduce the amount of income that would be subject to the state income tax and therefore reduce the taxpayer's state income tax bill, the amount of state taxes that could then be deducted against federal income would also be reduced, exposing more income to the federal tax rates which are set at a much higher rate. Thus, this measure actually increases the unemployed federal tax burden and shifts what could have been state tax revenues to the federal government.

Digested 2/3/09

The Twenty-Fifth Legislature  
Regular Session of 2009

THE SENATE  
Committee on Labor  
Sen. Dwight Y. Takamine, Chair  
Sen. Brian T. Taniguchi, Vice Chair

State Capitol, Conference Room 224  
Thursday, February 5, 2009; 2:45 p.m.

**STATEMENT OF THE ILWU LOCAL 142 ON S.B. 272  
RELATING TO INCOME TAX LAW**

The ILWU Local 142 supports S.B. 272, which excludes unemployment insurance benefits as income under the state income tax law.

More and more people in Hawaii are relying on unemployment insurance to help meet their daily living expenses. Many of them never before applied for benefits but have been forced to turn to government support because of job loss or reduced work hours in Hawaii's slowing economy. In December, the unemployment rate hit 5.5%, the highest in 10 years.

Workers forced to apply for unemployment insurance have had the benefit of federal extensions that allow them to collect benefits for more than 26 weeks. However, all unemployment income is taxable under state law.

S.B. 272 would exempt unemployment insurance benefits from state income tax. That would put more money into the pockets of the unemployed (or underemployed) and allow them to spend that money to buy goods and services for themselves and their families. Think of the multiplier effect of the money that will circulate in our economy.

The ILWU urges passage of S.B. 272. Thank you for the opportunity to share our views on this matter.