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Give low-income workers tax break

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The federal EITC has proven to be an effective way to encourage working for a living, by actually helping low-income earners make a living. The tax benefit can improve the fortunes of hard-working people living hand-to-mouth in places with a high cost of living — like Hawaii.

After years of putting it off, the Legislature finally approved an important measure to help Hawaii's working poor — a state Earned Income Tax Credit (EITC), based on the federal credit.

House Bill 209, while less generous than advocates had hoped, represents a milestone for state tax law. Low-income earners would get a tax credit equal to 20 percent of the federal EITC. The credit could save families with children hundreds of dollars each year in state taxes.

HB 209 has been sent to Gov. David Ige, who should sign it. Some 26 states and the District of Columbia have their own EITCs, and it's time Hawaii joined the list.

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The federal EITC has proven to be an effective way to encourage working for a living, by actually helping low-income earners make a living. The tax benefit can improve the fortunes of hard-working people living hand-to-mouth in places with a high cost of living — like Hawaii. In 2015, the federal EITC lifted about 6.5 million people out of poverty, including about 3.3 million children.

Numerous studies have shown that single mothers and female heads of household especially benefit from the wage boost provided by EITCs, according to the Center on Budget and Policy Priorities. They end up with higher incomes overall — boosting the amount of their Social Security payments in retirement.

That's a lot better than welfare payments, and no doubt why President Ronald Reagan, no fan of government welfare programs, described the tax bill that expanded the federal EITC as "the best anti-poverty, the best pro-family, the best job creation measure to come out of Congress."

Still, HB 209 could have been better. One of the features that make the federal EITC so effective is the fact that the tax credit is refundable. The proposed state EITC is nonrefundable, which is cheaper for the state but less of a benefit to the taxpayer.

A refundable credit would have provided a taxpayer with extra money in her pocket at the end of each tax year — a benefit that can offset the effects of Hawaii's highly regressive general excise tax, which disproportionately burdens the poor.

The nonrefundable credit simply offsets or zeroes out tax liability, with no cash back.

The nonrefundable EITC certainly would be cheaper: The state Department of Taxation estimated a refundable credit would have cost $49 million in fiscal year 2018. The nonrefundable credit would cost $12.7 million.

However, refundable credits have more impact: A poor wage earner gets more spending power while pumping money back into the local economy, an added benefit for everyone.

Critics say that the complexity of calculating EITC claims has led to a significant number of errors — an average of 24 percent in improper payments over the last five years, according to the IRS. And while that number has declined since 1999, it's a fair criticism.

However, it's hardly a deal breaker. Compared to other tax categories, the tax gap created by EITC misreporting is relatively insignificant — about 6 percent, according to the IRS. By comparison, the tax gap for individual business income is 27 percent.

Assuming Ige signs HB 209, as he is urged to do, the Legislature should review the effectiveness of the state EITC next year and revisit the refundability provision.

The Hawaii Appleseed Center for Law and Economic Justice advocated a refundable credit set at 10 percent of the federal EITC, rather than a nonrefundable one at 20 percent. Appleseed pegs the state's cost at $24.5 million — more than $12.7 million, but considerably less than $49 million. It's a reasonable compromise for a future time.

For now, low-income workers in high-cost Hawaii could use a break. A state EITC is a good way to give them one.

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