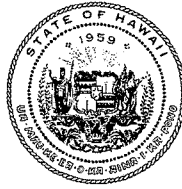


LINDA LINGLE
GOVERNOR

JAMES R. AIONA, JR.
LT. GOVERNOR



KURT KAWAFUCHI
DIRECTOR OF TAXATION

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STATE OF HAWAII
DEPARTMENT OF TAXATION
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**HOUSE COMMITTEE ON FINANCE
TESTIMONY REGARDING HB 1548
RELATING TO TAXATION**

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

DATE: FEBRUARY 26, 2009

TIME: 1PM

ROOM: 308

This measure is an omnibus tax measure intended to stimulate the economy and provide for tax equity. Among other things, this measure provides for a hotel remodeling income tax credit; amends the income tax brackets and reduces the income tax rate; increases the general excise tax rate on written contracts; increase the renter's credit; and reduces the corporate income tax rate.

The Department of Taxation (Department) appreciates the intent of this measure as a means of exploring broader tax policy amendments in the wake of the current economic crisis.

The Department offers the following **comments**—

HOTEL REMODELING CREDIT SHOULD BE NONREFUNDABLE—The Department supports the tourism industry and the importance of the economic activity this important industry brings to Hawaii. The Department acknowledges that having modern and newly renovated rooms are an important factor in maintaining the flow of tourists to this State. However, the Department does not think that a refundable income tax credit is prudent because it rewards unprofitable hotels. If the credit were nonrefundable, it would incentivize hotels to be profitable in order to capitalize on the credit because the hotels would not to have income to offset in order to enjoy the credit.

REDUCING THE TAX RATES IS GOOD STIMULUS—The Department supports the income tax relief proposed in this measure by widening the higher brackets to accurately reflect the cost of living in Hawaii. The Department believes that reducing the income tax rates will leave additional money in the pockets of Hawaii taxpayers and allow for more money to be spent. The bill also reduces the corporate income tax rate, making Hawaii a more attractive place to do business. Lowering the tax burden on Hawaii businesses also increases the amount of money expendable in the economy.

INCREASING THE GET SHOULD BE ACCOMPANIED BY EXPLORING EXEMPTION CUTS—The Department has concerns why written contracts were the target for the increased general excise tax rate. The Department remains open to discussing the broader tax policy amendments set forth in this measure, including potential tax increases. The Department points out that there are many exemptions that could be reviewed. As stated in the bill's introduction, the Tax Review Commission was relied upon as the basis of this measure. The Department points out that the Tax Review Commission's policy regarding the general excise tax was "broad-base and low rate," meaning that in order to keep the rate low many transactions had to be taxed. Exemptions erode the base, leading to the need to increase the tax. In short, the Department simply points out that in addition to exploring general excise tax increases, cutting exemptions should similarly be explored.

REVENUE GAIN—The Department appreciates that this measure is being heard and also results in a revenue gain of \$41.8 million for FY 2010 and a \$91.8 million revenue gain for FY2011 and after.

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SUBJECT: INCOME, GENERAL EXCISE, Adjust rates, additional GET rate, hotel construction and remodeling tax credit, increase renter tax credit

BILL NUMBER: HB 1548

INTRODUCED BY: Chong, M. Lee, B. Oshiro, M. Oshiro

BRIEF SUMMARY: Adds a new section to HRS chapter 235 to allow taxpayers subject to HRS chapter 235 and HRS chapter 237D to claim a refundable hotel construction and remodeling tax credit of 4% of the construction or renovation costs incurred for a taxable year. Stipulates that the credit shall not include the construction or renovation costs for which another tax credit was claimed for the taxable year. The total amount of credits shall not exceed \$4 million. The tax credit shall take effect on July 1, 2009 and shall not be available for tax years beginning after December 31, 2011.

Adds a new section to HRS chapter 237 to provide for the imposition of an additional general excise tax at the rate of 0.5% on the general excise tax. The increase shall not be applicable to: (1) gross income taxable at the 0.5% rate; (2) gross income taxable at the 0.15% rate; or transactions exempt under the current general excise tax. This additional general excise tax rate shall take effect on August 1, 2009.

Amends HRS section 235-51 to adjust the rate schedules for tax years beginning after 12/31/08 as follows:

Joint filers,	1.12% up to \$4,800 taxable income to 8.25% over \$160,000 - 11 steps
Head of Household,	1.12% up to \$3,600 taxable income to 8.25% over \$160,000 - 11 steps
Single, Married filing separate,	1.12% up to \$2,400 taxable income to 8.25% over \$160,000 - 10 steps
Estates and trusts,	no change

As proposed, the measure contains blank amounts for some of the upper income amounts of tax.

Amends HRS section 235-55.7 to increase the income threshold to claim the renter tax credit to \$50,000 for a joint return or \$28,000 for unmarried individuals, increases the amount of the credit according to graduated schedules depending on the taxpayers adjusted gross income with joint/head of households with under \$5,000 in AGI eligible for a credit of \$90 per exemption while those with under \$70,000 in AGI receiving \$15 per exemption; unmarried individuals with AGI of under \$5,000 would be eligible to receive a credit of \$90 per exemption while those with under \$40,000 would be eligible for a credit of \$40 per exemption.

Amends HRS section 235-71 to reduce the tax imposed on corporations, regulated investment companies, or real estate investment trusts from 4.4% to 3.96% if taxable income is not over \$25,000, from 5.4% to 4.86% if taxable income is over \$25,000 but not over \$100,000 and if over \$100,000 the tax is reduced from 6.4% to 5.76%.

EFFECTIVE DATE: July 1, 2009; applicable to tax years beginning after December 31, 2008

STAFF COMMENTS: The legislature by Act 195, SLH 2000, enacted a hotel construction and renovation tax credit of 4% for hotel renovations effective for tax years beginning after December 31, 1998 but before December 31, 2002. Act 10 of the Third Special Session of 2001 increased the hotel renovation tax credit to 10% for construction costs incurred before July 1, 2003. Act 10 also provided that the credit shall revert back to 4% on July 1, 2003 and sunset on December 31, 2005. This measure proposes a similar credit for hotel renovation costs incurred in a taxable year.

The original tax credit was promoted on the argument that the tax credit would be an incentive for hotels to refurbish their properties in order to remain competitive with other destinations around the world. The credit amount was set at 4% to seemingly offset the 4% general excise tax. When 9/11 hit, the momentum of the crisis fostered support for an increase in the credit to 10% to supposedly keep projects which were already in progress going. However, the governor objected and threatened to veto the sweetened credit. The legislature compromised and provided that the 10% credit would be nonrefundable.

While this measure proposes to reestablish a hotel renovation tax credit, it should be noted that no evaluation has been done to validate the effectiveness of this credit in spurring substantial renovations of hotel resort properties. While some may argue that this credit is necessary to make their upcoming renovations pencil out, one must ask whether or not it is the role of government to subsidize private investments. While the credit might be viewed as critical to a taxpayer's project or to the continued renovation of the resort plant, one must ask how long must all other taxpayers suffer the heavy burden of taxation so that this subsidy can be extended to a few?

It would be a very different picture if those who are asking for the subsidy would be willing to forgo other public services or make recommendations on how government can rein in spending, but that is not the case. Now, more than ever, lawmakers need to recognize that they need to set priorities for what precious few dollars taxpayers can part with to run state and local government. One must ask how lawmakers can provide subsidies like this proposal when they raised the general excise tax on all other taxpayers to pay for a transit system in Honolulu? Taking care of a few taxpayers at the expense of all other taxpayers is certainly a cavalier attitude for which taxpayers have long suspected comes with the legislature.

More importantly, if the intent of this measure is to entice hotel owners to undertake major renovations, then the sponsors do not understand what is happening to the nation's economy. In order to undertake large scale construction or renovations, either the hotel owner has to be cash rich or else have access to the credit markets. As the nation now knows, the credit markets have frozen and despite herculean efforts to thaw those credit markets, it will be a long road to recovery. Given that fact, it is doubtful that any hotel owner will undertake new renovation projects, in fact, some who had such projects underway have pulled back or completely shut down those projects for the time being. Thus, the sponsors of this proposal may find this incentive useless in this environment.

This measure would impose an additional general excise tax rate of 0.5%, reduce the income tax brackets and reduce the corporate income tax rates, increase the renter tax credit with an inversely graduated credit schedules to allow more taxpayers to claim the renter tax credit. While the purpose clause of the measure states that the "net effect of these tax changes for most taxpayers would be negligible" it also

purports that the changes proposed in this measure would boost the state's shrinking economy by generating \$300 million to assist small businesses and stimulate growth. With the state's financial condition and the current state of the economy, it is questionable whether such growth will occur - more than likely the imposition of the 0.5% additional general excise tax rate will increase the cost of living and doing business in the state. It should also be remembered that any increase in the general excise tax rate will translate into higher prices of goods and services as evidenced by the imposition of the 0.5% surcharge on the state tax in the City and County of Honolulu that is set aside for the mass transit project.

As lawmakers learned with the imposition of the transit surcharge, one cannot just make a straight line projection of the increase burden of the tax. Because the general excise tax is imposed on both goods and services and at all stages, the tax tends to pyramid even though the lesser 0.5% is imposed on sales for resale. The cost of the full retail rate applies to businesses as well as individuals on their purchases for consumption. Thus, businesses must build the added cost of the additional rate into their overhead and therefore it must be recovered in the cost of the goods and services they sell. The general excise tax is perhaps the worse tax to increase as far as rates because of its broad-based application. If there is any component of this bill that will drive more and more businesses out of operation and with them the jobs Hawaii's people need, it is the general excise tax.

The measure also states that it proposes to increase the food/excise tax credit to make it available to more taxpayers. However, the measure increases the income threshold to claim the renter tax credit and also increases the amount of the renter credit. While it may have been the intent of the measure to increase the food/excise tax credit to counteract the added imposition of the increase in the general excise rate, there is no such provision.

Given the current state of the national and local economies, it appears that the adoption of this measure will contribute to the demise of the state's financial condition rather than improve it.

It should be noted that there are numerous typographical errors and miscalculations within the net income tax schedules as proposed.

Digested 2/26/09



HAWAII GOVERNMENT EMPLOYEES ASSOCIATION

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The Twenty-Fifth Legislature, State of Hawaii
Hawaii State House of Representatives
Committee on Finance

Testimony by
Hawaii Government Employees Association
February 26, 2009

H.B. 1548 – RELATING TO TAXATION

The Hawaii Government Employees Association supports the general purpose and intent of H.B. 1548, which proposes to provide equity to taxpayers and stimulate the economy by increasing the general excise tax, lowering income tax rates, and increasing excise tax credits on rent. However, we are opposed to lowering corporate tax rates and reinstating the hotel remodeling tax credit. According to a recent Department of Taxation Annual Report, corporate income taxes comprised only 1.54% of all state tax collections. With regard to the hotel remodeling credit, we believe that the federal economic stimulus package and state capitol improvement projects should provide ample work for the construction industry.

The State's budget deficit is a reflection of weakness in the national and world economies. Decisions about how to close the deficit must be made carefully. Public investments are important to the health of the State's economy. Improvements to infrastructure such as roads, highways and schools, provide jobs and increases economic activity.

The current budgetary challenges can be addressed in part by increasing the general excise tax rate and offsetting this increase by making the State's income tax more progressive, and increasing certain tax credits for individuals/families. Careful consideration of budget choices, including tax expenditures, is also necessary.

Some tax increases will be necessary to avoid the negative effects of deep budget cuts. While tax increases also reduce economic activity, they have a smaller impact on consumption because some of the money paid in taxes might otherwise have been saved rather than spent. Modest tax increases are less harmful to the economy than significant budget reductions.

The answer to solving our budget deficit is a package of thoughtful proposals, which must include revenue increases. However, these should be offset by lowering income

Hawaii State House of Representatives, Committee on Finance
Re: H.B. 1548 - Relating to Taxation
February 26, 2009
Page 2

taxes and providing tax credits to lower-income families. Thank you for the opportunity to testify on H.B. 1548.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "N.A. Nomura", with a long horizontal flourish extending to the right.

Nora A. Nomura
Deputy Executive Director



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February 25, 2009

The Honorable Marcus R. Oshiro, Chair
House Committee on Finance
State Capitol, Room 308
Honolulu, Hawaii 96813

RE: H.B. 1548, Relating to Taxation

HEARING DATE: Thursday, February 26, 2009 at 1:00 p.m.

Aloha Chair Oshiro and Members of the Committee on Finance:

I am Craig Hirai, a member of the Subcommittee on Taxation and Finance of the Government Affairs Committee of the Hawai'i Association of REALTORS® ("HAR"), here to testify on behalf of the HAR and its 9,600 members in Hawai'i.

HAR strongly opposes H.B. 1548, Relating to Taxation, to the extent that it increases the General Excise Tax ("GET") rate from 4% to 4.5% for the following reasons.

1. The GET is a regressive tax that has a disproportionately adverse impact on poor people who need to spend proportionately more of their income on necessities, such as food and rent, that are subject to the GET.
2. An increase in the GET will increase the cost of living in the State of Hawaii in general, and will increase the cost of housing for renters if landlords subject to the GET can pass on the additional cost to their tenants.
3. An increase in the GET will become an additional cost of doing business in the State of Hawaii and may result in losses for landlords and other businesses if they cannot pass on the increase to their tenants and customers in these tough economic times.
4. The GET (and any increase) is imposed on businesses whether or not they are operating at a profit in these tough economic times.

HAR looks forward to working with our state lawmakers in building better communities by supporting quality growth, seeking sustainable economies and housing opportunities, embracing the cultural and environmental qualities we cherish, and protecting the rights of property owners.

Mahalo for the opportunity to testify.



**Testimony to the House Committee on Finance
Thursday, February 26, 2009
1:00 p.m.
Conference Room 308
Agenda #4**

RE: HOUSE BILL NO. 1548 RELATING TO TAXATION

Chair Oshiro, Vice Chair Lee, and members of the committee:

My name is Jim Tollefson and I am the President and CEO of The Chamber of Commerce of Hawaii ("The Chamber"). The Chamber does not support HB 1548 in its current form.

The Chamber is the largest business organization in Hawaii, representing more than 1,100 businesses. Approximately 80% of our members are small businesses with less than 20 employees. As the "Voice of Business" in Hawaii, the organization works on behalf of its members, which employ more than 200,000 individuals, to improve the state's economic climate and to foster positive action on issues of common concern.

House Bill 1548 is a tax bill to provide tax equity and stimulate the economy by increasing general excise tax rates, reducing income tax rates, and establishing a hotel construction and remodeling tax credit.

While we understand the intent of this measure and the urgency to find a solution to address the current fiscal status of the State's budget, the Chamber does not support an increase in the General Excise Tax. Although the measure reduces income tax rates, the overall result will be a net increase.

Businesses are already struggling to stay afloat and trying their best in continuing to provide benefits to their employees and avoiding job cuts during these tough economic times. Merely keeping up with operating expenses is difficult, especially for small businesses. Therefore, a tax increase will become an additional cost imposed on companies that they cannot afford to undertake at this time.

The priorities should be to save and create jobs and to revitalize the economy. Raising the GET, we believe, is not the appropriate solution.

However, we recognize that during these tough times, we need to remain steadfast in our search for a workable solution and this can't be done unless we work together. Therefore, we pledge to actively participate in discussions in evaluating a variety of options.

Thank you for the opportunity to provide testimony.



Representative Marcus Oshiro, Chair
Representative Marilyn Lee, Vice Chair
Committee on Ways and Means

HEARING Thursday, February 26, 2009
1:00 pm
Agenda #4
Conference Room 308
State Capitol, Honolulu, Hawaii 96813

RE: **HB 1548, Relating to Taxation**

Chair Oshiro, Vice Chair Lee, and Members of the Committee:

Retail Merchants of Hawaii (RMH) is a not-for-profit trade organization representing 200 members and over 2,000 storefronts, and is committed to support the retail industry and business in general in Hawaii.

RMH does not at this time take a position HB1548, an omnibus tax bill to provide tax equity and stimulate the economy by increasing general excise tax rates, reducing income tax rates, and establishing hotel construction and remodeling tax credit.

Historically, the retail industry has opposed any tax increases because of the greater burden on, and subsequent diminished buying power of, our residents and customers.

However, we understand the fiscal urgency created by the challenging economy. **Acknowledging the complexity of this issue, we would like more time to fully analyze this measure's ramifications and impact on our businesses and our customers. We would welcome the opportunity to be part of further discussion to attempt to strike a balance between increasing tax revenue and decreasing spending.**

Thank you for your consideration and for the opportunity to comment on this measure.

Carol Pregill, President

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STARWOOD

VACATION OWNERSHIP

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February 26, 2009

To: Representative Marcus Oshiro, Chair
Representative Marilyn Lee, Vice Chair
House Committee on Finance

Fr: Robin Suarez, Vice President & Associate General Counsel for Starwood Vacation
Ownership

Re: **HB 1548 - RELATING TO TAXATION – COMMENTS**
Agenda # 4: Committee on Finance, Thursday, February 26, 2009,
Conference Room 308, ~~10 a.m.~~

Aloha Chair Oshiro, Vice Chair Lee, and Committee members:

My name is Robin Suarez, Vice President & Associate General Counsel for Starwood Vacation Ownership, ("SVO"). Thank you for the opportunity to comment on HB 1548, Relating to Taxation.

This omnibus tax bill proposes to provide tax equity and to stimulate the economy by increasing general excise tax rates, reducing income tax rates, and establishing a hotel construction and remodeling tax credit.

SVO supports the intent of the bill, and respectfully requests that the committee clarify language in the bill regarding the total amount of taxable credits allowed in any taxable year. It is not clear if the intent is not to exceed \$4 million per year per individual taxpayer or for all taxpayers. Additionally, while we do support the extension of tax credits to stimulate hotel construction and remodeling, we caution against raising the General Excise Tax, which would cause undue burden to a tourism industry that is already experiencing severe recessionary challenges.

Timeshare projects with their high and consistent rates of occupancy and customer satisfaction are a vital part of Hawai'i's tourism industry. In addition to providing traditional resort operations jobs similar to hotel projects, timeshare projects add high skilled and high compensated sales and marketing jobs. As such, timeshare projects represent a valuable and diverse component of Hawai'i's important tourism market.

For these reasons, we respectfully request that you defer decision making on this bill in order to amend the measure with clarifying language.

As always, I thank you for the opportunity to share our views on this matter.