State-County Functions Working Group (Transient Accommodations Tax)
(Established by Act 174, Session Laws of Hawaiʻi 2014)
State of Hawaiʻi
http://auditor.hawaii.gov/task-forceworking-group/

Minutes of Meeting

Date: Wednesday, September 16, 2015

Time: 9:00 a.m.

Place: State Capitol
415 S. Beretania Street
Conference Room 225
Honolulu, Hawaiʻi

Present: Simeon R. Acoba, Chair, Chief Justice Appointment
Ed Case, House Appointment
Mary Alice Evans, Governor Appointment
Steven Hunt, County of Kauaʻi Appointment
George Kam, Senate Appointment
Neal Miyahira, Governor Appointment
Deanna Sako, County of Hawaiʻi Appointment
Ray Soon, City and County of Honolulu Appointment
Jesse Souki, Governor Appointment
Kerry Yoneshige, Governor Appointment

Jan K. Yamane, Acting State Auditor, Office of the Auditor
Jayna Oshiro, Analyst, Office of the Auditor
Pat Mukai, Secretary, Office of the Auditor

John Kirkpatrick, Belt Collins Hawaii
Elizabeth Spleth, Belt Collins Hawaii
Michael Lim, Belt Collins Hawaii
Joseph M. Toy, Hospitality Advisors LLC
Representative Tom Brower, Chair, Committee on Tourism

Excused: Sananda Baz, County of Maui Appointment
Tina Yamaki, House Appointment
Ronald Williams, Senate Appointment

I. Call to Order: Chair Acoba called the meeting to order at 9:06 a.m., at which time quorum was established. The agenda for this meeting was filed with the Office of the Lieutenant Governor, as required by Hawaiʻi Revised Statutes, Section 92-7 (b).

II. Public Testimony

None

III. Chair's Report

a. Announcements, introductions, and correspondence

None

b. Minutes of September 2, 2015 meeting

Draft minutes of the September 2, 2015 meeting were distributed for reference purposes only. Approval of those minutes will be taken up at the October 7, 2015 meeting.

IV. Consultant's Report

a. Revised summary and comparison of allocation models based on working group discussions and presentations (handout)

Mr. Kirkpatrick stated the revised summary integrated the comments made by the WG at the September 2, 2015 meeting.

b. Sharing TAT Revenues in Hawai'i: A Background Paper (handout)

Dr. James Mak prepared a handout entitled *Sharing TAT Revenues in Hawai'i: A Background Paper*. However, since Dr. Mak was unable to attend the meeting, Mr. Kirkpatrick presented the handout on Dr. Mak's behalf. Mr. Kirkpatrick stated that the background paper complements some of the information in the Auditor's Office Chapter 1 draft. It gives some perspective on examples from other states of how these issues have been handled, debated, discussed, and worked through.

The background paper includes useful calculations. One of the calculations Dr. Mak came up with is an estimated tax base for the TAT over a 15-year period. Instead of just looking at the TAT revenues, it would depend on the tax base and the rates. They inferred back the tax base by adjusting for different rates in different years, so we'll have a sense of what the tax base has been; what the TAT has drawn on from year-to-year. Also included in Dr. Mak's paper are scenarios which include models that impact different approaches and what it meant from 2000-2014.

Member Yoneshige stated that Dr. Mak mentions the taxes applicable to the time share units as TOT (timeshare occupancy tax) which should be a component of the WG. However, Member Yoneshige stated as he reads the statute, he assumes the time share component, the room tax was part of the TAT but the way the paper is presented, it's a separate tax. So, for this WG, the TOT is not taken into consideration as he understands it. Mr. Kirkpatrick replied it's for the WG to decide. There are two separate issues here. When they obtained information from the Department of Taxation (DoTAX) that was posted, DoTAX combined the two taxes. Whenever DoTAX say these are the TAT revenues, for such month and year, they combine the two taxes. The consultants had asked the Auditor's Office to consult with DoTAX to separate the taxes for annual totals.

Member Yoneshige said in the previous discussions they had about the amount ($420 million plus) that was derived for FY2014-FY2015, does it include TOT? Mr. Kirkpatrick answered yes. He said it's for the WG to decide and doesn't think the Legislature is clear on this. It becomes really important when you get to any model that tries to divide up the total—is the total TAT or TAT plus TOT. The way Hawai'i has proceeded so far, to say, some goes here, some goes there, the rest goes to the State, it doesn't really matter if you're just talking about TAT or TAT plus TOT. If you're talking only TAT, then TOT is already going straight to the State general fund. You never do a calculation based on the total in the current allocation the way it's set up now. When you go to the recommended model and other models where we're dividing up, we are dividing up a total. You have to decide what that total is, whether it's a total collection of TAT or total collection of both

TAT and TOT. He's leaving it up to the WG. As he reads the legislation, it's never been clear.

Member Miyahira stated this analogy would be like the general excise tax and the use tax levied for two different applications. For all purposes, it's one type of tax because one is for services, activities and things that are brought in but they are complementary. With the TAT and TOT, the Legislature uses it as complementary and views it as one tax. Mr. Kirkpatrick stated it's up to the WG.

Member Yoneshige stated the basis for TAT is the room tax. The only difference with the general excise tax is the type of organization that is providing the room; hotel versus bed and breakfast. Regardless, the substance is it's a tax on a visitor's room. Member Miyahira stated the room rate is one thing and the other is the timeshare principle.

Member Yoneshige stated when we look at the $430 million do we know how much TAT is? Mr. Kirkpatrick replied it's approximately 3 to 5 percent; however, he was not definite on that. We would need to contact DoTAX to clarify that.

Member Case asked if the TOT is allocated differently from the TAT. Member Miyahira said when looking at all the reports it's reported all under the TAT. Member Hunt said the rates and calculations are different. In their models, in estimating the de-facto population, they included that timeshare component; visitors that are owners that are not paying the TOT as part of visitor-related expenditures.

c. Overview and Discussion (handout)
   1. Principles relevant to TAT allocation
   2. Some implications of the models considered by the Working Group
   3. Alternative approaches to TAT allocation

Mr. Kirkpatrick discussed their handout, "Allocation Models for Review by WG." He stated the forecasts are being used for TAT only because that's what is studied in the Hospitality Advisors/Smith Travel research study of hotels, condos, etc. When looking at the TAT revenues, it gives us a conservative working number to look at.

Mr. Kirkpatrick stated that Dr. Mak identified six principles in deciding how best to allocate the TAT revenues in his background paper. The final allocation model should: 1) Comply with enabling statute; 2) Strive to achieve the goals established for the TAT; 3) Provide a predictable stream of revenues to facilitate budgeting; 4) Be (perceived to be) fair; 5) Be simple (low cost) to administer; and 6) Be politically accepted.

Mr. Kirkpatrick also stated that the Maui County Charter includes a Declaration of Policy for its budgeting. He said it's a good policy but it's mainly about how to spend money, not how to collect it, and what to do with collections and how to spend it efficiently. It aligns with the principle of simplicity which has already been stated as one of the important principles with an additional point that if you take that budgeting policy seriously, then obviously you want to allocate the budget in such a way for government to operate efficiently. One of the points that came up within the WG was are we allocating a tax in such a way as to encourage cost effective operations or to encourage people to sit back and just do the same thing they have done before because the money is given. That is the additional principle to think about.

Mr. Kirkpatrick stated in their handout, it provides some of the implications of emphasizing one or another of three key principles: 1) Predictability; 2) Fairness; and 3) Simplicity/Efficiency. He said there are several different ways to accomplish each one of these principles and there is no one way. None of these principles will automatically lead to a solution.

1) Predictability: Allocations should be both predictable and sufficient for the recipient to plan on key activities. To the extent that predictable allocations allow an agency to focus on its core mission, rather than on seeking funds, these allocations encourage efficiency in government. However, predictable funding can reduce incentives to cut costs, unless the funding is tied to particular operations.

   Mr. Kirkpatrick explained that a predictable distribution is not necessarily simple because a simple distribution can become unsatisfactory because it may give us something simple but not adequate to the task that was set out for. For example, what happens when you say something like $82 million and leave that while inflation goes on and $82 million goes from being a very large sum to a relatively small one.

   Predictability could be assured by fixing amounts in dollar terms (with or without adjustments for inflation) or by tying allocations to the costs of specifics activities of recipients.

2) Fairness: Is typically understood in terms of shares of the total amount to be allocated. Attention shifts from the amount received by one party or another to the division of the total collected.

   Mr. Kirkpatrick explained that what we've been grappling with is an essentially contested concept. Fairness is a matter of perspective. If we craft out the fairest possible distribution, you won't get to an agreement. Given concerns such as simplicity, predictability, and getting the model accepted for several years, then fairness becomes the important part of the mix. The Allocation Models Investigative Group's recommended model was to say that predictability and fairness can be worked through with various people sitting around the table.

Chair Acoba said fairness should not be eliminated because we talk about equity in a sense that everyone shares in an increase and decrease or there's a direct relationship between the burden that the counties might have versus what it would get in terms of revenues. Mr. Kirkpatrick said there are lots of ways to talk about equity but there's no definitive way. It's the WG's decision on what model(s) to recommend to the Legislature.

Member Souki arrived at 9:24 a.m.

Member Soon stated in general, this is all good but when you get into the details, for example, "Strive to achieve the goals established for the TAT." Dr. Mak's background paper assumes some goals; they assume it was for tourism marketing and a Convention Center but he's not sure that's totally true. The compensation to local government for their contributions to servicing tourists is also part of the mix or the counties would have never gotten any money. Some replacement for grants-in-aid seems kind of fuzzy, not sure what that meant, he can agree with that but not sure if he can agree with the goals. Mr. Kirkpatrick replied they didn't set out what the goals were for TAT. Member Soon stated it should have been footnoted. Mr. Kirkpatrick said that was a good point. Member Soon stated goals have evolved over time and different goals have been stated from different legislators and this was put together in the Auditor's Office Chapter 1 draft. We have to make it clear that the goals of the TAT have evolved over time.

Mr. Kirkpatrick stated on the models they came up with by way of comparison is called a pure percentage model which would be the simplest possible model, in other words, you have a pie and you divide it into three slices. The only point in doing that is to say, what happens if you have these slices? The way this is set up is, we have a model, take the total TAT revenues from the Hospitality Advisors forecast; slightly different than the ones that we've been using so far. This gives us a starting point for the fiscal year that is based on the Hospitality Advisors information on TAT only. The final numbers may be a little different and a little larger.

3) Simplicity/Efficiency: The simplest of models could take one of two forms: 1) A version with capped allocations for some parties, and the residuum for the State. A variant on the current allocation, with $82 million going to the Tourism Special Fund, $103 million to the counties, and all the rest to the State, exemplifies this form; and 2) A model defined by shares could also be simple. The "Pure Percentages" model would allocate 20 percent of TAT for the Tourism Special Fund, 35 percent for the counties, and 45 percent for the State. It would not have minimum allocations (baseline figures) or limits on the growth of particular allocations.

Belt Collins did a visual presentation on various models using Excel spreadsheets projected on the wall. The WG was able to manipulate the spreadsheets using different distributions.

Mr. Kirkpatrick walked through the following models:

1) Percentages model: This model was created for the WG's review to look at the implications of a straight share distribution. This model was set up to 2025 with the distribution of 20 percent (Tourism Special Fund), 35 percent (counties), and 45 percent (State). He said the numbers show what you'll be getting to given the model of tourism moneys. Exhibit 7 of the handout shows the TAT Allocations, Percentages Model.

2) Current allocation model: This is the current allocation. Mr. Kirkpatrick explained that this is what we've got and you can play with it and change the term to see what might happen. The table projected shows Turtle Bay, Convention Center Enterprise Special Fund, Tourism Special Fund, the counties is $103 million then it goes back down to $93 million and the State has whatever is left. The result is the counties' share, by 2015, is about 25 percent, then it goes down to about 14 percent. That's the implication of the current model if it continues as is. The current allocation is not capped; it's to basically be there until something better is suggested.

3) Recommended model: It divides up TAT revenues as follows:
   - The amount for tourism marketing—Tourism Special Fund—($83 million) should first be subtracted from total TAT collections.
   - Then take 90 percent of the balance and allocate 60 percent to the State and 40 percent to the counties, but in either case, no less than $100 million each. The State would be responsible for expenses related to the Convention Center and all other State spending initiatives, including those already committed—e.g. Turtle Bay, DLNR, etc. The Allocation Models Investigate Group reported that instead of a flat sum, this formula allows the counties to share in further increases in total TAT collections.
   - The final 10 percent would be allocated to the Legislature to be spent at its discretion with the recommendation that at least some of it should be

spent on tourism-related activities. Exhibit 8 of the handout shows the TAT Allocations, Recommended Model.

Mr. Kirkpatrick explained that this recommended model is a “keep on growing” version. In this version, the county share doesn’t change very much, it goes from 29 percent and goes up to 32 percent and the Tourism Special Fund stays where it is.

One of the questions raised is what happens if the Tourism Special Fund gets a share, not a straight dollar amount? Mr. Kirkpatrick stated if it gets 20 percent of the total then everyone is on a shared basis. We are now back to a four-sliced pie; the relevant sizes stay the same over time. The Tourism Special Fund share is set as a share, not a fixed amount.

He further stated that if it’s not fair to keep the Tourism Special Fund as a fixed amount at $83 million, it needs to grow in proportion to everything else. If it grows to 5 percent, it can go up to $135 million and the county’s share will grow; everybody’s total amounts will grow. Keep in mind, in this model, the State is getting both the additional legislative appropriation plus state remainder.

Chair Acoba stated that the State portion goes into the general fund and asked whether the additional legislative appropriation could go anyplace? Mr. Kirkpatrick replied that one of the points Dr. Mak made in his background paper is that it’s up to the Legislature to decide where it all goes. The distinction the investigative group made between the State’s share and the Legislature’s share of the pie is ingenuous. Chair Acoba said he thought the counties get their share and the State gets its share through the general fund which would be consistent with how it is set up today, where is the 10 percent the Legislature can play with that. Mr. Kirkpatrick said, yes, the assumption is that anything with the State is covered through special funds like the Convention Center Fund and Turtle Bay set aside, all of that comes out of the State’s share. Chair Acoba thinks that this may be an additional issue. He said theoretically the Legislature could spray that 10 percent, 80 percent wherever it wants back to the counties. It wouldn’t go back to the general fund. Mr. Kirkpatrick answered that it could go back to the counties and could go back to wherever the Legislature wants to direct it.

Member Case said the word, “ingenuous” is a little strong but he understands the point and there’s a reason for that. Member Soon’s political practicality principle is the fourth principle. He explained what the WG is trying to do is create a model the Legislature won’t play around with because they will feel this is stable over time and people can, within reason, predict what they are going to get.

Member Souki commented he understands the Legislature can do whatever it wants but rational decision making and political decision making, they don’t have to be mutually exclusive. What they are trying to do is offer a rational model upon which political decisions will be made. He was put on this WG because he came from DLNR and its concern was that the Legislature played around with its budget, and that affected its programs. So, moving money from one place to another is affecting State programs. For example, Turtle Bay, it’s great for the public, not a good thing for every program of DLNR. His understanding is that it would give some predictability to the agencies and leave that other big pot of money for the Legislature to do whatever they want. So, the 10 percent is important.

Mr. Kirkpatrick stressed that he's not agreeing or disagreeing, this is one model recommended by the Allocation Models Investigative Group. The additional model he will discuss is called, "Lessons Learned," it's not their recommended model, it's just some of the things they have been talking about. He said the consultants are in no position to say, that this is the right answer. They are there to provide tools to continue to work on what the WG has been working on so ideally, the WG can say it has looked at various models and forecasts.

Member Miyahira said this quantifies the different things we've talked about and we can argue about which one is the best, but for the Legislature, the best service to them is providing them a way we can have some rational basis, what are the goals they may have.

Chair Acoba stated what the consultant laid out for the WG has been very helpful. But he thinks Dr. Mak's point was that it doesn't make sense to put the 20 percent to a special fund. What Member Miyahira said is correct that the Legislature will want to see something.

4) Lessons learned model: This model draws on the Recommended Model:
   - Identify annual baseline shares for Tourism Special Fund, counties, and State based on FY2015 distribution ($82 million, $103 million, and $103 million) increase in line with inflation.
   - Once TAT revenues will clearly exceed the combined baseline shares, distribute these amounts. If TAT revenues appear unlikely to exceed the combined baseline shares, distribute the full Tourism Special Fund share and reduce the share of the State and counties proportionately.
   - Hold the next 20 percent of the combined baseline shares until the end of the fiscal year. If by that time, collections exceed 120 percent of the baseline shares, distribute the 20 percent to the Tourism Special Fund, counties, and State in proportion with their baseline shares (i.e., a division of 29.1 percent, 35.45 percent, and 35.45 percent). If the total collection does not exceed 120 percent of the combined baseline shares, all revenues over the baseline are to be allocated by the Legislature.
   - Additional revenues would be allocated by the Legislature.
     Exhibit 10 of the handout shows TAT Allocations by "Lessons Learned" approach.

   Mr. Kirkpatrick said they started with $82 million because it was in the Act and the Allocations Models Investigative Group wanted to give an extra million. It grows by the increase of the consumer price index so that $82 million in 2015 should buy the same basket of goods as $101 million when you get to 2023. If you grow in line with the consumer price index, then you have that control. That's the change they did with the baseline.

   Mr. Kirkpatrick said one of the things that came up is that revenues can dry up and could fall up to 15 percent in a single year. If you've allocated all of last year's revenues and you don't have 15 percent as much, you're in trouble. You can ask yourself when you're allocating the baseline, does this take us up to 80 percent of last year; in other words, have we set aside or have we spent all of it or less than 80 percent of last year's amount and if the answer is yes, then, as the moneys roll in, you can then add another 20 percent that goes to the Tourism Special Fund, counties, and the State the way it was set up.

Mr. Kirkpatrick stated with the result that you will have a baseline of 100 percent then an additional 20 percent if revenues support it. So your baseline has a 100 percent version and a 120 percent version and basically, the rest goes to the State. This was a two-step version of the recommended models. It is meant to be responsive to the fact, revenues may increase or decline. He also stated that when looking at the baseline, they took all three of these and increased them according to consumer price index. And that is because the expenses of all three increase with the consumer price index. There's no real basis for saying that State, county, and tourism marketing expenses don't increase in good times or bad. In bad times, you have to spend more; in good times, you have more people and there's always a reason to keep on spending more. That argument has already been made for tourism in the event tourism revenues go down, you need to market more and that also goes to the counties and State as well. Obviously, in any time of economic crunch, you will have more demands for services. Everyone has to see their money increase.

In summary, the Lessons Learned model approach provides for predictability and, by some measures, fairness. It is meant to be simple. Because it calls for two phases of distribution, based on revenues collected, it demands an additional step beyond those of the Recommended Model. It differs from the Recommended Model in allotting both the Tourism Special Fund and the counties a share in revenues above the combined baseline, but then limiting their total guaranteed amount. The two-step allocation process makes 20 percent of baseline potentially available to the Legislature for strategic redistribution to respond to near-term events (e.g., a sudden reduction in tourism spending).

Mr. Kirkpatrick explained the two-step version. He said here's the baseline, if you have lots of moneys, you can expand it, and then, as a result, you have two numbers for everyone to look at; one number is the worst possible conditions, the other number is expectable conditions. The results of the counties' share goes from 30 percent down to 25 percent.

The consultants have run all the above models and had additional comments. The consultant would like to present some time series and invite the WG to play with the models because that is what the WG should be doing is seeing the various implications of the models.

Mr. Kirkpatrick stated that Dr. Mak made a contentious comment that the counties cover all or nearly all of the costs of supporting the visitor industry through property taxes already. He said if you look at property taxes on resorts, vacation homes, etc., those cover pretty close to what we all figured out to be, if the counties don't know the visitors' share of county expenditures. It's perfectly sensible. If the counties know they are getting TAT moneys from the State, they better be raising that money through property tax is one way to look at it. If over time, the counties can count on TAT revenues being in a predictable level, there may be less pressure for the counties to take any additional demand for revenue out of resorts.

Member Soon commented that the State gets only enough money to cover its share of the income tax so maybe it should give back the TAT to the industry. Mr. Kirkpatrick would like to defer this matter to Mr. Toy because it's in his area of expertise. If the moneys go back to the industry, then you will have to think of some tax credit and that looks extremely complicated.

Member Souki stated the observation made by Dr. Mak is just an observation philosophically. There are many reasons why the TAT tax is distributed the way it is. One of them is, trying to explore the tax. Another is, if we didn't have to rely as a county so much like property taxes, maybe we could do something like fix roads and improve parks, it's the philosophical reality. It's just the observation that's already covered.

Member Evans said the consultant selected a 15 percent contraction of the TAT, she asked if they have an idea of the historical trend? Mr. Kirkpatrick replied, yes, referring to Exhibit 2 (Annual Change in TAT Tax Base) of the handout. If you take the implied tax base, and you ask, what's the annual change (referring to the brown line on the exhibit), the lowest was 15.9 percent annual change in 2009. This followed a small change the year before, about 3 percent. By looking at this exhibit, in any year, you're not going to see the 20 percent drop, you will see a 15+ percent drop and that's why they thought of a 20 percent holdback, that is to say, don't start giving out the predictable guaranteed shares until you reach 80 percent, then you can give them out that was just the working assumption based on the historical fact.

Member Case asked if this is a constant rate. Mr. Kirkpatrick said this is the tax base Dr. Mak worked out; cleaning out the differences in the change in rate. Mr. Kirkpatrick ran another version using Exhibit 1 (Change in TAT Collections over Time). He said it's not quite the same numbers. He also ran the TAT collections for the period 2000–2014 at 7.25 percent the whole way (referring to the red bars on the chart) and look at the growth and decline and it should parallel from the tax base analysis. These are two slightly different ways of getting at the same thing. Referring to the red lines in Exhibit 2, they did see two years of decline in 2009 and 2010; but even in 2011, assuming you're at the 7.25 percent collection you would be back up to the numbers you have seen before.

Member Case commented when he looked at Exhibit 2 and saw 15 percent, it's not a very big swing for what can happen. From the industry perspective, they don't function in a 15 plus or minus percent contingency situation it's more like 20-25 percent. The reason it becomes relevant is the discussion they had with the investigative group about trying to adjust for a reasonable worst case scenario so that the program wouldn't change just because you face that worst case scenario. There would be that elasticity in the program that would allow for certain flexibility up or down; the counties will get their share and everything we've talked about. What he's trying to avoid, in a worst case scenario, the major reaction from the Legislature is to increase the TAT tax to handle that situation as opposed to having some flexibility to handle the downturn.

Chair Acoba asked why are the counties and the State both set at $103 million? He thought they were working towards a 60/40 model. Mr. Kirkpatrick said the simple answer is it doesn't have to be. When they set that up, that's what they saw coming from the WG. Member Soon stated it was the baseline and you have to go to the bottom set of numbers, $98, $124, and $191 million, that shows you the distribution, that's the 60/40 split. If you get $413 million, the State is getting $191 million and the county is getting $124 million. It's a great model for the State but it doesn't track the counties' model. This caps the counties and that's why it keeps going down. Mr. Kirkpatrick indicated there are ways to change that.

Mr. Kirkpatrick stated that there are two general topics to discuss and then the WG can play with the models. He said that they've talked about historical time series. The key issue has been what kind of variance has been seen. He used 20 percent and the WG's advice is to think in terms of 25 percent as a good working number. Member Case said the 60/40 split throughout plus the 10 percent. But the 10 percent is really important. Mr.

Kirkpatrick characterizes the revenues over the baseline as a "sandbox" that the Legislature can use to allocate to whatever they chose. That was recommended to combine the two-stage predictable baseline. Member Soon stated the difference is how you split up the residual. In this model, it's basically given all to the State. Member Kam stated to philosophically think of what is the best use of the money from a tourist perspective and make sure it's utilized for tourist-related things and that's why he's thinking of 50/50. The State is a big thing, but when you go out there, things are getting done from the county level but to ensure it's directly towards tourist-related functions.

Chair Acoba asked about the $282 million baseline and what happens with the collection? Mr. Kirkpatrick said what happens if the baseline is less than 80 percent of the collection, than there's no next division of the pie. Chair Acoba asked what happens if the total collections are less than $282 million. Mr. Kirkpatrick said it should be more than the $282 million and this number leads to more than that and will need to add that in. A model can be set up so the question is, do the collections add up to the baseline and if they don't, then the obvious thing to do is to prorate it so that everyone gets 93 or 91 percent of what's been collected of what the baseline was.

Member Soon stated the Allocation Models Investigative Group had thought about that and the Tourism Special Fund should be $82 million all the way through. You could end up with the counties and the State getting nothing and that's very unlikely but the marketing arm is to be kept at $82 million as a whole as long as we could. Mr. Kirkpatrick said if that's what the WG wants, they can certainly put that into a version of this model. Member Kam stated they didn't think it would go from $413 million down to $286 million, that's quite a bit for the downside and if it did, just to be sure HTA is funded and everything else would be scaled appropriately at the State and county levels. The TAT for HTA should be solid so that they could make sure marketing was in place.

Chair Acoba asked whether there was a probability that it would go below the $282 million, looking at the historical data. It doesn't start above $282 million until 2011. All the years prior to that, it was less than $282 million. Mr. Kirkpatrick said given where we are today, $282 million is a fairly small share of total collections going forward even with the fact that things could go up or down from year to year, people will still come to Hawai'i even if it's at the $282 million.

Member Soon stated the reason they kept the Tourism Special Fund number as a fixed number goes back to Member Yoneshige's point, in hard times, you want the money there to be able to pull ourselves out. But in really good times, you need to expend dramatically more on the marketing side. We kept it whole and made sure HTA were always first in line. Increasing it by the Consumer Price Index (CPI) makes a lot of sense. Mr. Kirkpatrick said if you grow it by CPI, it's keeping it whole.

Mr. Kirkpatrick commented that another point is that the recommended model creates a tricky situation, when you get to the "sandbox." When you get to the Legislature saying you have additional money, the legislators will hold hearings and all sorts of people will show up. It seems the visitor industry and to some extent the counties, will be told, "You already got your piece, go to the back of the line." So, this is something for the WG to consider whether in fact it's time for the Legislature to make appropriations for special purposes, you may be creating a disadvantage for the counties and the visitor industry.

Member Miyahira stated in drafting legislation, having CPI measures will be a little bit tricky in trying to implement. Member Hunt said they've used CPI before in one of their tax-capped measures for homeowners. He said you have to be aware that typically the CPI comes out in February. When you're setting budget, you're going with the budget period. Mr. Kirkpatrick replied that you would need to go back one quarter to the December quarterly statistical and economical report from DBEDT and take the year on year and use that. Member Sako stated the harder you make it, the Legislature will reject it. Mr. Kirkpatrick asked what would be best—DBEDT is saying, 2.5 percent and 2.7 percent increase over the next few years.

Member Yoneshige stated there are negative CPIs and there are multiple indexes which are the first half of the year, last half of the year, and all-inclusive consumer goods, so it's very complicated. A DBEDT index, or a very simple index that there is no question when that index comes out June 30th, that's the number to use and no adjustments or a fixed percentage. Another item they looked at was CPI adjusted-type legislation is the fact there are times, in 2008 and 2009, when the CPI index went down, it was negative, how do you adjust for that? He said Dr. Mak's background paper also writes about putting ceilings and floors into the legislation. If you're going with percentages, and putting ceilings and floors into the legislation and if we do use an index and the index is negative, there will be no change. On the upside, if something happens to inflation and it goes through the roof, maybe capping the HTA share by an amount, 5 or 6 percent, provides the limitation on unwarranted growth. By looking at this model, he is struggling with it because if the basic model was 60/40, what's causing the proportions between the counties and State to be so disproportionate in the end.

Mr. Kirkpatrick stated what happened with this and the way it was set up, the counties get a baseline, then they get the "dessert" baseline and then when you get beyond the baseline, everything goes to the State. This is the way it was set up. It doesn't have to be set up that way. It can be set up in a way such that the counties and the State divide up the rest. Member Yoneshige stated he's just trying to understand the mechanics of the model. If it's 60/40, how does it end up with the State side being so much bigger in 2023. Mr. Kirkpatrick answered, if you look at what the State's total is, the State's total is everything that is left, which is the total minus Tourism Special Fund and counties.

d. Workshop (handout)
   1. Tourism and revenue forecasts
   2. Ways to calculate floors, shares and ceilings
   3. Variance in allocations over ten years

Mr. Kirkpatrick stated when you set up floors and ceilings, there are different ways to set them up, either fixed, CPI or straight percentage can take you to very different places. If it's something that depends on shares of basically total in-flow, then if there are fairly big market changes, then those reset; instead of having a line that goes up like this, you're resetting something close to where you started. Meanwhile if inflation has gone up, even with the change in total going up at 3.7 percent; CPI has gone up 11 percent, your money doesn't go as far as it did before. There are different ways to calculate floors and ceilings and there are different implications. It was meant to be a five-year example, something to play with.

Referring to Exhibit 4 DBEDT Forecast of Population and Visitor Spending, to 2040, they took the rate of change in visitor expenditures and applied it to the TAT. Using $425 million in TAT revenue; it went up for five years at a rate of 3.5 percent and another five years at 3.3 percent. That was the complicated economic rationale. The Hospitality Advisors has given us a better model and we're using those numbers now. The DBEDT rate of change was 3.5 to 3.3 percent. The Hospitality Advisors model goes up at a faster rate although it declines over time. Mr. Kirkpatrick stated that there's an exhibit that had two total collection forecasts, what if the State and counties succeed in getting everybody to pay the TAT. The counties are going after that because they are looking for illegal vacation rentals. Airbnb would love to pay TAT so, that would make it legitimate. If you go back to that exhibit, instead of 50 percent of total visitor spending on lodging, 70 percent estimated visitor spending on lodging. What if 70 percent of that was the tax base, then, you would get up to this higher number instead of $676 million, you would be over $900 million. The only reason why it might be thinkable, if all the visitors start going to Airbnb and the hotels start hurting and we have to collect that money. Then of course, you start getting all kinds of economic pressures that the hotels will be under severe pressure and then it becomes very complicated.

Mr. Toy explained how he does the monthly hotel survey. He said they have 85 percent of the hotel rooms surveyed and it's pretty good coverage; with the remaining 15 percent, they do an estimate. They have tracked it every year. When he first started, he would check with Dr. Tian, State Chief Economist at DBEDT, to see how far the TAT was in terms of the tax base compared to our revenues generated. The revenue information they received are from the financial statements of all the hotels which is accurate information. Referring to a chart, the first line, statewide hotel and county room revenues, that's pretty much where we are at; then it's reconciled back to the average daily rates; the way the numbers are set up, this is being done on a calendar year basis. When he took half of year 2014 and the other half of 2015, we are within 3 to 5 percent. For timeshare units, he said they do quarterly timeshare surveys, on average, the timeshares are running at about 90 percent occupancy and those are occupied rooms regardless of whether they are occupied by timeshare owners or exchangers. When they have capacity, they will sell these hotel rooms as hotels so, there's a daily rate for that.

Mr. Toy said roughly 18 percent of inventory of timeshares are free-sale into the hotel market. For example, if you're staying at the Hilton Hawaiian Village and they put you in a timeshare unit, they don't think about that because they are thinking a body in that hotel room. This is why they have the hotel TAT and then there are the individual vacation units. That's based on the visitor plant inventory. The numbers are elusive. He explained that what's been happening over the last five years is the substantial number of resort condominiums have come up; and we have a slew of resort condominiums coming up in the next five years and beyond that. The instance of individual vacation units is just going to increase. With air bed and breakfasts, it's a pervasive model because you don't have to necessarily be in a resort condo; whether they will be paying their fair share of the TAT is a question. At the Hawai'i Tourism Conference a few weeks ago, he convened an alternative accommodations panel and included the air bed and breakfasts and they are quite anxious to work with the State to try and get ahead of the curve and not have these flashpoints.

Mr. Toy stated that there's an anomaly here. In years past, he's done surveys on individual vacation units and they are running at about 70 percent capacity. The average daily rates have gone up as well. This is just based on his industry experience; it's not based on a survey. He said for the individual vacation units, they are trying to get a handle on the number of units and the numbers are elusive. There's not much data out there concerning what people are charging. Air bed and breakfasts say they do collect data and they can provide that as a basis for TAT. If you look at the total and see what the TAT is, their estimate was $395 million in 2014. It was a little below what the fiscal year was. He said as Mr. Kirkpatrick pointed out, when they came out with the initial numbers, they only had the hotels so there was a gap of what they had versus what DoTAX was reporting. The difference at that time was the TOT. He did his calculations and these are the numbers he came up with, which are fairly close to DoTAX's reporting. After receiving the schedule, the TOT numbers are included, roughly $33 million. To do this on the individual vacation units, he just made an assumption and he knew his assumption was incorrect that everyone had a TAT but obviously that wasn't the case because now they have $33 million in TOT which means most of these individual vacation units are not paid.

Member Case stated their inventory on the individual vacation units are lower than HTA. Mr. Toy said the HTA double counted inventory. The inventory is in the individual vacation unit study and it's counted as hotel. Member Kam asked Mr. Toy to guess at the right number. Mr. Toy replied that SMS has estimated 26,000. If you want to get the true essence of a single unit, it is about 15,000. With Airbnb, it expands the inventory. As great of a destination as Hawaiʻi is, Airbnb are latecomers into the industry. Whenever there's a pool or a check-in area at a condo, they have to put it in the reservation system. You can mandate that number because it's a big capture. There are ways to govern this a little bit closer.

Member Evans asked if the WG were to make an assumption, the counties are deadlocked, the TAT units, DoTAX is determined to collect the taxes due and DoTAX will be going to the Legislature and ask for additional tools to collect the taxes, GET and the TAT, is it consistent with the model Mr. Toy projected. Mr. Toy responded that in his model, it is assumed that all the individual vacation units are compliant with TAT. Mr. Kirkpatrick stated we have 9,000 individual vacation units and in the discussion, the number might be closer to 15,000, so there's about a 60 percent compliance. To get an inventory of the TAT licenses, the TAT license may represent a lot of different rooms and it may represent a pool, etc., but for the individual units, if it's individual, there should be individual TAT licenses. It would be good to know if DoTAX can pull that and try to categorize the TAT licenses to match up; only about 1,200 are compliant. There are ways to do it.

Chair Acoba asked what is the significance for the WG? Mr. Toy replied for the purposes of this data, the significance is apparent when you do alternative allocations to see how that might change in the future. Mr. Kirpatrick stated another basic reason is that to say let the 2015 number be $425 million and that seems reasonable. Even though the numbers keep on shifting, there are question marks no matter which way you play it, this gives us a better starting point. Mr. Toy said when they pulled the numbers, it's from the financial statements; a lot of the companies are publicly-held companies. They are comfortable with the numbers that they receive.

The Chair called for a recess at 10:40 a.m.

The meeting was reconvened at 10:50 a.m.

At this time, the consultant held a workshop in which the WG had the opportunity to work with the different models based on various assumptions.

Mr. Kirkpatrick referred to a spreadsheet projected on the wall that included the models that were previously shown with certain assumptions. He referred to columns that included the following models: simple share; current allocation; and recommended. There are versions with tourism share; the current spreadsheet shows that the Tourism Special Fund grows with a fixed rate at 2-1/2 percent; some things were put in with CPI; for the sake of looking at it, a couple more things were done, the additional legislative appropriations was cut back just to see what would happen. As of 2017, SARS hit all of China and Hong Kong and Japan stopped going any place too and things didn't get any better in 2018 and then, things start to get a little bit better, and so forth.

Referring to a model with the entire visitor industry and the entire State takes a significant hit and in this model, they cut it by 20 percent down in 2017 and by 2025 it was up by almost $550 million.

Member Soon referred to the first spreadsheet projected on the wall. Mr. Kirkpatrick explained that it was the first, simplest model he set up. Member Soon asked if it is defensible and how would the WG argue that. Member Hunt said he thinks 35 percent is very close to 44.8 percent of the established original 7.25 percent that was the original establishment for the cap. Member Soon asked how would the WG defend that. Mr. Kirkpatrick replied the 20 percent number is based on what everyone agreed made sense and is a baseline for tourism; it starts you off with $83 million. The 40 percent of the remaining 80 percent would be 32 percent. Member Kam said he likes that model because it's more for the counties.

Mr. Kirkpatrick stated if you do a simple three-sliced model, 20 percent for the Tourism Special Fund; and you put in the remainder 60/40, this is what you get. Both Member Kam and Member Soon agreed with the 65/35.

Member Soon stated any time the Legislature decides they want something out of the TAT, everybody loses. They will add that additional expenditure and that erodes our consistency and predictability. Member Souki asked if that comes out of the 45 percent. Mr. Kirkpatrick referred to the simplest model, the three slices of the pie. Member Soon said it's the simplest but is it defensible. Member Souki was trying to understand if the State decided to fund something, it would affect, for example Turtle Bay. Member Soon said this is the model, philosophically a few reiterations ago, every time the State decided they wanted to fund a DLNR project or something like that, everybody loses a piece. If the Legislature decided to fund something, it comes out of the State's share, just like anything the counties decided to fund would come out of the county's share.

Mr. Kirkpatrick stated the next question—which will be a "sandbox"—is what happens, if in a given legislative year, the Legislature says that they really need to put $25 million a year to State parks on the Big Island, does that next year go into the fixed State's share or does that still stay above the line, that's the problem we always keep talking about. And then, the current allocation, we have basically some things that are above the line; the Convention Center and Turtle Bay are first in order and one of the things we've been working towards is getting that into the State's share.

Chair Acoba stated he believes that it is one point of view and to make it a little more balanced. Member Hunt asked the consultants if they knew what the amounts were. Mr. Kirkpatrick replied that the current allocation is: Convention Center is $26 million; Turtle Bay is $1.5 million; Tourism Special Fund is $82 milllion which includes certain parts has to be spent a certain way. Also, the counties have the rider, that in the future, EUTF provision gets shared. This is the way it's set up right now, the State share has a special and development fund which is the DLNR, $3 million which is from the State's share. As he understands the way it's been written, it's not quite up there as the Turtle Bay and it does get more complicated.

Chair Acoba stated according to the handout, there are two ways this is set out, one way is to keep all the stuff that's there and then apply the ratio to whatever is left. Either the Legislature will need to unravel all those commitments or the second would be, a proposition coming out of the WG would be to treat the State as having been taking the responsibility for some of those items. If you saddle the State with these already fixed items, it's not really a truly 60/40 split or if you allocate those items, than it would be far more comfortable, appearing before a legislative committee if you have some rational basis of how to split it up. He mentioned that at a prior meeting, during which Member Soon was not present, that Turtle Bay should go to the counties if you think about direct benefit versus costs even though the State set up the funding mechanism. Based on legislative history, the Convention Center should go to the State, if there is no legislative history, it should go to the counties, or it could be split. There are all different kinds of ways to do this but how to allocate the fixed items that are already there would really impact the division.

Member Hunt stated that's where they're headed, we have those fixed costs. If we revise the percentage by incorporating those hard costs much like we've done with the $83 million and we revise the percentage instead of the 35/45, and figure out what the percentage would be and all future acquisitions by the State would come out of the remaining share. When incorporating the existing debt into that percentage, but no more, instead of 45 percent, you get a little higher share because we are already incorporating the existing obligations that are in there and even more saleable to the Legislature, once those bonds are paid off, they are not going to re-adjust those shares, you can now go out there and do other things with those moneys.

Member Sako stated she doesn't understand how Turtle Bay and the Convention Center benefited the counties. Chair Acoba answered it benefits the City and County of Honolulu. Member Kam stated what if you preserve something on the Big Island or Kaua‘i, the counties probably cannot fund it themselves. The State needs to do that. There are some things, even though specific to that island, the county cannot pay for everything and the more we bucket and allocate on the 45 percent, it should all go to the State. It's just numbers but they have to be fiscally responsible in the bucket because the 35 percent should be for the counties and he's leaning more towards the counties so they can direct it for their specific needs that are tourist-related, compared to a general fund that can be used for all kinds of things.

Member Hunt stated if we're going to create that "sandbox" bucket, you are already starting with some sand in it. You may have some extra that the 10 percent can afford to acquire, but we need to look at the already encumbered portions. Member Kam stated actually, the "sandbox" opens up a whole new can of worms compared to the 45/35/20 split.

Mr. Kirkpatrick asked what happens to those "sandbox" dollars for next year. Member Souki stated that he agrees whole heartedly with what Member Kam is saying in trying to say that the existing Turtle Bay debt should be part of the 45 percent and not increase the 45 percent. Member Souki's rationale is, you cannot base the rational model that the WG developed on things like Turtle Bay which he feels is ad-hoc; it's not even part of a master plan, they wanted to solve for a group of vocal people in the community who didn't like the development that was already approved and in order to do that, buy it. The WG is trying to develop a rational model and that is not rational.

Chair Acoba stated the 40/60 split they can play with that but that was derived from Member Yoneshige because he looked at the CAFRs. So, it was sort of a compromise of all these factors. Now the WG has come up with 45/35 split, how do you justify that? Member Kam said the 45/35/20 split is justified from what the counties are getting. Chair Acoba said there are data that support what Member Yoneshige stated. Member Kam said the WG has that same data on a rational basis from the counties as it is today.

Member Hunt stated part of the issue is the group only discussed expenditures and didn't talk about revenues and that's part of the problem. If you look at items that are high nexus to tourism like airports and harbors; they have revenues; concession fees, gate fees, etc. What is the disparity? What are we subsidizing? Maybe they collect 100 percent of their expenditures in fees and maybe they don't. Because we are looking only at expenditures, it definitely will be one-sided towards the State because they have a much larger expenditure.

Referring to a spreadsheet projected on the wall, Mr. Kirkpatrick said they did do an analysis of total expenditures and tried taking out proprietary funds and things that basically pay for themselves and that didn't shift the balance. But if you ask do you do that for things that are tourism-related, the point is very good. The State's a lot better at getting things that seem tourism-related to pay for themselves than the counties. That would shift the needle on this one.

Member Case asked a question in the straight share approach, it's not the counties' share of the total between the counties and the State; if you take out the Tourism Special Fund, the two lines, 25 and 26, that split is more towards the 40/60. Mr. Kirkpatrick replied, if you did it with the 40/60, it will be 32/48 split. Member Case said it's the 40/60 on the 80 percent. Mr. Kirkpatrick did some calculations to show the 40/60 after the special fund is taken out.

Member Miyahira said the Legislature is being creative in their own way. There might not be fixed things. For example, the Convention Center, we may not have debt service but there's going to be costs and there will be other kinds of costs. There will be other Turtle Bays someplace else. Member Kam stated he rather have the counties because the counties can fight for it at least, and justify it. Member Miyahira said it might be rational to have a "sandbox." Member Hunt stated the counties do pay for the Turtle Bay, what was owned by a private entity, what is the tax base, you give up to State entity which is non-taxable.

Member Soon said it's a question of who makes the decision. Chair Acoba stated the Legislature does both, it appropriates for the State and counties. It's almost like a grant-in-aid for the counties and the State's share goes to the general fund and they can do whatever they want with it. In Dr. Mak's background paper, he said the three taxes (hotel room, property, and vacation rentals) they raise enough revenue to take care of all the expenses to take care of the tourists. So in effect, the TAT moneys is revenue moneys, not reimbursing the counties for expenses because the counties are being paid through the three taxes for cost of services to the tourists.

Mr. Kirkpatrick said Dr. Mak made that point but there are various ways to see it. One way to see it is if the counties can expect the State to give them what they should get out of the TAT or they have to raise it out of property taxes. Member Hunt stated that's the delicate balance, we need to make the hotel prices affordable in all taxes. If it's strong-arm on one of the taxes, then you will see the other taxes go up. We are all in this pool together and we want to make sure we do things nicely and fairly.

Mr. Toy stated that's exactly what happened in the second half of last year. We can see a lot of push back on pricing and taxes and people will start complaining about that. Right now Hawai'i is on the radar because of the GET and TAT tax issues and higher pricing and then we start to see a lot of diversion in the market. Member Sako stated if we're saying the real property tax is paying for tourist-related expenses, we can raise the tax but there is no reason to market any of the islands. Chair Acoba stated Dr. Mak's point is we should take that into consideration which the WG is not, revenues aside from TAT that cover services. Member Soon stated the counties will be happy to look at property taxes if we look at all taxes from the State as well. The revenues of the State are dramatically higher. He doesn't know if the group really wants to go there because it gets really messy.

Member Souki said this goes back to the very first conversation the WG had which was, there's this TAT tax, what is it for, how should we spend it, and then it went into the conversation that maybe it should go into the tourism nexus because that makes sense whether it's historical or not. When we fast-forward to today, never mind the TAT because we should pay with these other taxes, it takes us away from where the discussions first started. We have this big pot of money, who should decide how to spend it. When he looks at the three containers there, the Legislature, again, might do whatever they want, it makes it harder for them when an earnest group like us comes up with these things, this is a rational way to do this. If they get out of the 48 or 45 percent, that means all the counties descend on the Legislature and it makes their day hard. If they stay within the 45 percent, they can buy whatever they want, spend whatever they want, and do what they want. Going back to Member Kam's point, when looking at Turtle Bay and other costs, it fits comfortably in the 45 percent and they have a lot more money to spend. If we say the two fixed costs are part of the 45 percent, what's the percentage on that? Mr. Kirkpatrick answered the Convention Center is $26 million.

Chair Acoba asked the WG if they want to stick with the percentage model or go with what the consultants came up with; do the baseline and adjust depending on the revenues. Member Kam expressed he liked what Mr. Kirkpatrick presented which was the 45/35/20 because it's very clean, specific, and weighted appropriately. Mr. Kirkpatrick stated the 48/32/20 is the same as the 60/40 which is also possible.

Member Case stating the four different principles—simplicity, fair, predictable, and practical—fair would depend on revenues if it goes up or down, someone's going to feel if it's fair or unfair. The fourth principle, practical, he doesn't know if that's practical over time because this is something to monkey-around more than the 45/35/20. There's exposure to the principle of predictability for the counties and HTA. It concerns him that this may not work as well as the "sandbox."

Mr. Kirkpatrick said going back to the smaller "sandbox" variance they were playing with and that version has the Tourism Special Fund growing at 2.5 percent. Then divided all the rest up in a pie, it did not prioritize the "sandbox" additional appropriation. This ends up being, 10 percent remainder goes to the additional legislative appropriations; what's left after the additional legislative appropriations plus tourism is divided 60/40 between counties and the State. What happens if the market goes down, the total numbers go from $413 million up to $441 million, and then a 20 percent drop, and this was for the 2017 epidemic.

Member Soon asked what it would be like for the smaller "sandbox." Mr. Kirkpatrick replied, the "sandbox" still exists, it goes from 35 percent down to 26 percent, there's still something to play with. What they have done with the "sandbox" is what they identified are new moneys to play with.

Member Yoneshige stated if the economy goes down, that's when the floor will increase to protect HTA. Member Kam stated we can do the 20/35/45 with a 20 percent down shot based off 80 percent. This can be done on the down-side cap. Member Yoneshige stated if we have a worldwide epidemic, it could affect the CPI index and that's where the Tourism Special Fund will be affected.

Member Kam stated with the 20/35/45, if it goes down, if you take 5 percent from the State and county, it's up 30/30/40 if it hits that down side floor. The county and State's share will drop but it will keep funding the Tourism Special Fund.

Mr. Kirkpatrick said speaking of predictability, once you get past the tourism moneys, counties go from $125 to $135 down to $101 million; given county budgets, that's a big hit. And given the TAT is a sizeable percentage of county revenues, it could be a 10 to 15 percent hit to county revenues. The way this is set up for the moment, there's no protection for the counties. Member Soon said he doesn't want to speak for the counties, but he is willing to take that chance because they will be also enjoying the upside. As of today, because they are locked at $113 million and $93 million next year, they have no opportunity to participate in the upside.

Chair Acoba asked if you put all the fixed costs for the State, if there's a down turn how would it affect the State. Mr. Kirkpatrick said to keep in mind, if the TAT goes down, so does the GET. The State will get hit a couple of times. The counties are slower to react because property taxes don't go down as fast. Member Souki said both the State and counties need to observe that counties run more lean than the State.

Chair Acoba wanted to say something about equity. He said because in terms of treating everyone the same, one equitable way of doing it is to separate present fixed costs from the formula; apply the formula to what's left because those are already established costs. That would be fair because it wouldn't impact the State or the county. The other way might be to have some rational basis for looking at each one of those items and decide whether they should be treated equally as part of county or State or all of county or all of State, depending on whom it directly benefits. This would be an equitable way of allocating the costs. It seems less equitable to put all of the costs with the State because obviously the State's share is really not the 60/40. This is what concerns him about equity and how do you sell it to the Legislature.

Member Sako stated most of the things that have happened to the counties have never been equitable. Even the EUTF and mandating that, they have to pay that. They took away that decision making process from them out of their budgets. So now, because they don't pay it, that's where the TAT pays. The Legislature keeps doing that to the counties and making decisions for them. If the State's making the decision, they can pay for it.

Member Case commented on equity and things adjust over time. If you set a reasonable, rational basis to the allocation of the TAT, it will adjust over time and if we can do something rational with the TAT.

Chair Acoba asked what would be the rational basis for putting all the fixed costs entirely on the State. Member Case said the State decided on and administers that. Because the Legislature decided to fund those items and the same argument with counties as well, things they fund are the State's responsibility. State versus county parks, who's park is it, State or county, who should pay for it. If the WG goes down that road and tries to unwind all of those decisions, the WG will get itself all tangled up; they will not be able to come up with a way of defining it so the Legislature understands. Chair Acoba stated it should be set aside and the formula applied. When you allocate, there should be some rational basis on whether it is a county benefit versus a State benefit. In a situation like the North Shore, the Legislature wasn't thinking in terms of saying if it's a State obligation into the future where we have a situation the tax will be spread out among the counties; it's a different context than what the WG is proposing.

Member Case stated he doesn't know how that formula will be crafted for the Legislature to administer year-to-year. Chair Acoba stated after the fixed costs are paid, into the future, then you would have the pure formula. But until then, the State carries the burden of paying.

Member Souki stated from the conversation, there seems to be things that are mixed up. It is wrong terminology if State benefits, county benefits; it's who's deciding. The State's going to decide what the Legislature spends on "x." They should think about how it impacts State programs. The counties will decide to spend on something, they should think about how it's going to impact them. The argument that the State made the decision to put it with the State and allocate the money is a powerful argument.

Chair Acoba said the fairness is in the context in which you make it. Imposing this new context, what they did in the past, the Legislature wasn't thinking that if we pay for the North Shore than, it's a State burden. Mr. Kirkpatrick said what the Chair is basically saying is that the three-slice model, but first slice is not the Tourism Special Fund, it's the Tourism Special Fund plus fixed costs that have been set out there in previous legislative sessions. Does it include the $3 million to DLNR, he's not sure. It's an operating cost, not a capital cost. It's a long-term commitment. Instead of $83 million, it might be $103 million and the rest gets sliced up.

Member Case stated another observation that he's not happy about including the State's fixed costs into the State's bucket is because the counties came up with a range of the CAFR analysis of State versus counties, the counties are taking a little bit more on some things and should have higher reporting.

e. Next Steps

Mr. Kirkpatrick stated he will be glad to share with the WG versions that have been discussed and the variances that were plugged in. They will finalize it and send it to the Auditor's Office for distribution.

He said what's next really should be, what would the WG like to have. They would like to end up with the WG's preferred model, accepted and finalized at the next meeting. What does the WG want the consultant to prepare to get us there?

Chair Acoba asked the group for a discussion on the various models: two-stage model, baseline model and percentages model. Member Evans stated it's simple to understand. Member Kam said he still prefers the 20/35/45 because it's the cleanest and fairest. If you want to put a little cushion there, you can and you can justify the 20/35/45, it's a question if you want a cushion there or not.

Member Case said he has concerns about practical applications; there are a lot of compelling reasons to go with straight percentage versus "sandbox" model. He feels they have the relative concepts in place; HTA rising with reasonable CPI. The 60/40 model is solid and defensible. He doesn't know what the actual numbers look like but prefers the "sandbox" and straight percentage right next to each other and would run the baseline according to their projections for one of the options of the two and run the 20 percent scenario again. What is the bottom line number to the counties and the State?

Member Case also stated that there are four different scenarios. For the top row, you have the straight percentages; the bottom row, you have the "sandbox" model. One subset of that has no reduction in 2017 and 2018 and then, run one for both those scenarios with 2017 and 2018 with a 20 percent reduction because it will provide some comfort of what the down side will be so we can anticipate a severe downturn in the economy.

Member Hunt stated it would depend on how you couch what the “sandbox” is used for and what it’s already committed to. If we’re looking at the existing debt for the Convention Center and Turtle Bay, if we use the 10 percent “sandbox,” then we would include that as part of the funds we are already receiving, otherwise, would we like to see a smaller “sandbox.” He’s thinking more of the simplicity; if they need to see modification on debt service.

Mr. Kirkpatrick said for Tourism Special Fund, Convention Center, and Turtle Bay become existing debt which is the top line straight share and State and county divide the rest. Member Kam stated the Tourism Special Fund should have some conditions and not just an open checkbook and to take care of the down side if it’s a straight 20 percent. Member Miyahira stated the group needs to account for the Convention Center and put it into the “sandbox.”

Member Soon said what he thinks Member Miyahira is saying is to create the “sandbox” but it already has the fixed costs in it. It will still have $3 to $4 million extra and as you write down the debts, the “sandbox” continues to increase. They have always had the 10 percent share and they have already used up part of it.

Member Soon stated he likes Member Miyahira’s idea and likes the “sandbox” model to find some common ground and compromise, we need to split the encumbered costs. By putting it into the current “sandbox,” it says to the Legislature if they make a decision, it comes out of the “sandbox.” And he also likes the 60/40 split. He would suggest keeping the $83 million and appreciate by a fixed rate as opposed to 20 percent.

Chair Acoba asked what about the “sandbox” with unencumbered funds for the Legislature. Member Soon said the “sandbox” has 10 percent and it includes all the current encumbered funds. Member Kam suggested 20/35/35/10 percent “sandbox”, 20 percent Tourism Special Fund; 35 percent State; 35 percent counties; and 10 percent sandbox.

Member Souki said he’s thinking without the “sandbox” because the State will look at it as general fund so you may as well just call it general fund; the 45/48 should include fixed costs. Member Sako agreed with Member Souki to say no “sandbox.”

Member Yoneshige agreed with “sandbox” net of the encumbered amounts without current fixed costs can be netted out from the 10 percent and the 40/60 split. It would be the 10 percent share; all the fixed costs would be minus from the 10 percent share so the Legislature could have it at their disposal the net amount. Chair Acoba stated the fixed costs would exceed the 10 percent.

Mr. Kirkpatrick explained the way it is set up, we are telling the Legislature they have $5 million to play with and maybe $7 million the next year, then everything falls apart, then, to cover fixed costs you need to go back to the State pool and no extra funds to play with.

Member Evans said the debt for Convention Center and already approved Turtle Bay and DLNR should not come out of the State’s share fluctuating percentage but basically an obligation from the TAT. With the Tourism Special Fund, she likes the idea of a slow increase but not necessarily a share of the upside or downside. She is in favor of the “sandbox” but not with the debt obligations.

Member Yoneshige stated he's proposing the "sandbox" amount, less the fixed costs. It would be 10 percent less the fixed costs. That amount would increase as the debt service is reduced.

Chair Acoba asked how would the "sandbox" work if it's to cover fixed costs. Mr. Kirkpatrick replied, if it's to cover fixed costs and additional appropriations, his understanding is the additional legislative appropriation is additional appropriations, not fixed costs. Given the fixed costs are already in the range of $30 million, the 10 percent additional legislative appropriations is pretty tight. It will be even tighter if there's a downturn.

Member Case stated the way it's constructed, the difference is priority. The 10 percent is supposed to be the part of it that floats up or down depending on the TAT. The State and county get the 60/40 share, fairly stable as to HTA, than the 10 percent would go up or down. It's not new appropriations it's a recommended allocation of the general fund under a specific formula. What he likes about Member Yoneshige's idea is that it does provide the State with some incentive. Chair Acoba asked if you treat the "sandbox" as part of general fund, you don't need to separate it out. He figured the original thought was that the Legislature would want to spend some money that would not be conditioned on anything. The differentiation would be the other State money goes into the general fund.

Member Soon stated to Chair Acoba that he does have the right way it was originally proposed but it helps the State administration people to know that reducing the discretion a little bit of the Legislature.

Member Miyahira stated with the models that we have and say, these are the various models, these are the pros and cons. We may be able to agree on a preference to set it out for the Legislature to look at it with numbers.

ASA Yamane spoke about logistics, for every model that has been discussed, if the consultant can put together a one-page cheat sheet and spell out the assumptions. This can be compiled for the report, as well as the Legislature, as they will want to see the adjustments.

Member Souki suggested having the report with appendices so the Legislature can see how we got there.

Member Sako stated she doesn't think they are ready to vote yet but if the consultants could draw out all the scenarios before the next meeting, pros and cons, and also the impacts on revenues go up or down, to see those charts will help the group to make the final decisions.

Chair Acoba asked for inclinations on some of the issues like on the 60/40, does everyone agree on the 60/40. Member Kam stated he likes the 20/35/45. Member Hunt said it would depend.

Mr. Kirkpatrick stated they will run two versions for the future – one with the straight Hospitality Advisors scenario; the other, they will take the percentage changes; historical changes from 2000-2014, and use those to go 2015 on up.

Member Soon agrees with Tourism Special Fund set aside, but not with a percentage.

It was agreed with the Tourism Special Fund set aside and a 60/40 split.

V. Final Report to the 2016 Legislature

a. Draft Chapter 2, Objective 1 (handout) – Discussion

This item was not discussed and no handout was distributed.

VI. Allocation of TAT Revenues

This item was not discussed.

VII. Evaluate the division of duties and responsibilities between state and counties relating to the provision of public services

This item was not discussed.

VIII. Adjournment: With no further business to discuss, Chair Acoba adjourned the meeting at 12:09 p.m.

Reviewed and approved by:

Jan K. Yamane
Acting State Auditor

[ ] Approved as circulated.
TATWG/20150916