

COUNCIL ON REVENUES

Meeting Minutes, Tuesday, March 13, 2018 (2pm)

DLIR Conference Rooms
Princess Ruth Keelikolani Building
830 Punchbowl Street, Third Floor
Rooms 310-313
Honolulu, HI 96813

PRESENT:

Council Members:

Kurt Kawafuchi (Chair), Marilyn M. Niwao (Vice-Chair), Carl Bonham, Christopher Grandy, Ed Case, and Kristi L. Maynard

Staff Members:

Department of Taxation (DOTax): Seth Colby and J. Guitguiten

Department of Budget and Finance (B&F): Terri Ohta, Donovan Chun, Kenneth Shirokane and, Neal Miyahira

Others:

Ross Tsukenjo, Senate President's Office
Erin Conner, Senate Ways and Means
Alika Ke-Paloma, Senate Ways and Means
Ken Kitamura, Budget & Finance
Jeff B.
Robert Yu, HART
Mike McGrane, HART
Dane Wicker, Senate Ways and Means
Linda Chu Takayama, Director of Taxation
Damien Elefante, Director of Taxation
Deborah Kwan, DOTax Public Information Officer

Absent: Jack P. Suyderhoud, Member

CALL TO ORDER:

Chair Kawafuchi called the meeting to order at 2p.m. A quorum was present.

COMMUNICATIONS TO THE COUNCIL AND PUBLIC COMMENT:

There was no communication to the Council and there was no public comment.

APPROVED MINUTES OF THE MEETING OF JANUARY 8, 2018:

Chair Kawafuchi asked if there was any discussion on any item in the minutes. There were none. Chair Kawafuchi called for a motion to approve the minutes for the meeting of January 8, 2018. Dr. Bonham abstained from the vote because he was not present at the meeting.

It was moved by Ms. Maynard and seconded by Ms. Niwao that the minutes of the January 8th meeting be approved. The Chair called for the vote, and the motion passed with the following votes:

Kurt Kawafuchi	Yes
Marilyn Niwao	Yes
Jack P. Suyderhoud	Absent
Carl S. Bonham	Abstain
Christopher Grandy	Yes
Ed Case	Yes
Kristi L. Maynard	Yes

GENERAL FUND REVENUE FORECAST FOR FISCAL YEAR 2018:

Chair Kawafuchi asked Dr. Colby for any comments. Dr. Colby said revenue has been higher than in past months. He thought that this is a national trend with all 50 States at 10.8% revenue growth year-over-year. Dr. Colby said it has a lot to do with a vibrant economy which can be seen through the GET and other income including capital gains. He said the hypothesis is that the 2017 Tax Cuts and Jobs Act has prompted people to take capital gains--taking profit on dividends that are showing up in the estimated tax payments (February up at 23%).

Chair Kawafuchi asked Dr. Colby if he thought there was significant pre-payment of the income tax and property taxes because of the limit of the SALT (state and local taxes) deduction capped at \$10,000. Dr. Colby said there were strong numbers in January and February as well. Dr. Colby agreed with Chair Kawafuchi that there was a large increase of \$74 million for estimating individual taxes. Dr. Bonham said the February growth rate (total General Fund) was larger than in January.

Ms. Niwao mentioned that people were paying their estimated taxes (state income tax and real property taxes) and pre-paying tax preparation fees and maybe investment fees as well. She said there were a lot of people preparing for the new changes before December 31st because itemized deductions were no longer going to be allowed in 2018 under the new federal tax law.

Chair Kawafuchi said the GET is still strong at about 10%. Ms. Niwao said some activities would have increased GET paid in January or February in 2018 and there is the Amazon effect during this first period (including the not knowing the amount of that payment with the holiday sales). Dr. Bonham said maybe it's just the economy is incredibly strong. Dr. Colby mentioned the Amazon collections began on April 1, 2017. Ms. Niwao said this fiscal year there would be expected GET increases due to the online sales reported compared to the prior fiscal year to date. Dr. Colby said there were adjustments made in August 2016 with the transfer from the GET to the TAT of \$25 million, which inflated the FY 2017 revenues. And, with that adjustment taken into account the actual TAT growth is 10.2%.

Dr. Grandy said that in January 2017 the declaration of estimated taxes monthly numbers were just over \$150 million; January 2018 was \$9.5 million; February 2017 was \$14 million; and, February 2018 was \$146 million. He said taking the average of the two months there is not

much change and he wouldn't want to draw conclusions about the health of the economy from just one month of numbers because it may be a timing issue.

Chair Kawafuchi said individual estimated taxes are usually based on profits for small businesses and individuals. Dr. Grandy said December 2016 was \$28.3 million; and December 2017 was \$48 million.

Ms. Maynard said there may be a little bit of acceleration and she knows that it sometimes takes a while for checks to clear even though on the average it might be 5 days (although for her it was 21 days).

Dr. Bonham said inflation is a bit stronger than it has been in years past; incredibly strong visitor arrivals growth, which will continue for the rest of this year. He suggested the Council look at the real economy and not trying to figure out why the numbers are coming in strong.

Ms. Niwao said November actual collections were the most surprising--contracting was down from the fiscal year to November versus the prior fiscal year and retailing services were up. She said she was very pessimistic about everything for many years. However, things have been looking up. Ms. Niwao said from her perspective, there are many more tourists on Maui, the airport is crowded, and it seems that Maui is looking more and more attractive to the visitors. She said compared to Oahu, actual visitor arrivals to Maui apparently increased by a 14% for January and February.

Dr. Bonham said that the direct domestic airline seats for Maui are expected to be up 13% for March and April and, 20% for May. He said the growth last year wasn't as strong as the Big Island but Maui still grew pretty significantly. Ms. Niwao said the West Coast tourists are arriving in Maui, where traditionally Maui had a lot of strength. In the meantime the Japanese tourist arrivals are down.

Mr. Case said the arrival of Japanese tourists is steady, but not at the same growth levels across the State as from the West Coast as Ms. Niwao has pointed out. He said some markets are coming back such as Australia. Overall the arrivals are more prevalent on the neighbor islands than on Oahu.

The Members discussed briefly on the increased hotel room rates on the neighbor islands, visitor arrivals statewide, visitor expenditures, home-share vacation rentals, nominal GDP (Gross Domestic Products) numbers between 3%, 3.25% and 4.25% and, the GDP real numbers and GDP deflator, Hawaii real personal income at zero for 2017 and, unemployment up at 2% (Maui at 1.9% and Oahu at below 2%).

Ms. Niwao said she is aware that younger people who can't afford to make a living in Hawaii are moving to the mainland. She said the restaurants that hire lower wage earners are experiencing the shortages of employees.

Dr. Bonham said the City and County of Honolulu is struggling having to hire people. He said everybody is having a hard time finding someone to work. And according to the 2017 data which is pretty significant, the domestic out-migration was larger than the international in-

migration, resulting in a net small decline in population. Dr. Bonham said that's kind of distant and besides the mix of ages, there could also be just the mix of industries. Most of the job gains have been of what you would sort of think of as the hospitality sector, if you're hiring very young people to work in retail or food service. Dr. Bonham said that food service saw pretty significant growth last year. He said that would also change the total of the averages.

Chair Kawafuchi asked if there were any national or global factors to consider. Ms. Maynard said we need to consider the tax reform changes and the impact of that.

The Members discussed the comprehensive tax reform and the impact of federal grants and entitlements (emergency funds for FEMA, etc.) being cut with the federal funds flow. Ms. Niwao was concerned with the Federal deficit, saying they're going to have to balance it out sometime.

Also discussed was the increase in military and non-military spending—increasing spending and cutting taxes, potential trade war and the tariffs on steel and aluminum, the start of the collection from the Amazon online sales, tax rate increases in 2018 (8.25% to 11%) for higher income earners and, how much the State of Hawaii will adopt changes to the federal tax laws. It was by mentioned by one member that Federal-State nonconformity will be a problem for practitioners--allowing for complexity and making it difficult to determine the impact of tax law changes.

Chair Kawafuchi asked if the Tax Department has taken any position with written testimony on personal exemption because that's going to weigh on the federal side in 2018. Dr. Colby said the Legislature is currently considering conformity laws. Dr. Colby told the Council they could check the Legislative website for the department's testimony although he wasn't sure if it's made available to the public. Chair Kawafuchi said if it's written testimony and submitted to the Legislature, it is public information.

Dr. Colby said conformity will not tax effect between now and June. Dr. Colby told the Council Members that when the conformity bill passes, the Tax Department will provide the COR with the revenue estimates and when the impact will occur. Chair Kawafuchi said it will impact the out years. Ms. Niwao said it would also impact 2019 and the change of the tax rates will probably be collected in 2019. She asked how much effect the Amazon GET collections were because it was not likely to have an increase in future years. Chair Kawafuchi said it's about 6.9%, not a large increment.

Ms. Niwao suggested a 5.5% or 5.3% growth rate for fiscal 2019. Dr. Grandy said the current forecast is 4.5%. He said 4.5% seems more reasonable to him. In a response as to why 4.5%, Dr. Grandy said real personal income and wages will be adjusted—it happened before so it's possible.

Dr. Bonham said that construction jobs have been falling for between 12 and 16 months and then rebounded in the 4th quarter of the year quite strongly then continued into the 1st month of the year. Dr. Bonham said UHERO (UH Economic Research Organization) received the revised jobs data. He said that for last year we lost (he would say), probably 4% construction jobs but rebounded in the 4th quarter. The construction sector was on the decline and he said he's not real clear as to why a big jump in construction jobs 4th quarter.

Chair Kawafuchi asked Dr. Bonham his thoughts on a forecast. He said his General Fund forecast for UHERO's model is 5.6% for this year. The forecast that came out of the Council's models are all over the place and questioned model 3. He said model 1 is 5.1% for his inputs; model 2 is 6.3%. He said he's comfortable with 5.5% for this year. Ms. Maynard said she always likes to be cautious and not to be too exuberant. She said we are seeing some evidence in the banking world of some slowdown in lending and she didn't know how much that is due to slightly higher interest rates. Ms. Maynard said that certainly we're seeing fewer people re-financing and taking advantage of lower rates (obviously because interest rates are higher). She said we are seeing people cashing-out and they're re-financing to take money out of the increased in value in housing as housing prices have gone up. Dr. Bonham said if you re-finance a million dollar plus loan, you just lost some of your interest deductibility. Ms. Niwao said with the new tax laws the interest on borrowed money on home equity loans, will no longer be deductible in 2018.

Dr. Colby mentioned an article in the New York Times about a notice from the IRS stating that HELOCs (home equity line of credit) home improvements are still deductible. Ms. Niwao said home equity loans trace expenditures to determine whether it's for a home residence or home equity. She said usually home equity (for example, \$100,000) could be spent on anything like travel, personal things, etc. The portion of the home equity line of credit traced to home improvements would be deductible as home mortgage interest.

Mr. Case said 4.5% is too low and thought 5% is probably a little low. He said his range is 5.25%, 5.3% to be a little more cautious about it. Mr. Case said there're a lot of economic and political and other kinds of volatility right now.

Chair Kawafuchi said Dr. Grandy proposed 4.5% and Ms. Niwao proposed 5.3%. Dr. Bonham said to get to 5.5% you need 3% growth for the rest of the year. He said that seems like a really low bar, barely even inflation. Dr. Bonham said just so we're clear, volatility works both ways. And, we've had it work both ways—we've been badly wrong on the low-side and badly wrong on the upside. Ms. Niwao said demographic-wise, the baby boomers are probably saying maybe they should travel. She said that virtual travel is coming on to the horizon. Dr. Bonham said he's not so sure about that.

Ms. Maynard seconded Ms. Niwao's motion of 5.3%. Chair Kawafuchi said 5.3% growth rate for the current fiscal year 2018 and asked for the vote. It was unanimous.

It was moved by Ms. Niwao that the general fund tax revenues growth rate be 5.3% for FY 2018 (below-the-line). Ms. Maynard seconded. The Chair called for the vote, and the motion passed with the following votes:

Kurt Kawafuchi	Yes
Marilyn Niwao	Yes
Jack P. Suyderhoud	Absent
Carl S. Bonham	Yes
Christopher Grandy	Yes
Ed Case	Yes
Kristi L. Maynard	Yes

GENERAL FUND REVENUE FORECAST FOR FISCAL YEARS 2019 THROUGH 2024:

Next, the Council discussed the General Fund revenue forecast for FY 2019 through 2024.

Chair Kawafuchi asked if there was any discussion. Mr. Case said he wouldn't have a problem with raising 2019 slightly to 4.5% and keep the out years unchanged.

Chair Kawafuchi asked if there was any other discussion. Dr. Grandy said he was happy with the current out year forecasts and 4.5% for 2019. Dr. Bonham agreed saying it's pretty reasonable.

Dr. Colby said we present our tax law estimates in the September meeting. Dr. Bonham made a motion of 4.5% for fiscal 2019 and to keep the remaining out years unchanged at 4.0% (FYs 2020 to 2024). Ms. Maynard seconded the motion.

Chair Kawafuchi asked if there was any further discussion. There was no further discussion. The vote was unanimous.

A motion was made by Dr. Bonham that the General Fund revenue for FY 2019 be at 4.5% and the remaining out years remain the same: 4.0% (2020); 4.0% (2021); 4.0% (2022); 4.0% (2023); and 4.0% (2024). Ms. Maynard seconded. The Chair called for the vote, and the motion passed with the following votes:

Kurt Kawafuchi	Yes
Marilyn Niwao	Yes
Jack P. Suyderhoud	Absent
Carl S. Bonham	Yes
Christopher Grandy	Yes
Ed Case	Yes
Kristi L. Maynard	Yes

**REPORT BY THE DEPARTMENT OF BUDGET & FINANCE ON OTHER REVENUES:
Significant Changes from January 2018 Report**

Mr. Donovan Chun provided the Council members with Budget & Finance's report of revised projections of General Fund non-tax revenues and non-General Fund tax and non-tax revenues since the January 8th meeting.

Mr. Chun said the report includes a brief summary of significant changes and that there are several significant changes highlighted:

Other Than Special Fund Non-Tax Revenues

Charges for Current Services – the net increase in FY 18 reflects rebates on prescription drug plans and rate credits or experience gains from insurance carriers to the EUTF (B&F).~\$37.4M (18)
Non-Revenue Receipts – the increases in FYs 19-24 reflect the revision of the required

employer contributions for prefunding the State's OPEB at EUTF (B&F).

3,951,413	41,546,000	58,268,000	59,717	64,868	64,248	56,593
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Ms. Maynard and Ms. Niwao both moved to accept the B&F report as submitted. The Chair called for the vote, and the motion passed with the following votes:

Kurt Kawafuchi	Yes
Marilyn Niwao	Yes
Jack P. Suyderhoud	Absent
Carl S. Bonham	Yes
Christopher Grandy	Yes
Ed Case	Yes
Kristi L. Maynard	Yes

NEXT MEETING:

The Council tentatively agreed to meet on Thursday, May 24, 2018 at 2 p.m.; however, the date and time will be confirmed by e-mail. The Council staff will attempt to secure the DLIR Conference Rooms 310-313.

The Chair adjourned the meeting.

ADJOURNMENT:

The meeting adjourned at 3:01 p.m.