

# MEMORANDUM

Date: October 15, 2021

To: Tax Review Commissioners

From: Alton Miyashiro

RE: Proposed Recommendation on Adopting a Simpson-Bowles Type of Commission

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I am submitting the following proposed recommendation for the commission's discussion and decision-making at our meeting on October 20, 2021.

The Hawaii Tax Review Commission (TRC) recommends that the Legislature establish a Simpson-Bowles type of commission (SB commission) to address the issues noted below.

In 2020 and 2021, the Covid situation has taken an immense toll on Hawaii's economy and the people of Hawaii. Fortunately, the State of Hawaii as well as the counties received billions of federal dollars through the American Rescue Plan Act to help cover budget shortfalls and mitigate Covid related costs. Senator Brian Schatz estimated the final package could bring Hawaii at least \$1.7 billion.<sup>1</sup> Federal assistance may be substantially reduced in the future. Hawaii must anticipate this reduction in federal funds and plan, accordingly.

In 2019, a report called "Troubled Waters: Charting a New Fiscal Course for Hawaii" produced for the Hawaii Executive Conference stated that projected cost to the state and the four counties to mitigate climate change, improve infrastructure and meet the public employee pension and retiree health care obligations is over \$88 billion over the next 30 years. This cost exceeds Hawaii's 2018 real GDP of \$80.8 billion and is five times larger than the state government's operating and capital improvements budget for the fiscal year 2019-2020.<sup>1</sup>

## **Maintaining and Improving Infrastructure**

### **Water and Wastewater**

Water, wastewater and sewage systems are vital to the people of Hawaii and must be constantly maintained and upgraded for the future benefit of the people of Hawaii. In 2019, it was estimated that Hawaii's government future costs over the next 30 years for county water and waste water was \$11.4 billion.<sup>2</sup> The responsibility for this

infrastructure lies primarily with the counties. The counties charge a user fee to cover current operating costs. Each county may have different financial situations and priorities; therefore, we recommend that the SB commission establish minimum funding guidelines to ensure each county will have adequate funds to pay for maintenance and future upgrades. These guidelines could include annual funding of a reserve fund with a percentage of annual county revenue.

### Transportation Infrastructure

Hawaii is an island state surrounded by water and is very dependent on air and ocean transportation. It is imperative that the Legislature provide adequate funding to maintain and improve this vital infrastructure.

We recommend that the SB commission set aside a percentage of revenue or specific dollar amount to fund these projects. Specific taxes and user fees are currently assessed and Federal dollars may also be a source of funding. We recommend that the SB commission determine if current funding is adequate to cover the current and future cost of maintaining and improving this infrastructure and establish financial metrics to properly fund and monitor this initiative.

### Roads and Bridges

Roads and bridges in certain parts of the state are old and may create safety issues. The TRC recommend the SB commission set aside adequate funds to address this issue.

The TRC recommends that the SB commission also promote a strategy that will ensure effective use of capital and efficient project management for these infrastructure projects.

## **Climate Change and Natural Disaster**

### Climate Change and Rising Sea Levels

The impact of climate change and global warming cannot be denied especially for an island community in the middle of the Pacific Ocean. Experts predict sea level rise to exceed 3 feet along the coastlines before the end of the century and will undermine infrastructure and other improvements along our shoreline.<sup>2</sup> The TRC recommends the SB commission project these future costs and properly budget for these anticipated costs.

### Natural Disaster

The constant threat of hurricanes, tropical storms and an active volcano is real and Hawaii must be prepared for a natural disaster to happen. A direct hurricane hit to Oahu or Maui would be catastrophic as core systems and facilities would be disrupted for weeks.<sup>2</sup>

The TRC recommends the SB commission establish a “rainy day” fund to be available, if needed. Restrictions should also be imposed on raiding or borrowing these funds for other purposes.

## **Public Employee Healthcare and Pension Obligations**

Public employees in Hawaii are entitled to vested retiree healthcare and pension benefits which is guaranteed by the State Constitution. This obligation has created a large unfunded liability in the future. The state is gradually paying down the unfunded liabilities through annual contributions but the remaining outstanding unfunded obligation remains enormous. In 2018, the state’s pension plan was only 55% funded and healthcare benefits were 16% funded. A lump sum payment in 2020 would cost the state \$25.7 billion to fully fund these two programs and be able to pay for future retirement benefits already incurred for existing employees. <sup>2</sup>

The Legislature has taken steps to mitigate this issue but more needs to be done. The TRC recommends the SB committee to “drill down” on the relevant issues and devise a long term, financial strategy to mitigate this increasing future liability.

## **Promote Economic Growth**

The TRC recommends that the SB commission explore specific strategies to stimulate economic growth and diversify the economy in the State of Hawaii. Hawaii’s natural resources such as our weather and surrounding ocean may be good resources to promote. Renewable energy is a good example of a new industry that has created new jobs and is good for our environment.

1 Fujji- Oride, N. (2020, January) Hawaii’s Future Liabilities are Expected to Cost \$88 Billion

2 Hawaii Executive Conference (2019, October) Troubled Waters:: Charting a New Fiscal Course For Hawaii