

COUNCIL ON REVENUES

Office on Aging Conference Room
No. 1 Capitol District Building
250 S. Hotel Street
Fourth Floor, Room 410
Honolulu, HI 96813

Wednesday, January 9, 2008
10:00 A.M.

PRESENT:

Council Members:

Paul Brewbaker (Chair), Jack Suyderhoud (Vice-Chair), Carl Bonham, Pearl Imada Iboshi, Richard F. Kahle, Jr., and Albert Yamada

Staff Members:

Department of Taxation: Tu Duc Pham, Yvonne Chow, Jacquelyn Guitguiten, Glenn Ifuku, Davis Kawamoto, Kyle Nakahara, and Cathleen Tokishi
Department of Budget and Finance: Neal Miyahira, Keith Shimada, Karen Matsunaga, and Terri Ohta

Others:

Gordon Arakaki, Senate Committee on Ways and Means
Huong Bassford, Department of Budget and Finance
Derrick DePledge, Honolulu Advertiser
Casey Hines, Senate Majority Office
Lowell Kalapa, Tax Foundation of Hawaii
Kurt Kawafuchi, Department of Taxation
Nandana Kalupahana, House Committee on Finance
B. J. Reyes, Honolulu Star-Bulletin
Titin Sakata, Department of Taxation
Linda Taylor, Senate Majority Office

ABSENT:

Council Members:

Dean Hirata

CALL TO ORDER:

The Chair called the meeting to order at 10:06 A.M. with a quorum present.

COMMUNICATIONS TO THE COUNCIL:

The Chair acknowledged the receipt of a letter dated November 21, 2007, from Governor Lingle, thanking the Council for its November 2007 report.

MINUTES OF THE MEETING OF NOVEMBER 1, 2007:

The Chair asked if there were any corrections to or comments about the minutes of the November 1, 2007, meeting. There were none, so the Chair called for a vote.

It was moved by Dr. Suyderhoud, and seconded by Mr. Kahle, that the minutes of the November 1, 2007, meeting be accepted. The Chair called for the vote, and the motion passed with the following votes:

Paul Brewbaker	Yes
Jack Suyderhoud	Yes
Carl Bonham	Yes
Dean Hirata	Absent
Pearl Imada Iboshi	Yes
Richard F. Kahle, Jr.	Yes
Albert Yamada	Yes

REPORT BY THE DEPARTMENT OF BUDGET & FINANCE ON OTHER REVENUES

Ms. Matsunaga reported the significant changes from the August 2007, report.

General Fund Non-Tax Revenues: Significant changes in charges for current services (increased central services assessments and decreased county surcharge reimbursements) and non-revenue receipts (increased transfers from pension accumulation and social security reimbursements and decreased FY 2008 transfers from the Hawaii Hurricane Relief Fund).

Special Fund Tax Revenues: Significant changes in liquid fuel (1-cent fuel tax increase), transient accommodations tax transfers, and rental motor vehicle surcharge (higher \$4 per day tax rate extended) categories.

Special Fund Non-Tax Revenues: Significant changes in the use of money and property (decreased Department of Transportation (DOT), Airports Division, interest earnings), the federal category (federal funds for the DOT, Airports Division), charges for current services—utilities and other enterprises (lower FY 2007 DOT Airports and Harbors Division revenues; and FY 2008–2014 increased DOT Airports Division landing fees, decreased airport system support charges and decreases due to the delayed start-up of the Hawaii Superferry and the cancellation of one cruise ship), charges for current services—others, and non-revenue receipts.

Regarding charges for current services—others, the Chair questioned the significant \$300 million decrease in the FY 2007 revenues. Ms. Matsunaga explained that the decrease was partly due to lower University of Hawaii (UH) undergraduate tuition and Department of Labor and Industrial Relations special assessments, but that most of it was due to issues with how Hawaii Health System Corporation revenue is reported. All Corporation revenue is reported in the State's revenue-tracking system, but the revenue is only partially reflected in the State's accounting system. The problem with how the income appears in the State's accounting system versus the State's revenue system is being addressed, and information will be presented at the next meeting.

Other Than Special Fund Non-Tax Revenues: Significant changes in federal grants (to the Departments of Hawaiian Home Lands, Human Services, and Health and to the UH), charges for current services (increased public facilities development dedication fees for DBEDT), and non-revenue receipts (private donation to the Department of Accounting and General Services for the Leeward Coast homeless and DBEDT research and development funding).

The following corrections resulted in offsetting entries:

- Department of Business, Economic Development and Tourism (DBEDT) housing development funds previously reported in Special Fund Non-Tax Revenues (under the use of money and property and the non-revenue receipts categories) are now reported in Other Than Special Fund Non-Tax Revenue (under the use of money and property and the non-revenue receipts categories).
- For FYs 2008–2009, approximately \$100 million from a Kapolei land sale for the UH previously reported in Other Than Special Fund Non-Tax Revenue (revenues from other agencies), is now reported in Special Fund Non-Tax Revenues (revenues from other agencies).

The Chair called for a motion to approve the report.

It was moved by Mr. Kahle, and seconded by Mr. Yamada, that the report of the Department of Budget and Finance be accepted with the clarifications. The Chair called for the vote, and the motion passed with the following votes:

Paul Brewbaker	Yes
Jack Suyderhoud	Yes
Carl Bonham	Yes
Dean Hirata	Absent
Pearl Imada Iboshi	Yes
Richard F. Kahle, Jr.	Yes
Albert Yamada	Yes

GENERAL FUND REVENUE FORECAST:

The Chair began with his forecast of 4.9% growth for FY 2008, 2.9% for FY 2009, and 1.4% for FY 2010. Dr. Bonham reported that, with respect to the Council's mean forecast of economic indicators, the growth rate of nominal construction completed was significantly lower than what he and the Chair had forecast in late August 2007.

Since then, however, the Chair noted that the impact of financing difficulties was worse than anticipated; particularly as they constrain nonresidential construction funding, which he and Dr. Bonham still think will partly offset the decline in residential construction. Certain large commercial projects are funded with relatively thin pieces of equity and credit in the form of securities that, for the last six months, have been hard to sell; the market for these securities has ceased to exist. Recent federal intervention helped, but the damage was done. Therefore, the trough in his construction forecast, though still shallow, is lower than before.

Dr. Bonham thought that 4.9% was too low for FY 2008; his nominal rate is about 5.5%.

The Chair stated that residential construction on the neighbor islands, other than high-end properties, had dropped precipitously. Military housing construction is bolstering Oahu construction and making up for much of the decline on the neighbor islands. Though much is not subject to the general excise tax, the wages paid will generate revenue.

There is risk in the out years for construction, according to Dr. Bonham, but the near term risk is in visitor arrivals. The Council's mean for visitor arrivals is much too high; his visitor arrival growth rate is 0.15% and will go down. Dr. Imada Iboshi's rate is 0.1%. The Chair's 1.6% growth rate should be -1.6%, which would affect the Council mean.

European and Canadian international arrivals are increasing as expected due to favorable exchange rates, but the overall international arrival number is down because of the decrease in Japanese arrivals. Although there may be an increase of Korean arrivals at the end of 2008, it won't return to its record high. The lack of airline seats to Hawaii is problematic.

The Council expects Hawaii's cruise industry to decline due to the withdrawal of one inter-island cruise ship. Dr. Imada Iboshi mentioned a possible federal rule change that could kill Hawaii's international cruise business. Instead of foreign-flagged ships traveling from the West Coast to Hawaii with only a brief stop at a foreign port (e.g., Ensenada, Mexico), ships would be required to stop at a foreign port for a minimum of 48 hours, stay for at least half the amount of time spent in U.S. ports, and allow the passengers to disembark. This would make a seven-day cruise to Hawaii untenable. A final decision is due at the end of January.

The Council decided to first address FY 2008, then FY 2009, and then FYs 2010–2014.

The August forecast for FY 2008 was 5.7%. The Chair proffered 4% to start the discussion. Dr. Bonham's model shows 6.8%, which he acknowledged was too high. Even if a 6% growth

rate were assumed for the remainder of the fiscal year, the growth rate for the entire fiscal year would be only 4.1%, which is far from the previously forecasted 5.7%.

Discussion addressed the flat income and general excise tax collections, two weekend effects (\$40 million each) that would net to zero by the end of the fiscal year, inflation (not slowing as much as anticipated), and other factors. A consensus grew around a 4.9% growth rate forecast due to the erosion of some economic activity indicators (e.g., CPI and construction moving in different directions and a worsening tourism outlook).

It was moved by Dr. Suyderhoud, and seconded by Mr. Kahle, that the FY 2008 below the line growth rate be 4.9%. The Chair called for the vote, and the motion passed with the following votes:

Paul Brewbaker	Yes
Jack Suyderhoud	Yes
Carl Bonham	Yes
Dean Hirata	Absent
Pearl Imada Iboshi	Yes
Richard F. Kahle, Jr.	Yes
Albert Yamada	Yes

The Council asked that they be given updated general excise tax data, by business activity, in preparation for the March meeting. They currently have such data only through June 2007; they are particularly interested in the construction data. Dr. Pham will try to have that data through December 2007.

Dr. Suyderhoud suggested a 4% forecast for FY 2009, which is slightly higher than the 3.8% previously forecasted. The Chair noted that Hawaii isn't immune to events on the mainland, and pointed out that construction on the Big Island had plummeted in the last six months.

Dr. Bonham believed that the impact on tourism would be larger than the impact on construction. The Chair mentioned that there is some recent speculation about whether the next president would effect changes that would result in fewer military personnel and dependents in Hawaii that would in turn affect the State's economy; neither he, Dr. Bonham nor Dr. Imada Iboshi felt that there would be an impact.

Dr. Bonham agreed that 3.8% was too low; should be 4% to 4.5% for the next few fiscal years. He projected 5% growth by FY 2010; both Dr. Imada Iboshi and the Chair projected 5% growth by FY 2012. After further discussion regarding slower disinflation, in part due to oil prices, and more strength in construction (particularly stronger public construction funded by municipal bonds although there is a very real downward risk regarding commercial construction), which would increase by a few tenths of a percent general excise tax and individual income tax revenues, the consensus was that the FY 2009 growth rate would be about 4.1%.

At this time, the Chair called for a motion on the FY 2009 forecast.

It was moved by Dr. Suyderhoud, and seconded by Dr. Bonham, that the FY 2009 below the line growth rate be 4.1%. The Chair called for the vote, and the motion passed with the following votes:

Paul Brewbaker	Yes
Jack Suyderhoud	Yes
Carl Bonham	Yes
Dean Hirata	Absent
Pearl Imada Iboshi	Yes
Richard F. Kahle, Jr.	Yes
Albert Yamada	Yes

After a brief discussion regarding the outlook for FYs 2010–2014, the consensus was that the growth rates for those years remain unchanged.

At this time, the Chair called for a motion on the FY 2010–2014 forecast.

It was moved by Dr. Bonham, and seconded by Mr. Kahle, that the below the line growth rates previously forecast for FYs 2010 through 2014, 4.9%, 4.7%, 5.0%, 6.2%, and 6.0%, respectively, be retained. The Chair called for the vote, and the motion passed with the following votes:

Paul Brewbaker	Yes
Jack Suyderhoud	Yes
Carl Bonham	Yes
Dean Hirata	Absent
Pearl Imada Iboshi	Yes
Richard F. Kahle, Jr.	Yes
Albert Yamada	Yes

NEXT MEETING:

The next reporting date is Saturday, March 15, 2008, regarding the General Fund Revenue forecast for the current fiscal year.

The next meeting will be held on Wednesday, March 12, 2008, at 2:00 P.M.; staff will try to again reserve the Office of Aging Conference Room.

ADJOURNMENT:

Before adjourning, the Chair reminded the Council that, on Friday, January 11, 2008, he would be testifying on behalf of the Council before a joint hearing of the Senate Committee on Ways and Means and the House Committee on Finance, and that the testimony would reflect the results of this meeting.

The meeting adjourned at 11:23 A.M.