

## **COUNCIL ON REVENUES**

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

Thursday, August 2, 2012  
10:00 A.M.

### **PRESENT:**

#### Council Members:

Richard F. Kahle, Jr. (Chair), Jack P. Suyderhoud (Vice-Chair), Avery K. Aoki,  
Carl S. Bonham, Christopher Grandy, Kristi L. Maynard and Marilyn M. Niwao

#### Staff Members:

Department of Taxation (DOTAX): Donald Rousslang and Hamid Jahanmir

Department of Budget and Finance (B&F): Terri Ohta, Keith Shimada and  
Gregg Hirohata-Goto

#### Others:

M. Takai, House Minority  
Paul Harleman, Senate Minority  
Peter Fritz  
Sharon Kotaka, Budget and Finance  
Sam Slom, Senate  
John Kawamoto, Healthcare Association of Hawaii  
Susan Hirai, Ways and Means  
Roderick Becker, Ways and Means  
Neal Miyahira, Budget and Finance  
Nandana Kalupahana, House Finance  
Randall Hiyoto, House Finance  
Laurel Johnston, UH System  
Lowell Kalapa, Tax Foundation of Hawaii  
Anthony Valdez, Ways and Means  
Titin Sakata, Department of Taxation

### **CALL TO ORDER:**

Chair Kahle called the meeting to order at 10 a.m. with a quorum present.

**COMMUNICATIONS TO THE COUNCIL:**

Chair Kahle introduced the COR's newest member, Ms. Kristi L. Maynard, replacing Mr. Ronald K. Migita. The Council welcomed Ms. Maynard to the Council. Next, Chair Kahle mentioned receipt of a letter from Budget & Finance's Director Kalbert Young requesting the Council to revisit the forecast for the general fund projections.

**MINUTES OF THE MEETING OF MAY 29, 2012:**

The Chair called for a motion to approve the minutes.

**It was moved by Dr. Bonham and seconded by Mr. Aoki that the minutes of the May 29, 2012 meeting be accepted. The Chair called for the vote, and the motion passed with the following votes:**

<b>Richard F. Kahle, Jr.</b>	<b>Yes</b>
<b>Jack P. Suyderhoud</b>	<b>Yes</b>
<b>Avery A. Aoki</b>	<b>Yes</b>
<b>Carl S. Bonham</b>	<b>Yes</b>
<b>Christopher Grandy</b>	<b>Yes</b>
<b>Kristi L. Maynard</b>	<b>Yes</b>
<b>Marilyn M. Niwao</b>	<b>Yes</b>

**TOTAL PERSONAL INCOME FORECAST:**

The Council then turned to the forecast for the growth rate of total personal income.

Chair Kahle asked the Council whether they wanted to discuss the total personal income forecast or the general fund forecast first. The Council opted to first discuss the total personal income (TPI) forecast.

Dr. Suyderhoud asked what the models were forecasting. Dr. Rousslang referred the members to Tables 3 and 4 of the workbook. He said for 2011 the November forecast for TPI for CY2011 was 4.5% and the actual growth was 4.68%. Dr. Suyderhoud said they were forecasting TPI growth of 4.5% for CY2012 and 4.9% for CY2013. He said the forecast for CY2012 is based on just one quarter of data in 2012, which shows growth of 3.6%.

Dr. Bonham said the forecast for 2012 is 4.4%. He said that is partly because the inflation forecast was reduced due to the retreat in energy prices. Suyderhoud asked Dr. Bonham if he had a forecast for 2013. Dr. Bonham said yes, it is 4.6%. Dr. Suyderhoud asked if that were largely due to energy prices. Dr. Bonham said no, the change in the forecast from 2012 is partly due to energy prices and partly due to the first quarter data that were higher than expected. He said BEA also revised the historical data. He added that stronger economic growth was expected – his jobs forecast goes from 1.3% in 2012 to 2.50% in 2013. Dr. Suyderhoud asked if that translated only to a 0.2% increase in personal income. Dr. Bonham said yes, the other thing going on is the changes in tax laws.

Ms. Niwao said we might see more of the income growth this year and much less next year. She said people are planning to accelerate their income into 2012. She said the tax rates are scheduled to go up next year, so higher income taxpayers are planning to sell their assets. Dr. Grandy said he did not think the assets sales would show up in personal income. Ms. Niwao asked if that were true for capital gains. Dr. Bonham said he was not sure and wondered if it showed up in dividends, interest or rent. Dr. Grandy said he was not sure, though he said it will certainly show up in taxable income. Dr. Suyderhoud asked if investment income was part of personal income. Dr. Grandy said yes, if it consists of dividends or interest, but he was not sure if capital gains were part of personal income. Dr. Suyderhoud asked why they would not be. Dr. Suyderhoud asked where else one would capture capital gains. He said for instance if people sell their stocks and experience an increase in income, whether the income gain would be included in personal income. He said he understood that unrealized capital gains would not be included. Dr. Grandy said he did not know for sure. He wondered whether there was a difference between taxable income and what is included by BEA in personal income. Dr. Bonham said he thought a forecast of 4.5% growth in TPI for both CY2012 and CY2013 would be a good idea.

Ms. Niwao asked Dr. Bonham if he thought the Bush tax cut will be extended. Dr. Bonham said it would not surprise him. He said the question is whether the tax cut would be extended for everybody or just the middle class. He said if they did not extend it, we would have much bigger problems in the very near term. He said his forecast counted on some changes in both the sequestration and in the tax provisions. Ms. Niwao thought that people would accelerate income this year to avoid the 3.8% tax on net investment income and the change in the capital gains tax rate, which she was not sure would be changed. She said she thought that there would be some tax increases next year, but the question was how much. She said they have the spending cuts also to factor in starting from January 1<sup>st</sup> of next year. Dr. Bonham said that at some point the tourism boom that we are experiencing would spill over into the rest of the economy. He said we have been in a boom period for 2 years now, and people are going back to work in large numbers in that sector. He said it is also beginning to spread to the neighbor islands and not just Oahu. He said hotels are full and TAT revenues are coming in. He said we are at the point where the effects of government reductions are starting to go away. He thought that another factor that should be considered is that the HGEA and UPW and other unions would start to see their income come back. He said he would argue that these effects are quite a bit larger than the effects of tax law changes on the wealthiest people in the State.

Ms. Niwao asked about the rail construction and what will happen if it does not go through. Dr. Bonham said if they stop construction then that would diminish the construction forecast, but it might also imply spending elsewhere. He said he did not know what would happen. Dr. Grandy said it is interesting to him that the time-series data on nominal personal income growth, which was above 5% about a year ago, has moderated a little. He said he is concerned about that. He said he thought that the pattern of growth for 2012, and somewhat higher growth for 2013 is right. He said if he was to come up with a number, he might go with growth of 4.2% and 4.4% for 2012 and 2013.

Dr. Bonham said that the traditional behavior of forecasters is to under-forecast when the economy is recovering. He said they are intentionally trying to be more optimistic because they

know that at this point in a business cycle that the tendency is for forecasters to be too pessimistic. He said income growth in 2004, 2005 and 2007 was much higher than right now, because construction tourism boomed at the same time. He thought that is what is going to happen.

Dr. Suyderhoud said the national economy is in a different type of expansion than it was in those time-periods. Dr. Bonham agreed, but said there was very strong growth this year in U.S. visitors, and that there are some real downside risks, but asked what probability one should assign to events such as the U.S. going off a fiscal cliff. He said under the best case scenario, none of them happen. He said he is comfortable with Dr. Grandy's forecasts of 4.2% and 4.4%. Ms. Niwao said that she is a little more conservative. She asked if Dr. Bonham thought that construction was going to pick up next year. Dr. Bonham said that is part of his forecast. He said we were wrong this year when we said it was going to pick up; it has on Maui but construction hiring really has not gone up anywhere on Oahu.

Dr. Suyderhoud asked if someone wanted to make a motion. Mr. Aoki said he was fine with 4.2% and 4.4%. Chair Kahle asked if there would be any more discussion. There was no more discussion.

**It was moved by Dr. Grandy and seconded by Ms. Niwao that the Total Personal Income forecast for CY2012 be 4.2% and CY2013 be 4.4%. The Chair called for the vote, and the motion passed with the following votes:**

<b>Richard F. Kahle, Jr.</b>	<b>Yes</b>
<b>Jack P. Suyderhoud</b>	<b>Yes</b>
<b>Avery A. Aoki</b>	<b>Yes</b>
<b>Carl S. Bonham</b>	<b>Yes</b>
<b>Christopher Grandy</b>	<b>Yes</b>
<b>Kristi L. Maynard</b>	<b>Yes</b>
<b>Marilyn M. Niwao</b>	<b>Yes</b>

**GENERAL FUND FORECAST:**

Chair Kahle said the reason for discussing the general fund forecast was that the Council's projection through the end of fiscal year 2012 was for growth of 12%, but collections actually came in at 14.9%. Dr. Suyderhoud asked if they could talk a little about what happened at the end of the year and if there was anything that caused the surprise for May and June collections. He addressed the question to Dr. Rousslang, who said he found that corporate income taxes in the last two months came in about \$10 million higher than last year, whereas the individual income tax came up from the last two months of last year by \$106 million. He said he thought the total shortfall in the Council's estimate was \$127 million.

Dr. Bonham said if the Council is doing a year-over-year comparisons of personal and corporate income tax collections, there was double-digit growth for all income sources. He asked if some TAT revenues ended up in the general fund. Dr. Rousslang said yes. Dr. Bonham asked how much. Dr. Rousslang said he thought that it was \$126 million. Dr. Bonham asked if that is the

same as the Council's estimate. Dr. Rousslang said no; the forecast was about \$113 million. Mr. Aoki said it has nearly doubled; the prior fiscal year was about \$60 million. Dr. Rousslang said that was accounted for in the below-the-line adjustments. Dr. Bonham said he was relatively sure that all of the members under-forecast visitor arrivals, visitor's spending, and therefore TAT revenue. Dr. Rousslang said he thought that the forecast for TAT general fund revenues was not that far off, after accounting for the below-the-line adjustments to the model – that it may have been \$6 million or something (for the last two months).

Dr. Suyderhoud said he was looking at the growth rate of general fund forecast from the previous meeting, which is what we need to focus on right now. Dr. Rousslang said yes, that it was included to show what would happen if the percentage growth rate forecast was maintained. Dr. Suyderhoud said yes, but focusing on the 2012 and 2011 numbers, there was nearly doubling of the TAT that goes into the general fund. He asked if he was right. Dr. Rousslang said yes, that is because of the below-the-line adjustments for tax law changes. Dr. Suyderhoud asked if part of the tax law changes is the caps. He asked what the TAT would have been in FY2012 without the tax law changes. Dr. Rousslang said he was not sure, but some modest growth over 2011. Dr. Bonham said earlier in the year, the forecast for general fund growth was 15%, or 14.5%. He said the members lowered the forecast when they should not have lowered it, that it happens all the time, and that is why he argued in his email that as you go into the year you start to see confusing month-to-month variations. He said the members spent hours talking about tax law changes and lowering the forecast. He said it is not clear to him that there is a strong reason for revising next year's forecast beyond the fact that the base was raised.

Dr. Grandy said he decomposed the growth of the revenue burst in June. Looking at GET and individual income tax, somewhat unusually most of the increase, about 60%, was due to the individual income tax and 40% to GET, and almost all of the income tax increase in June (about 93%) was due to lower refunds. He said the members may have been fooled by one month's data because they were largely on track for 12.0, 12.5, or 13.0% growth through May, and then a big bump-up came in June. He said he thought they may still be seeing some of the effects of the timing of refunds in 2010. He said he was not sure if we should revisit our revenue forecast. He added that the members were going to meet next month anyway to do the normal revenue forecast, so he argued waiting until then.

Ms. Niwao said there was a big change in the amount of refunds and she wondered if there was any delay this year in refunding taxpayers. Dr. Rousslang said he did not think so. He said when the members met for the last meeting they did not have May's numbers. He said refunds came out a little faster at the end of this year than previously. He said the refunds were processed a little faster inside the past fiscal year.

Mr. Aoki said that for FY2010 the collections were \$4.4 billion, whereas in FY2013 the forecast is for \$5.1 billion, the base will change and the compound average growth rate for that period is 5.37%. He said 5.4% over that period sounds reasonable. Dr. Bonham said real growth may be 2.5%. Dr. Suyderhoud said yes, but that tax law changes were a part of the big bump in FY2012. Dr. Rousslang said tax law changes were about 5.0%.

Ms. Niwao said this past year, the taxes for individuals were a lot higher because the change in tax laws denied certain itemized deductions and State income tax deductions for State taxpayers, so people were paying a lot more taxes. It was not because they had more income.

Dr. Suyderhoud said that the question is whether the members revisit their forecast. Dr. Bonham said the data is pointing at a number that is not that far off from the existing forecast.

Dr. Suyderhoud said the issue was Kalbert Young's letter of request. Dr. Bonham said the question is if there is enough new information to justify changing the forecast. Ms. Niwao said some of the tax law changes were temporary. Dr. Suyderhoud said that was figured into the forecast. Ms. Niwao said the question is if the members were going to assume that the tax law increases were temporary. Dr. Bonham said they already had. Dr. Suyderhoud said yes that was in the forecast. He asked how many members wanted to revisit the general fund forecast. He said he would rather wait until next month although Mr. Young would like to have something a little sooner. Ms. Niwao said he wants it for the budget. Dr. Bonham said the question is should the forecast be changed. He asked if there is information other than that the May and June collections came in higher than expected. He said he did not have another quarter of income data for the State. Dr. Suyderhoud said in addition, they had no July data. Dr. Suyderhoud asked if there is any sense of what is happening. Dr. Rousslang said preliminary data on Oahu collections show they are down compared to July of last year. He said that is total collections and not just the general fund.

Ms. Niwao asked if hotel rentals were near capacity. Mr. Aoki said HTA is predicting that visitor arrivals will go to 8 million. Ms. Niwao asked if the hotels can accommodate these visitors. Dr. Bonham said Waikiki is already full, Maui is almost half full, but the Big Island is still empty.

Dr. Bonham said the demand will help drive up hotel rates, which will generate revenue. He said he would move to not change the forecast. Dr. Suyderhoud said he would not consider a forecast. Dr. Rousslang asked, whether by keeping the forecast the same, did the members mean the dollar amount or the growth rate? Dr. Bonham and Chair Kahle said the growth rate. Dr. Suyderhoud said there was a big difference that keeping the growth rate the same meant \$5.2 billion rather than \$5.1 billion for FY2013. Dr. Bonham said that is a change in the forecast. Dr. Suyderhoud said yes. Mr. Aoki said the increment was \$134 million. Dr. Suyderhoud said yes.

Chair Kahle asked Dr. Bonham if he wanted to make his motion. Dr. Bonham said he did. Dr. Grandy seconded the motion.

Dr. Suyderhoud suggested making the motion that the percentage growth rate be unaltered for 2013 and later years. Dr. Bonham seconded Dr. Suyderhoud's version of the motion. Chair Kahle asked if there was any more discussion. Ms. Niwao asked what the motion was.

Dr. Suyderhoud said the motion is that the growth rates of 5.3%, 4.0%, 6.2%, 4.0%, 5.0%, and 5.0% remain in place for the fiscal years 2013 and beyond. Chair Kahle asked for a second to the amendment. Dr. Suyderhoud said he will second his clarification. Ms. Maynard also seconded the amended motion.

**It was moved by Dr. Bonham and seconded by Dr. Grandy that there be no change to the general fund revenues. Dr. Suyderhoud clarified the motion by Dr. Bonham that the growth rate of 5.3% (FY2013); 4.0% (FY2014); 6.2% (FY2015); 4.0% (FY2016); 5.0% (FYs 2017 through 2018) remain in place. Dr. Suyderhoud and Ms. Maynard seconded the amended motion. The Chair called for the vote, and the motion passed with the following votes:**

<b>Richard F. Kahle, Jr.</b>	<b>Yes</b>
<b>Jack P. Suyderhoud</b>	<b>Yes</b>
<b>Avery A. Aoki</b>	<b>Yes</b>
<b>Carl S. Bonham</b>	<b>Yes</b>
<b>Christopher Grandy</b>	<b>Yes</b>
<b>Kristi L. Maynard</b>	<b>Yes</b>
<b>Marilyn M. Niwao</b>	<b>Yes</b>

**NEXT MEETING:**

The Council tentatively agreed to meet on Thursday, September 6, 2012 at 10am; however, the date and time will be confirmed by e-mail. The Council staff will attempt to secure the Office on Aging Conference Room 410.

**ADJOURNMENT:**

The meeting adjourned at 10:45 am.