

## COUNCIL ON REVENUES

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

September 5, 2013  
2:00 p.m.

### **PRESENT:**

#### Council Members:

Kurt Kawafuchi (Chair), Marilyn M. Niwao (Vice-Chair), Carl S. Bonham,  
Christopher Grandy, Jack P. Suyderhoud and, Kristi L. Maynard

#### Staff Members:

Department of Taxation (DOTax): Donald Rousslang, Hamid Jahanmir and  
Jacquelyn Guitguiten

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

#### Others:

John Roberts, HI Association of Public Accountants  
Marc Takei, House Minority  
Lowell Kalapa, Tax Foundation of Hawaii  
Sharon Kotaka, Budget and Finance  
Eugene Tian, DBEDT-READ  
Titin Sakata, Department of Taxation

### **ABSENT:**

#### Council Member:

Elizabeth P. Cambra

### **CALL TO ORDER:**

Vice-Chair Suyderhoud called the meeting to order at 2 p.m. with a quorum present.

### **ELECTION OF OFFICERS:**

Vice-Chair Suyderhoud said that the Council needed to elect a Council Chair and re-elect a Vice-Chair and that as Vice-Chair he would preside over the meeting until the election of officers. He asked the Council how they wanted to proceed with the election of officers. The Council members agreed to ask for volunteers. Mr. Kawafuchi suggested Dr. Suyderhoud as Chair. Dr. Bonham said that the Council had a history of having a former Tax Director as Chair. Dr. Grandy and Dr. Suyderhoud agreed. Dr. Bonham said that there might be a perception problem if a University of Hawaii faculty member were to Chair the Council. Vice-Chair Suyderhoud added that they are

State employees. Dr. Bonham suggested that the Council needs someone who could explain the 'nuts and bolts.'

Vice-Chair Suyderhoud asked for a nomination. Dr. Grandy nominated Mr. Kawafuchi as Chair. Ms. Niwao seconded the motion. Mr. Kawafuchi accepted the nomination saying that he will do his best for the Council.

Vice-Chair Suyderhoud asked if there were any further discussion. There was none. All were in favor. Vice-Chair Suyderhoud welcomed Mr. Kawafuchi as Chair. Mr. Kawafuchi then presided over the meeting.

**A nomination was made by Dr. Grandy and seconded by Ms. Niwao that Mr. Kawafuchi be Chair. Vice-Chair Suyderhoud called for the vote, and the motion passed with the following votes:**

<b>Kurt Kawafuchi</b>	<b>Yes</b>
<b>Jack P. Suyderhoud</b>	<b>Yes</b>
<b>Carl S. Bonham</b>	<b>Yes</b>
<b>Christopher Grandy</b>	<b>Yes</b>
<b>Elizabeth P. Cambra</b>	<b>Absent</b>
<b>Kristi L. Maynard</b>	<b>Yes</b>
<b>Marilyn Niwao</b>	<b>Yes</b>

Chair Kawafuchi asked the Council to nominate a Vice-Chair. Dr. Grandy suggested keeping the present one. Dr. Suyderhoud said he would be happy to serve as the Vice-Chair but said others may want a chance. The members asked for volunteers for Vice-Chair. Dr. Bonham said that he would start Sabbatical in a month.

Ms. Niwao volunteered to serve as Vice-Chair. There were no other volunteers. Dr. Suyderhoud told the Council that a motion had been made and that a second was needed. Chair Kawafuchi asked if he could second. Dr. Suyderhoud said no, but that he would happily second the motion. Chair Kawafuchi congratulated Ms. Niwao as Vice-Chair. Ms. Maynard said it was a good choice. Chair Kawafuchi asked for a vote from the Council and all were in favor.

**Ms. Niwao volunteered to serve as Council Vice-Chair and Dr. Suyderhoud seconded. Chair Kawafuchi called for the vote, and the motion passed with the following votes:**

<b>Kurt Kawafuchi</b>	<b>Yes</b>
<b>Marilyn Niwao</b>	<b>Yes</b>
<b>Jack P. Suyderhoud</b>	<b>Yes</b>
<b>Carl S. Bonham</b>	<b>Yes</b>
<b>Christopher Grandy</b>	<b>Yes</b>
<b>Elizabeth P. Cambra</b>	<b>Absent</b>
<b>Kristi L. Maynard</b>	<b>Yes</b>

**COMMUNICATIONS TO THE COUNCIL:**

None.

**MINUTES OF THE MEETING OF AUGUST 1, 2013:**

Chair Kawafuchi asked the members for comments on the minutes of the August 1<sup>st</sup> meeting. There were no comments. Chair Kawafuchi asked for a motion to accept the minutes.

**It was moved by Ms. Niwao and seconded by Ms. Maynard that the minutes of the August 1, 2013 meeting be accepted. The Chair called for the vote, and the motion passed with the following votes:**

<b>Kurt Kawafuchi</b>	<b>Yes</b>
<b>Marilyn Niwao</b>	<b>Yes</b>
<b>Jack P. Suyderhoud</b>	<b>Yes</b>
<b>Carl S. Bonham</b>	<b>Yes</b>
<b>Christopher Grandy</b>	<b>Yes</b>
<b>Elizabeth P. Cambra</b>	<b>Absent</b>
<b>Kristi L. Maynard</b>	<b>Yes</b>

**DISCUSSION OF THE EFFECTS OF LEGISLATION ON TAX COLLECTIONS:**

Dr. Rousslang provided the Council with an update to the tax law changes. He said there were four Acts in 2013 that had noticeable effects on the general fund. He began with 2013 legislation. He said Act 89 amends the motion picture digital media and film production tax credit. The Act increases the credit rate from 15% to 20% for productions on Oahu and from 20% to 25% for productions on the neighbor islands. The Act also increases the cap on the amount of the credit per production from \$8 million to \$15 million and moves the expiration date for the credit from January 1, 2013 to January 1, 2019. The Act is estimated to raise the cost of the credit by about \$21 million over the level in FY 2013.

Chair Kawafuchi asked about the effective date of the film TV production credit. Ms. Sakata said it is July 1<sup>st</sup>. Dr. Suyderhoud asked if the credit would be certified by the Film Division or the Tax Department. Ms. Sakata said that the qualified expenditure would be certified by the Film Office. Chair Kawafuchi added that he thought the credit had always been certified by the Film Office.

Dr. Rousslang continued his update of legislation, saying that Act 160 eliminates the GET (General Excise Tax) exemption for liquor, tobacco and food sold to common carriers and that the Act is estimated to raise GET collections by about \$6 million per year. He said Act 161 makes permanent the TAT (Transient Accommodations Tax) rate of 9.25% and the caps on TAT allocations to the special funds. He said the Act also raises the cap on the allocation to the Tourism Special Fund by \$11 million. The Act is estimated to reduce general fund revenues by \$11 million in FY's 2014 and 2015, but to raise them by \$177 million in FY 2016, increasing to \$246 million in FY 2020.

Dr. Bonham asked if the TAT rate was set to go back down in FY 2016 and beyond. Dr. Rousslang said yes. Chair Kawafuchi asked if the rate was supposed to drop back to 7.25% and that now it would stay at 9.25%. Dr. Rousslang said yes, and that the caps are now permanent.

Chair Kawafuchi asked whether the caps to the counties or the special funds would increase. Dr. Rousslang said that only the Tourism Special Fund cap was raised, by \$11 million. He said the other caps were kept the same. He said the increase in the Tourism Special Fund cap took effect right away, so it would reduce general fund revenues for FY 2014 and FY 2015. Chair Kawafuchi asked if the reduction in general fund collections was offset by other factors. Dr. Rousslang said not in 2014 and 2015.

Dr. Bonham asked Dr. Rousslang how the TAT growth forecasts were calculated. Dr. Rousslang said TAT revenues were assumed to increase by the rate of inflation plus the growth in visitor arrivals. He said Act 163 makes permanent the GET exemption for certain expenses paid by hotel operators and timeshare projects and removes the cap on the aggregate amount of the exemptions that can be acclaimed. He said the Act is estimated to reduce GET collections by about \$20 million in FY 2014 and by about \$13 million annually thereafter.

Dr. Rousslang said Act 105, SLH 2011, which eliminated certain GET exemptions and which expired June 30, 2013, is estimated to reduce GET collections by about \$70 million annually relative to the level in FY 2013. He said Act 62, SLH 2011, allocates GET revenues directly to the Hurricane Relief Fund in FY 2014 and FY 2015 to replace the amounts that were taken from the fund in prior years. He said the Act would reduce GET allocations to the general fund by \$55.5 million in each of FY's 2014 and 2015.

Chair Kawafuchi asked if the exemption altered by Act 163 originally had a cap. Dr. Rousslang said yes, but the cap was eliminated. Chair Kawafuchi asked if Act 105 took away exemptions for subcontractors and subleases. Dr. Rousslang said yes, those were some of the exemptions that were taken away. Chair Kawafuchi asked if the revenue estimate was only \$70 million a year. Ms. Niwao said the members were originally presented something like \$200 million. She said they revised it down to \$70 million. Chair Kawafuchi said there was a transition of rule. Ms. Niwao said yes, and added that construction was increasing, and although we would not have that additional money from the Act, we would get more money from the regular GET on income of the general contractors.

Chair Kawafuchi asked if the taxpayers have to list their GET exemptions. Dr. Rousslang said they do, but that the data on the exemptions are not captured electronically. Ms. Niwao said she asked Tax Director Pablo and others to see whether she could get that information, but was told it was not possible. She said it would be nice if they computerized the information.

Chair Kawafuchi asked if there had been any thought about computerizing the data. Dr. Rousslang said yes. The Chair said that would make it much easier to capture the data. Dr. Rousslang said computerizing would make it easier to get data, but that the exemptions on Schedule GE also need to be put in a standard format that would allow a research statistician to identify them.

Chair Kawafuchi said that in the past, some forms were required to be filed electronically, like the survey forms for Act 221, which makes it much easier to capture the data and produce reports. Dr. Rousslang said there was an electronic survey for the GET exemptions, but the response was not sufficient to provide reliable results. Chair Kawafuchi asked if there was a penalty for not filing the survey. Dr. Rousslang said it was voluntary. Chair Kawafuchi said he was not suggesting a penalty

but said an attempt should be made to better capture the data. Ms. Niwao asked if the \$70 million revenue loss for Act 105 is accounted for in the model provided to the members. Dr. Rousslang said yes, and that the effect of the allocation from the GET to the Hurricane Fund is also accounted for in the model.

Dr. Suyderhoud asked if there was anything else. Dr. Rousslang said yes, there was also the administrative rules that he estimated would reduce the cost of the renewable energy credit by \$20 million a year relative to the level in FY 2013.

Dr. Bonham said that looking at solar permits for Honolulu, which is the only data we have, the number of permits is roughly the same as last year's but the dollar value of the permits is down about 10% because the cost of PV (photovoltaic) is continuing to decline. He said that would imply that we are not going to see an additional \$70 million in tax credit costs over and above what we put in for fiscal 2013. Dr. Rousslang said the adjustment in the model says the payout would be \$20 million less than last year's. Dr. Bonham questioned the figure. Ms. Maynard asked if that meant that instead of being \$90 million, the adjustment going forward would be \$70 million. Dr. Rousslang said no, that any increase in FY 2013 over FY 2012 was reflected in the figure for FY 2013. Chair Kawafuchi asked if the \$70 million was based on the tax returns and the credits claimed on the tax returns. Dr. Rousslang said it was an estimate before any information was available on 2013 tax collections. Chair Kawafuchi asked if there are any hard data. Ms. Niwao said that is what she asked the Tax Department earlier. Dr. Rousslang said he did not yet have the data for FY 2013.

Dr. Suyderhoud said the Council had asked DBEDT (Department of Business, Economic Development and Tourism) a few meetings ago to provide an update on the credit cost estimates for the PV, but that DBEDT had said "no." He asked if DBEDT was going to provide more information in the future.

Dr. Tian said DBEDT's estimate for the cost of the tax credit was about \$174 million in tax year 2012. He said he thought the Council had already built in \$90 million in its model but needed to do some adjustment for the additional dollars. He said for tax year 2012 the Council raised some kind of an issue based on 2010 data, and now the tax credit data for 2011 is available but we still do not have the 2012 data. He said the 2011 tax credit was about \$65 million, but for 2012, the estimate is more than 3 times as great, so if you use about \$65 or \$60 million and multiply it by 3 it is about \$180 million. Chair Kawafuchi said that is quite a difference from \$70 million or \$90 million. Dr. Bonham said that is why the Council built about \$170 million into the forecast.

Dr. Tian said the Council built in an additional \$90 million for 2013, but the formula for the tax year 2012 is no longer valid because of the rule change. He said he wanted to report to the Council that there are several components for the tax credits; solar water heating, for which the number is almost exactly the same as 2012 and 2013 (about 3,000 permits for the new solar water heating in 2013, which is the same as in 2012). He said there is also an issue between the permit and actual construction. He said according to the permit numbers and HECO (Hawaiian Electric Company) connections, about 60% of the permits went into the actual installations. Dr. Suyderhoud asked if it is possible to set up a system without net metering. Dr. Tian said the permitting and net metering is about 60%. He said this year, the number of residential PV permits is running at about 1,000 per month. He said so far, up to the end of August, there is an increase in terms of number of permits,

but that for the last 4 months of last year every month was 2,000, so there were about 12,000 for the whole year.

Dr. Bonham said you will not see 2,000 permits for the last two months of this year, because there is no threat of a law change. He said you can claim \$5,000 per system and you can install multiple systems on a roof under one permit. Chair Kawafuchi said yes, even under the new rules. Dr. Tian said this is why it is difficult to calculate, but if you assume one system, one tax map key and \$5,000 maximum, that is equivalent to somewhere around \$52 million. He said if you can still claim multiple, that is a different story, so his simple calculation for water heating is about \$60 million; commercial is somewhere around \$20 million. He said altogether it should be somewhere around \$80 million. Dr. Bonham said there are huge uncertainties, because we do not know why the 60% of permits became net metering and we do not know if people installed them or not. Dr. Tian thought it had something to do with HECO. He said when they connect to the meter, the taxpayer is qualified for a tax credit, but HECO connection may be late. Dr. Bonham said 3 or 4 months late or even longer.

Chair Kawafuchi asked if there were any more discussion about the tax credits. Dr. Bonham asked, on a different topic, when we would get the money from Expedia. He asked if there was another appeal. Dr. Rousslang said he believed there was. He said he has asked the audit people to give him plenty of warning for the Council on Revenues when those funds are going to be released. Dr. Bonham said we are talking about a couple hundred, \$150 or \$160 million plus increased payments. Dr. Rousslang said there would be legal fees coming out of the money. Ms. Niwao said that might throw off the forecast. Dr. Suyderhoud asked if there was anything else. Dr. Rousslang said no.

### **GENERAL FUND REVENUE FORECAST:**

Chair Kawafuchi said the next topic is the general fund revenue forecast. Dr. Grandy asked if it would be appropriate to talk about a graph he had prepared before they discussed the forecast. Chair Kawafuchi said yes.

Dr. Grandy said he had sent around a graph of short-term forecast errors and was surprised that the Council was off 3 percentage points in the May forecast trying to forecast general fund revenue as of the end of following June. He said with 10 months of data, the uncertainty should be pretty small. He said his motivation for doing the graph was to see whether the 3 percentage point errors are unusual. He said the good news is that they were not unprecedented, but the bad news is that they are large. He said the Council tends to under-forecast as the economy is improving and tends to over-forecast as the economy turns down. He said the Council has been missing the overall macro-conditions.

Dr. Suyderhoud asked Dr. Grandy if he thought that the main reason for the errors is that the Council is "in the weeds." Dr. Grandy said that is what he is suggesting. Dr. Suyderhoud was wondering if there were alternative explanations, other than modeling tends to miss the turns on a regular basis. Dr. Bonham asked Dr. Suyderhoud to think about their long history on the Council and cite specific examples. He said he remembers instances when the debate centered around some kind of tax refund or tax credit, and missed the fact that jobs were falling in the State economy. He said he was more concerned about the slightly longer-term forecast errors. He said he understood why one might focus on the short-term forecast errors, since one would expect the error to be small

in May, but that at the beginning of last fiscal year, the forecast was 4.9%. He said Act 221 was another topic that received much attention in the members' debates, when they should have been focusing on macro-issues. Ms. Niwao said she wanted to be more comfortable with what is happening with the Tax Department as far as collections, accounts receivable and other tax matters.

Ms. Niwao said there is information on accounts receivable. She said sometimes they collected the accounts at one time and also big numbers like the Expedia case, and yet the members did not have very much information on these things. She said the members would need advanced notice on these things. She said the data used to be on the Tax Department's website.

Dr. Bonham disputed whether the data was available on the Tax Department's website in a timely manner. Ms. Niwao said many of the old reports, like those on the individual income tax, were no longer being done. Chair Kawafuchi said it has to do with staffing.

Dr. Bonham returned to the issue that Dr. Grandy had raised. He said he found that since the big downturns in 2009, 2010, the Council's September forecasts were, on average, 1.8% too low, so the members missed the upturns. He said the members had a conversation about the tendency to under-forecast during recoveries, but nevertheless lowered the forecast. He said he is pretty sure it was in the September meeting last year that the members lowered the forecast because of the solar tax credits. He said spending all of their time talking about things like the solar tax credit instead of things like visitor arrivals growing at 8% a year and room rates going up, might cause them to miss the forecast. He said the forecast that came out of his model was for growth of 8.5%, but the members picked 4.9% at the beginning of last year. Dr. Suyderhoud asked if Dr. Bonham was suggesting spending less time talking about the solar tax credit numbers or other legislative changes. Dr. Bonham said just let Dr. Rousslang decide what is important on the tax rules. Dr. Grandy said there was a tremendous amount of expertise around this table that was helpful, but that the members needed to determine which things were more important, and that they ought to be able to do better in May than missing the forecast by 3 percentage points.

Dr. Suyderhoud said he shared the frustration in dealing with short-term data, for instance when the July numbers came in one wonders what happened. He said it was a mistake to focus too much on short-term phenomenon rather than on the more important underlying macro-economic factors.

Dr. Bonham said the forecasting experience over the last 5 or 6 years has led him to believe that the paying attention to short-term "noisy" data often causes forecasters to doubt their models and to end up reducing the quality of their forecasts.

Dr. Suyderhoud said we are somewhat victims of the calendar in the sense that we are required to make a January and a May forecast, and sometimes it is really needed. He said they have had June surprises in the past also.

Dr. Bonham said that in the past, issues such as TAT collections, refunds, or delinquent taxpayers (where the Tax Department suddenly found 2 or 3 hundred million dollars) have disrupted the forecast. Ms. Niwao said that is why she wanted better information from the Tax Department, including on receivables. She said the receivables went way up and on the downturn in 2009/2010, so the question is when that money would be collected. She said when the economy does better they start collecting more money, which magnifies the effect of the upturn. Dr. Suyderhoud said

the point is that there is a lot of noise when you are on a cash basis vs. accrual basis. Ms. Niwao said that is correct, but there is a way you can manage the problem when you know what the receivables are. Dr. Grandy said he thought the macro-effects swamp such considerations for the most part. Dr. Suyderhoud agreed that it was not a good idea to pay too much attention to that kind of information to the neglect of more fundamental economic issues.

Dr. Suyderhoud asked if the Council should start talking about the forecast. Chair Kawafuchi said yes. Dr. Suyderhoud asked if the members collectively were coming in at 6.8% growth for FY 2014. Dr. Rousslang said yes that is the result from the standard model.

Dr. Suyderhoud said the UCLA model is coming in stronger than the traditional model. Dr. Bonham asked if there is an average of all the models' results. Dr. Rousslang said yes, in Table 6A. Dr. Suyderhoud asked if that was a below-the-line number. Dr. Rousslang said yes. Dr. Suyderhoud said the average above-the-line number was about 7%. Dr. Bonham said the average comes out to 6.8%. Chair Kawafuchi asked Dr. Rousslang what are some of the major differences between the Tax model and the UCLA model. Dr. Rousslang said only the first 3 tax items were different, namely the GET, the individual income tax, and the corporate income tax. He said for all the other items, the UCLA model uses the results for the standard model, because it does not have its own equations for them. He said the differences in results for the GET are very small, but they are more important for the individual income tax and the corporate income tax. He said the thing he would point out about is that the UCLA model does not use total personal income to forecast individual income tax collections. He said from 2006 to 2012 total personal income grew something like 27%, but individual income tax collections declined slightly, so something was going on that changed the relationship between total personal income and net income tax collections. He said he thought capital gains might be the biggest factor. Dr. Bonham said there has not been tremendous growth in personal income from 2008 to 2012.

Ms. Niwao said there were large capital gains in 2012. Chair Kawafuchi asked if the income level went up but the tax amount went down. Dr. Rousslang said taxes declined slightly. Ms. Niwao and Ms. Maynard asked if that was after tax credits. Dr. Rousslang said yes.

Dr. Grandy asked if capital losses could be the cause. Dr. Rousslang said he thought it was failure to have capital gains, or recognize capital gains. He said he does not know what the capital gains were for Hawaii, since we have not done an individual income tax study. Dr. Bonham said dividends and interest were almost completely flat from 2008 until now, but that he knew these categories did not reflect capital gains.

Dr. Suyderhoud asked where there was a big change. Ms. Niwao said capital gains. Dr. Bonham said labor income went up only by 3.39%.

Dr. Grandy said things were slowing, but it could be capital losses. Chair Kawafuchi agreed. Dr. Rousslang pointed out that total personal income does not include capital gains or losses. Dr. Suyderhoud said but it will show up in the tax collections.

Ms. Niwao asked if there were changes in the way total personal income is measured. Dr. Grandy said not to his knowledge. Dr. Bonham said there are redefinitions every once in a while. He said



he does not try to forecast the categories because some of them are extremely volatile, particularly corporate income.

Chair Kawafuchi agreed that corporate income is very volatile. Mr. Jahanmir said he did not think that wages and salaries went up as much as personal income did. Dr. Bonham agreed. Dr. Rousslang said the forecast error in the model was in the individual and corporate income tax collections.

Dr. Suyderhoud asked to bring the discussion back to the forecast. Chair Kawafuchi said yes. Dr. Suyderhoud said the models were indicating growth of roughly 7% for 2014, and roughly 8% for 2015. Ms. Niwao said the last forecast was for growth of 6.4% and 5.7%. Dr. Bonham disagreed. He asked Dr. Rousslang if the above-the-line forecast for FY 2014 was 8.6% growth, so that a new above-the-line forecast of 6.8% or 7% would knock 1.8 percentage points off the forecast. Dr. Suyderhoud said, yes, but that the forecast for 2015 was increased from 6.7% to 8%. Dr. Bonham agreed that having the growth rate come down made sense, because of the end-of-year surprise in FY 2013, but perhaps not as much as the members were indicating. Dr. Suyderhoud asked if Dr. Bonham meant to say perhaps not as much as the models were suggesting. Dr. Bonham said yes, not as much as the models suggest. Dr. Bonham said usually the members do the forecast one year at a time, to avoid confusion. Chair Kawafuchi said we are looking at FY 2014. Dr. Bonham said his model forecast 7.8% growth for the general fund, but that his model does not include the tax law changes. Dr. Suyderhoud said that forecast was also lower than the May forecast for 8.6% growth. Dr. Bonham said yes he is okay with it being a little bit lower because some of that was probably a technical issue.

Dr. Suyderhoud said we are now operating on a higher base, and before, for 2014 we had 8.6% above-the-line, and for 2015, 6.7% above-the-line. Dr. Bonham said another way to look at it was to go back and look at the levels. Dr. Suyderhoud asked Dr. Bonham to suggest a number for discussion purposes. Dr. Bonham said 7.8%. Ms. Niwao asked why go down from the May forecast. Dr. Suyderhoud said because the base was higher. Dr. Bonham said things like a slowdown in visitor spending, higher room rates that seem to be affecting other visitor spending, the change in the exchange rate, and rising airfares might cause him to revise his forecast downward. He said the value of the yen is not going to keep changing, so we have seen most of that movement and it would not continue to be a growth factor in 2016. He said his reports have pointed to a need for strong economic growth in the rest of the world so that they become comfortable paying higher hotel rates and airfares. Chair Kawafuchi asked if interest rates were likely to go up. Ms. Niwao said yes, interest rates have been going up quite a bit.

Ms. Niwao said the home mortgage interest rates have gone up 1 point. Dr. Bonham pointed out that they are still at levels not seen for thirty years. Dr. Suyderhoud said affordability is still very good. Dr. Bonham agreed, but said that the problem is that there is nothing for sale. He said he expected to see prices to rise significantly and for that to contribute to more construction activity. He said he does not see the rise in the mortgage rate right now as a problem. He said the UHERO (University of Hawaii Economic Research Organization) forecast for the mortgage rate is for below 5% rates all the way into 2016.

Dr. Suyderhoud said the original forecast was for \$6050 million in FY 2014. Dr. Bonham said yes, \$6050 million above-the-line. Dr. Suyderhoud said with 7.8% on a higher base it is \$6.84 billion,

so we are actually increasing even though we are lowering the growth but applying it to a higher base and therefore the dollar amounts are bigger. Dr Rousslang pointed out that one change in the model that should have been in the earlier version is that roughly one percent is going to the Hurricane Relief Fund. Dr. Bonham asked if that was in the last model. Dr Rousslang said no, it was not in the model before. Dr. Grandy said it is a direct transfer from the general excise tax for two years. Dr. Rousslang said yes, and that it is roughly 1% of the total general fund tax revenues. Dr. Suyderhoud asked if the transfer occurred in 2013. Dr. Rousslang said no. Dr. Bonham asked what that meant. Dr. Rousslang said it was not in the below-the-line adjustments. Chair Kawafuchi said it is in Table 6AA the first line. Dr. Suyderhoud asked if it was part of the \$133 million below-the-line adjustment for the GET. Dr. Rousslang said yes, and the other part is the effect of Act 105. Chair Kawafuchi asked how 1% is \$132 million? Dr. Rousslang said no, the 1% is \$55.5 million for the transfer to the Hurricane Relief Fund.

Dr. Grandy said his personal forecast is growth of 6%, and that he thought that the economy is slowing down a bit. He said the question is how much is it slowing down. Ms. Niwao said she could see the slowdown. Dr. Grandy said he would be interested in hearing what others have to say. Chair Kawafuchi asked what factors Dr. Grandy was looking at to conclude that the economy is cooling. Dr. Grandy said personal income growth and visitor expenditure growth have been trending down for a while now, as well as other indicators.

Dr. Bonham said he had thought this upturn is a little different from past upturns, because up until the last 6 months it has been only about tourism, with nothing else really contributing to growth in the State's economy. He said construction had been acting as a drag on the economy. He also said the State and local governments, through attrition of work force, spending cuts and tax increases, were also a drag on economic growth. He said some of the surge in revenues came from tax law changes that were put in place in the midst of the crisis. He said he would argue that these two big drags during the last couple of years are now reversing.

Ms. Maynard asked how much construction contributes to the economy as opposed to tourism. Dr. Bonham said it contributes tremendously in tax revenues. He noted that his forecast for construction was high. Dr. Grandy said he thought the contracting tax base looked as though it might be peaking now. Dr. Bonham did not agree. He said if it is the contracting tax base is peaking right now, permit data would be going down and you would have actual activity going down. Dr. Grandy said he meant the rate of growth is peaking at around 20% and that he did not see it going much above its historical level in 1991. Dr. Bonham said one difference might be differences in inflation. He said another factor was the federal government, which could pose another drag on the economy.

Dr. Suyderhoud asked if they could go around the table and get the members' forecasts. He said he would be comfortable with something in the high 7%'s. Chair Kawafuchi asked if the members wanted to discuss it further or if they wanted to take a vote. Ms. Maynard said she likes 7%. Dr. Grandy said maybe some of the other members had a number that they would like to discuss. Chair Kawafuchi asked Ms. Niwao if she had a number. Ms. Niwao said 6.3% or so, but that she was worried about the decline in tourism.

Ms. Maynard said her concern was also a slowdown in the visitor industry. Ms. Niwao said the question is how big the downturn in visitor spending would be verses the upturn in construction.

Dr. Bonham moved for 7%. Dr. Suyderhoud seconded the motion. Ms. Maynard and Ms. Niwao agreed to 7%. Dr. Suyderhoud asked if all were in favor. Chair Kawafuchi said it is unanimous and we are done with 2014.

**Dr. Bonham made a motion that the general fund tax revenues growth rate be at 7% for FY 2014. Dr. Suyderhoud seconded. The Chair called for the vote, and the motion passed with the following votes:**

<b>Kurt Kawafuchi</b>	<b>Yes</b>
<b>Marilyn Niwao</b>	<b>Yes</b>
<b>Jack P. Suyderhoud</b>	<b>Yes</b>
<b>Carl S. Bonham</b>	<b>Yes</b>
<b>Christopher Grandy</b>	<b>Yes</b>
<b>Elizabeth P. Cambra</b>	<b>Absent</b>
<b>Kristi L. Maynard</b>	<b>Yes</b>

Dr. Rousslang asked for clarification that the forecast was for above-the-line growth and asked if the below-the-line adjustments were all adopted. Dr. Suyderhoud asked if the Council is adopting all the below-the-line adjustments. Ms. Niwao said yes. Ms. Maynard said she moves that they adopt the below-the-line adjustments. Ms. Niwao seconded the motion. The Chair asked if all were in favor. It was unanimous.

**Ms. Maynard moved that the Council adopt the below-the-line adjustments. Ms. Niwao seconded. The Chair called for the vote, and the motion passed with the following votes:**

<b>Kurt Kawafuchi</b>	<b>Yes</b>
<b>Marilyn Niwao</b>	<b>Yes</b>
<b>Jack P. Suyderhoud</b>	<b>Yes</b>
<b>Carl S. Bonham</b>	<b>Yes</b>
<b>Christopher Grandy</b>	<b>Yes</b>
<b>Elizabeth P. Cambra</b>	<b>Absent</b>
<b>Kristi L. Maynard</b>	<b>Yes</b>

Next, the Council discussed the general fund revenues forecast for FY 2015. Ms. Niwao said her concern was small businesses that would be hurt by a health insurance rate increase caused by the affordable care act. She said the changes would cause her small firm to go up from \$575 per month to about \$1,400. Dr. Grandy said that may be true, but he was not sure how that would translate into general fund revenue changes. He said the rate increases are not really a surprise, we have known they were going to for a while. Ms. Niwao said not that much.

Dr. Grandy said he was not aware of any study of the effect of Obamacare on Hawaii's economy, but that the Congressional Budget Office has done the economic analyses for the overall economic impact on the country and that they expect the economic effects on GDP (Gross Domestic Products) to be positive, not negative. Dr. Bonham said we do not actually know what the effects would be, but that we would know pretty soon. Ms. Niwao said the health insurance exchange is going into effect October 1<sup>st</sup> and the individuals and sole proprietors can buy from the exchanges. She said for

small businesses that have group plans, like her firm, the rate changes start July 1<sup>st</sup> of next year. Dr. Suyderhoud said there was a lot of uncertainty associated with the health care changes and asked how many of the members felt comfortable adjusting the revenue forecast for 2015 based on the uncertainty associated with the implementation of affordable care and asked what changes they might suggest.

Ms. Niwao said probably by December we should have a better idea. Dr. Suyderhoud said that would be in time for the January meeting. Chair Kawafuchi asked if the Council should wait to try to incorporate the effects of the health care changes until later. Ms. Niwao said yes. Dr. Suyderhoud said they still have to make a forecast for FY 2015. Dr. Bonham said in their calendar year forecast, 2014 and 2015 are the strongest years of the cycle. Dr. Grandy agreed. He asked if growth for FY 2015 would be higher or lower than 7%. Dr. Bonham thought it would be higher. Dr. Suyderhoud said his model also says higher. The Chair asked for a specific number. Dr. Suyderhoud said his model estimated 8.2% for 2014 and 9.3% for 2015.

Ms. Maynard said she would feel more comfortable with a flat 7% growth forecast for both years. Ms. Niwao agreed. Ms. Maynard added that it does not feel like things are going that well. Dr. Bonham agreed. Dr. Suyderhoud said but they would be. Dr. Grandy said he was not sure he could agree with a pattern where revenue growth for FY 2015 would be higher than for FY 2014.

Chair Kawafuchi asked if they had a number. Ms. Maynard said she liked 7%. Ms. Niwao said she would be comfortable with 7% rather than higher because she thought there are many uncertainties that she could not quantify. Dr. Suyderhoud suggested 7.5% or 8%. Dr. Bonham pointed out that Dr. Suyderhoud's forecasts were higher than that. Dr. Suyderhoud agreed. Dr. Grandy asked if Dr. Suyderhoud believes growth would be as high as his model. Dr. Suyderhoud said probably not.

Ms. Maynard made a motion for 7% for FY 2015. Ms. Niwao seconded the motion. Chair Kawafuchi asked who is in favor of 7%.

Chair Kawafuchi asked if the below-the-line growth forecast is over 7%. Dr. Grandy said yes, slightly more than 7%. He suggested that the members focus on the above-the-line forecast, because the below-the-line adjustments are just arithmetic to account for tax law changes. The Chair agreed. Ms. Niwao asked if they needed a motion for that. Dr. Suyderhoud said it is in the motion that they accept the Department's below-the-line adjustments.

**Ms. Maynard made a motion that the general fund tax revenues growth rate be at 7% for FY 2015 (above-the-line) and, accepting the Tax Department's below-the-line adjustment. Ms. Niwao seconded. The Chair called for the vote, and the motion passed with the following votes:**

<b>Kurt Kawafuchi</b>	<b>Yes</b>
<b>Marilyn Niwao</b>	<b>Yes</b>
<b>Jack P. Suyderhoud</b>	<b>abstain</b>
<b>Carl S. Bonham</b>	<b>abstain</b>
<b>Christopher Grandy</b>	<b>Yes</b>
<b>Elizabeth P. Cambra</b>	<b>Absent</b>
<b>Kristi L. Maynard</b>	<b>Yes</b>

Chair Kawafuchi asked about the forecast for the out years. Dr. Suyderhoud made a motion to adopt Table 6AA above-the-line forecasts for the FYs 2016 through 2020, specifically, growth rates of 6.9%, 6.3%, 5.8%, 5.2% and 4.8%. Ms. Maynard seconded the motion. The Chair asked for a vote. It was a unanimous yes vote. Dr. Suyderhoud said the motion was also to adopt the below-the-line adjustments from the Tax Department.

**Dr. Suyderhoud made a motion to adopt Table 6AA (above-the-line) the general fund tax revenues growth rates for the out years: FY 2016 (6.9%); FY 2017 (6.3%); FY 2018 (5.8%); FY 2019 (5.2%); and FY 2020 (4.8%) along with the below-the line-adjustments made by the Tax Department. Ms. Maynard seconded. The Chair called for the vote, and the motion passed with the following votes:**

<b>Kurt Kawafuchi</b>	<b>Yes</b>
<b>Marilyn Niwao</b>	<b>Yes</b>
<b>Jack P. Suyderhoud</b>	<b>Yes</b>
<b>Carl S. Bonham</b>	<b>Yes</b>
<b>Christopher Grandy</b>	<b>Yes</b>
<b>Elizabeth P. Cambra</b>	<b>Absent</b>
<b>Kristi L. Maynard</b>	<b>Yes</b>

Next, the Council heard the report by Budget and Finance.

Mr. Chun provided the Council with revenue updates for Budget & Finance.

**REPORT BY THE DEPARTMENT OF BUDGET & FINANCE ON OTHER REVENUES:**

**Significant Changes from May 2013 Report**

**General Fund Non-Tax Revenues**

**Charges for Current Services** - increase in FY 13 reflects higher than estimated refunds and reimbursements from federal programs, primarily Obamacare drug rebate collections (Department of Human Services (DHS)).

**Special Tax Revenues**

**Unemployment Compensation Tax** - increases in FYs 13 and 14 are attributed to more employers contributing at higher rates than projected. The increases are offset by decreases in FYs 15-20 due to the anticipated lowering of the contribution rate for employers as unemployment rates are low (Department of Labor and Industrial Relations (DLIR)).

**Conveyance Tax** - increases in FYs 13 and 14 reflect actual FY 13 revenues and revised FY 14 projections that are more consistent with the actual collections. These revenues are deposited to DBEDT's Rental Housing Trust Fund.

**Special Fund Non-Tax Revenues**

**Federal Grants** - increases in FYs 13-20 reflect an increase in unemployment compensation benefits to federal employees and ex-servicemen in FY 13 (actual) and FY 14 (projections) (DLIR).

**Non-Revenue Receipts** - the increase in FY 13 reflects the actual transfers that were made to the Department of Education's (DOE) State Educational Facilities Improvement Special Fund and revised FYs 13-20 projections.

**Other than Special Fund Non-Tax Revenues**

**Federal Grants** - the net increases in FYs 13-19 reflect increases in federal funding for Operating Aid in Federally Impacted Areas (DOE).

**Current Services** - the increases in FYs 14-19 reflect revised projected revenues for the Medical Assistance Program (DHS).

Chair Kawafuchi asked that the Council move to accept the B&F report. The Council voted an all in favor to accept the B&F report as submitted.

**Dr. Suyderhoud moved to accept the B&F report as submitted and, Ms. Maynard and Ms. Niwao seconded. The Chair called for the vote, and the motion passed with the following votes:**

<b>Kurt Kawafuchi</b>	<b>Yes</b>
<b>Marilyn Niwao</b>	<b>Yes</b>
<b>Jack P. Suyderhoud</b>	<b>Yes</b>
<b>Carl S. Bonham</b>	<b>Yes</b>
<b>Christopher Grandy</b>	<b>Yes</b>
<b>Elizabeth P. Cambra</b>	<b>Absent</b>
<b>Kristi L. Maynard</b>	<b>Yes</b>

**NEXT MEETING:**

The Council's next meeting is tentatively scheduled for Thursday, October 31, 2013 at 2:00 pm, but the date and time will be confirmed by e-mail. The Council staff will attempt to secure the DLIR Conference Rooms 310/313 for the meeting.

**ADJOURNMENT:**

The meeting adjourned at 3:50 p.m.