

COUNCIL ON REVENUES

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

Thursday, March 12, 2015
2 p.m.

PRESENT:

Council Members:

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

Staff Members:

Department of Taxation (DOTAX): Donald Rousslang and J Guitguiten

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

Others:

Kate Stanley, Office of Senator Jill Tokuda
Julie Haruki, Senate Ways and Means
Nicolas Ayabe, Senate Ways and Means
Titin Sakata, Department of Taxation
S. F., DHS
Kevin Dayton, Star Advertiser
Sharon Kotaka, Budget & Finance
Eugene Tian, DBEDT
Josh Frost, Governor's Office
Jana Chang, Governor's Office
Brandon Asuka, Governor's Office
Ken Kuraya, DOE
Sheila Kanemaru, DOE
Bjorn Ramos, Senate President Mercado Kim's Office
Paul Young, HAH
Paul Harleman, Senate Minority Office
Nandana Kalupahana, House Finance
Ed Beal, Department of Taxation
Puna Na'auao, University of Hawaii

ABSENT:

Council Member:

Kristi L. Maynard

CALL TO ORDER:

Vice-Chair Niwao called the meeting to order at 2:05pm. A quorum was present.

PUBLIC COMMENTS OR COMMUNICATIONS TO THE COUNCIL:

Vice-Chair Niwao asked if there were any public comments or communications to the Council. There were none.

MINUTES OF THE MEETING OF JANUARY 6, 2015:

Vice-Chair Niwao called for a motion to approve the minutes for the meeting of January 6. Dr. Grandy moved to approve the minutes and Dr. Bonham and Dr. Suyderhoud seconded the motion.

It was moved by Dr. Grandy and seconded by Dr. Bonham and Dr. Suyderhoud that the minutes of the January 6th meeting be accepted. The Vice-Chair called for the vote, and the motion passed with the following votes:

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|----------------------------|---------------|
| Kurt Kawafuchi | Absent |
| Marilyn Niwao | Yes |
| Jack P. Suyderhoud | Yes |
| Carl S. Bonham | Yes |
| Christopher Grandy | Yes |
| Elizabeth P. Cambra | Yes |
| Kristi L. Maynard | Absent |

Vice-Chair Niwao asked that while waiting for Chair Kawafuchi to arrive, the Council move to item VII of the agenda "B&F's Report on Other Revenues" before taking up item IV "Discussion of Possible Growing Effects of Tax Refund Fraud."

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

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

Significant Changes from January 2015 Report

Special Tax Revenues

Conveyance Tax - the Department of Business, Economic Development and Tourism's Rental Housing Trust Fund increased their FY 15 projected revenues based on the actual FY 15 revenues collected to date. (\$10,000,000)

Other than Special Fund Non-Tax Revenues

Non-Revenue Receipts - the net increases in FYs 15-21 are reflective of the increased projections in employer and employee contributions by the State, City and County of Honolulu, City and County of Honolulu Board of Water Supply, County of Hawaii, Kauai County, Maui County, and Hawaii Department of Water to EUTF (B&F) based on actual contributions received through the first seven months of the fiscal year. (\$17,765,000 - Medical Health Benefits Premiums)

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

| | |
|----------------------------|---------------|
| Kurt Kawafuchi | Absent |
| Marilyn Niwao | Yes |
| Jack P. Suyderhoud | Yes |
| Carl S. Bonham | Yes |
| Christopher Grandy | Yes |
| Elizabeth P. Cambra | Yes |
| Kristi L. Maynard | Absent |

POSSIBLE GROWING EFFECTS OF TAX REFUND FRAUD:

Vice-Chair Niwao told the Council that she had some material on the tax refund fraud problem that she wanted to discuss. She said in 2006 the IRS did some extensive studies and issued a report on what they called a Tax Gap, which is the difference between tax revenue that has been collected and tax revenue that was actually owed by taxpayers. The Tax Gap results from non-filing of tax returns, underreporting of income, and underpaying of taxes. She also stated that in February 2015 the GAO (US Government Accountability Office) issued a report that the federal tax gap was \$450 billion in 2006, but the gap was reduced by \$65 billion by enforcement action and late payments, leaving a net tax gap of \$385 billion.

Vice-Chair Niwao stated that Hawaii has produced no formal studies of the Tax Gap that she was aware of, but that she believed the State's Tax Gap may be growing, making it increasingly difficult for the Council on Revenues to accurately forecast tax revenues. She said there is evidence of increasing noncompliance with Hawaii tax laws as more out-of-state businesses and individual taxpayers conduct business in Hawaii. She said some of the individuals may not file GET (general excise tax) returns, because they did not know that GET is assessed on gross service income and applies also to rental income, unlike the retail sales taxes of most states. A second group of taxpayers are willfully ignoring their Hawaii tax obligations, assuming they will not get caught. She said a decrease in the number of audits, for example, may cause people to say, "well, the businesses here are not paying their taxes, I know it, I reported them, and nothing was done. So if they don't pay their fair share of taxes, I'm not going to pay either because it will put me at a competitive disadvantage." She said that in the past couple of years, Congress also cut the funding for the IRS by about 10%, which caused less enforcement by the IRS, which probably will continue until the funding is restored.

She also said that there is sometimes a disconnect between the audits done by the IRS and what happens with the taxpayer's State tax returns. She said, for example, when there's an adjustment for a federal tax return, she didn't see the adjustment reflected on the taxpayer's State income tax return. She said in the past, many notices of federal adjustments would come automatically, but that she has not seen those notices lately.

Vice-Chair Niwao stated that there is also a third group of taxpayers who are in the business of defrauding Hawaii through fraudulent tax refund schemes and other methods. Going back to the first group (those who are not aware of their GET liabilities) she said the Hawaii Association of Public Accountants (HAPA) conducted a study in December 2009 of out-of-state CPAs who received a temporary CPA permit to practice in Hawaii in 2007/2008. The study found that over 70% of out-of-state CPA firms whose owners or employees obtained a temporary permit to practice in Hawaii did not have a Hawaii GET license number. Without a GET license, the out-of-state firms could not pay GET on their Hawaii source income. She said this also raises the question of whether the State was capturing the proper income taxes from those providing services to Hawaii consumers.

She stated she was concerned about the HAPA finding on noncompliance from practitioners, because the CPA's are tax advisors for a lot of out-of-state companies doing business in Hawaii. The out-of-state CPAs may not be informing the businesses of their Hawaii GET obligations due to lack of knowledge of Hawaii laws. She mentioned she had been involved in litigation support with out-of-state advisors who had not informed Hawaii businesses of their GET obligation. She said the number of Hawaii CPA licenses issued to out-of-state CPAs over the last few years has increased markedly so that now about 22.5% of all Hawaii CPA licensees are out-of-state or foreign CPAs. She said that as more people move to Hawaii to retire or start businesses, she sees more cases of non-compliance with Hawaii tax laws. She suggested linking business and professional licensing with registration for the GET license.

Dr. Grandy asked how much noncompliance had increased in the last several years. Vice-Chair Niwao said she thought it was quite a bit, because a lot of people were moving in now. Dr. Suyderhoud asked how big the effect of noncompliance was, whether it was on the order of \$100 million, because prior noncompliance was already in the data. He said the question was the amount by which growth in noncompliance reduced the Council's revenue growth forecast.

Vice-Chair Niwao said one reason she was concerned about the issue is that she noticed that the construction tax base in the last few years has gone up and down and that Council members had been talking for a while now about how the economy was supposed to turn around due to construction activity, yet revenue growth last year was negative 1.8%. She said a lot of out-of-state construction companies were now doing business in Hawaii. Dr. Suyderhoud said we've always had out-of-state construction firms. Dr. Bonham asked Vice-Chair Niwao what she was trying to explain with the construction tax base. Vice-Chair Niwao said she thought that more auditors were needed, because she had clients in construction who complained that they saw out-of-state construction firms not paying the GET and Use tax. Dr. Bonham said that was not a new phenomenon. Vice-Chair Niwao said that when there is a surge in demand or boom in construction activity, the local construction companies are often not able to handle all of the additional construction work, and developers and builders rely on out-of-state construction firms to handle some of the excess work. She said that with the influx of out-of-state firms coming to

Hawaii to do business, we might not be capturing the amount of GET revenue that you normally would have expected from the increase in construction activity. Dr. Bonham asked what she recommended.

Dr. Bonham said he had also been looking at the construction data, because they didn't reflect the expected strength and that there were many anomalies in them. But he said he wasn't sure that tax fraud was the main explanation. He said we didn't see the tax revenue growth from the construction boom and that maybe some of the cause was fraud, but he said tax law changes (Act 105) dragged down the construction tax base significantly last year. Vice-Chair Niwao said that Act 105 expired in 2013. Dr. Bonham thought it affected revenues through the end of last fiscal year. Vice-Chair Niwao said the effect would have shown up in FY 2013, but not in FY 2014. Dr. Bonham said it would affect growth in FY 2014 over FY 2013.

Dr. Suyderhoud said solar was another issue in the construction data. Dr. Bonham agreed and said that total permitting activity last year was very weak, so that the construction boom may not have materialized because it may not have happened. Rather than fraud, there may simply have been less activity than expected. He said the construction growth hasn't shown up in the permitting data, in the employment data, or in the tax data, so there was consistency among these sources and that tax fraud wasn't needed to explain the failure of the construction tax base to grow. Vice-Chair Niwao said it was not necessarily tax fraud, just non-reporting or noncompliance. Dr. Suyderhoud said he wanted to revisit the question of the size of the effect of growing tax noncompliance. He asked whether the effect of increasing noncompliance was a fraction of one percent, in which case it was not a material concern for the forecast.

Vice-Chair Niwao said the changes are that the IRS has lost a lot of their funding so they don't have as many auditors. Dr. Bonham said we still don't know how big it is and how much it would slow expected growth in revenues from the growing economy. He said noncompliance in tourism (informal bed and breakfast establishments) might also be an issue.

Vice-Chair Niwao said refund fraud was likely to occur when the following elements exist: incentive or pressure to commit a fraud (when someone really needs the money), opportunity to commit a fraud (is it simple to do?), and the ability to rationalize the act ("other people are doing it, I'll do it too"). She said the US Government Accountability Office has identified tax refund fraud as one of the government's top high risk weaknesses and that in February 2015 the GAO reported the IRS estimated that they paid out \$5.8 billion in stolen refunds in 2013 and that they prevented \$24.2 billion in tax refund fraud. Dr. Grandy said he looked at the article that Vice-Chair Niwao had distributed and it quoted a similar figure for the federal tax refund fraud. He said that was about four-tenths of 1 percent of total income tax receipts at the federal level in 2013. If we take that percentage and apply it to the Hawaii individual income tax, it was about \$7 million and the error in the Council's May forecast last year was 7 times that great, so the importance for the forecast was small. Vice-Chair Niwao noted that tax refund fraud is a growing problem.

Dr. Bonham said even if it were 5 times bigger, it would still be smaller than the typical forecast error. Vice-Chair Niwao said her point was about increasing leakages in the tax system. Dr. Bonham said he acknowledged the point but thought it might be more important to focus on the

slowdown in refund processing. Vice-Chair Niwao asked if the State was trying to hold back refunds to investigate fraudulent claims.

Dr. Bonham asked Dr. Rousslang to explain what was happening with refund fraud. Dr. Suyderhoud asked to move on to the next agenda item dealing with the general fund forecast for FY 2015.

GENERAL FUND REVENUE FORECAST FOR FISCAL YEAR 2015:

Vice-Chair Niwao said that the members had received a cumulative comparison showing refunds in FY 2015 have gone down quite a bit. Dr. Suyderhoud asked for explanation of the refunds. Dr. Rousslang said there was a change in processing that caused the accumulated refunds for February to grow. He introduced Edward Beal, the Department's Returns Classifying Officer, who said the refunds were being held up for further scrutiny because of tax fraud. Dr. Bonham asked how long the refunds would be held up and when the holdups started.

Mr. Beal said the holdups started when the tax season started. He said electronic refunds were taking about 4 to 6 weeks; paper refunds about 6 to 8 weeks. Dr. Suyderhoud asked how that compared with prior years. Mr. Beal said the refunds were about one month slower. Vice-Chair Niwao asked if the Department was seeing a lot more tax refund fraud this year. Mr. Beal said yes, it was growing. Vice-Chair Niwao asked if it was coming from TurboTax or from everywhere. Mr. Beal said the TurboTax incident appeared to be an isolated incident. Vice-Chair Niwao said there was a lot of identity theft. Mr. Beal said it was all identity theft. Dr. Bonham asked how delaying the refund helped prevent fraud. Mr. Beal said that the Department had put screens in place to identify likely fraudulent returns. Dr. Bonham asked if the extra time was for the screening. Mr. Beal said yes. Vice-Chair Niwao asked if the screening had been used in the past. Mr. Beal said the size of the problem is much larger than it was in previous years and it is growing.

Dr. Suyderhoud asked if this was known, because fraudulent returns have been detected. Mr. Beal said yes. Dr. Suyderhoud asked how the problem was affecting collections. Mr. Beal said there were two things: fraudulent refunds were prevented, and the extra scrutiny slows down the processing of refunds. Dr. Grandy said if revenue is higher this year because of the slowdown in refunds, the legitimate refunds will go out next year. Mr. Beal said the Department hoped to be caught up by the end of the fiscal year, except perhaps for those filing paper returns. Dr. Bonham asked what fraction of returns are filed after extensions and may be moved into next fiscal year. Mr. Beal said it was a 6-month extension to file a return. Dr. Bonham asked if it was large. Mr. Beal said it was large in the sense that most of the big refunds are returns on extensions that are filed October 20th. Dr. Grandy asked if, given the April 20th paper filing, the Department expected to be caught up by the end of the fiscal year. Mr. Beal said it was a goal, but that the big hold up is later in the fiscal year when most of the paper returns come at the filing deadline. Dr. Suyderhoud asked if fraudulent refund claims were the reason for the change in processing. Mr. Beal said yes.

Dr. Bonham said the statement in the preliminary monthly report said that the change processing caused refunds from last fiscal year to this fiscal year to fall by \$89 million, but that we didn't know that for sure. He asked if it was also possible that refunds fell partly because people owed

more tax. Dr. Rousslang said the presumption is that the big share of the refund decline is the delay caused by increased scrutiny given to the tax returns.

Dr. Bonham said there are economic reasons why refunds could be smaller - people owe more taxes because their income is increasing. Dr. Suyderhoud asked if the greater scrutiny to prevent fraudulent refunds could cause refunds to decline compared to prior years.

Mr. Beal said that if we rounded it to the nearest percent, that percent would be zero – the fraudulent refunds were not that significant in the past.

Dr. Bonham expected the refunds to be behind by a month or two at the end of fiscal year. Vice-Chair Niwao asked for the effect on the general fund collections for the fiscal year. Dr. Suyderhoud noted that the answer was given in the monthly collection report. Dr. Rousslang clarified that he had compared growth in gross collections before any refunds are subtracted out. Dr. Suyderhoud said the result was that growth in general fund revenues through February was 5.1%.

Dr. Bonham said if the refund processing got caught up by the end of the year, revenue growth would be 5.1 %.

Vice-Chair Niwao noted that growth in the GET revenue declined from 7% to 6.1%. Dr. Suyderhoud asked where the figures came from. Dr. Rousslang said they came from the preliminary monthly reports. Dr. Grandy asked Ms. Cambra for her opinion on growth in the economy from January. Ms. Cambra said it was about the same, that there were some changes from Japan, but nothing drastic and that despite the currency conversion, visitors from Australia were up from the market and projections, on top of the strong growth last year. She said airlifts still look solid and that domestic airfares were down to 2 to 3 hundred dollars and that there may be extra airlifts coming in towards the end of the year. She said they were optimistic for the year for the tourism industry.

Vice-Chair Niwao said one of her concerns was that U.S. growth would lead to additional foreign currency exchange rate strength of the dollar and raise the price of Hawaii vacations to foreign visitors and make foreign destinations more attractive to U.S. tourists, especially those from the East Coast. Ms. Cambra said those were fair points, but noted that the East Coast was not a major feeder for Hawaii visitors. Vice-Chair Niwao agreed, but pointed out that Canadians might also find other destinations more attractive. Ms. Cambra said she had just been in Fiji and said their Australia business is off, because Australians were going to Bali and some other destinations. She said Hawaii tourism is continuing to grow.

Dr. Suyderhoud said that in spite of the strong dollar, they were still expecting a relatively strong year in the tourism sector. Ms. Cambra said she thought Mexico was a more important source of competition to Hawaii than was Europe.

Dr. Bonham said their most recent forecast showed a small decline in growth of total visitor arrivals, from about 2% to about 1%. He said they were expecting growth from Asia, except Japan. He said they were expecting strong growth from the US. He said exchange rates were important and would affect visitor spending as well as visitor arrivals.

Ms. Cambra said that growing airlift does not necessarily mean all of our hotels or vacation rentals will experience that increase.

Vice-Chair Niwao said she thought the neighbor islands would benefit more from the US mainland travelers than Honolulu. Dr. Bonham said Honolulu was full, that occupancy rates on Oahu would stay high and that room rates would stay relatively stable, so the neighbor islands should benefit. Ms. Cambra said except for Lana'i because they're closing down their hotels. Dr. Grandy asked for forecasts for visitor arrivals and expenditures for the coming fiscal year. Dr. Suyderhoud said for FY2015 he had growth in arrivals at 3% and for FY 2016 growth in arrivals of 2%. His forecast for growth in expenditures was 4% for FY 2015 and 4.2% for FY 2016.

Vice-Chair Niwao noted that Mr. Kawafuchi had arrived.

Dr. Bonham said he had growth in visitor arrivals of 2.6% for FY 2015 and 0.75% for FY 2016 and growth in visitor expenditures of 2.25 in FY 2015 and 1% in FY 2016. He said he thought construction would really start to grow this year. He noted that there were variety factors, for one thing, residential permitting fell in 2014, but he noted that in Kaka'ako one can see high rises going up that don't yet have a permit issued. He said in talking to builders, it was evident they were hitting capacity constraints. He also mentioned the slowdown in construction of the rail. Vice-Chair Niwao said that a lot of people have gotten approvals for photovoltaic installations, which means more construction but also more tax credits.

Mr. Kawafuchi asked Dr. Rousslang the size of the additional refunds that were being held. Dr. Rousslang said it was about \$90 million, cumulative through February compared with the same period last year. Mr. Kawafuchi said it was his experience that a lot of people file their refund claims very early when they have the low income housing credits or other refundable credits. Dr. Rousslang said his figure of \$90 million included only individual refunds.

Mr. Kawafuchi asked if the refund fraud extended beyond the individual returns. Dr. Rousslang said the corporate collections and refunds varied so much from year-to-year that he did not try to examine their effect. Mr. Kawafuchi also noted that the corporate refunds were small. Dr. Rousslang said yes. Mr. Kawafuchi asked when the Department expected to get caught up on the refund claims. Dr. Bonham said the Department was hoping to be caught up by the end of the fiscal year, but that most of the returns at the April deadline are paper returns so there are no guarantees.

Vice-Chair Niwao noted that this filing cycle is delayed, because brokerage companies took longer to issue the 1099s and that new repair and capitalization rules slowed return preparation for anyone who owns a business. She said anybody who has a rental property or a schedule C business and depreciable assets would have to deal with the new repair and capitalization rules. Mr. Kawafuchi asked if it was fair to say that more people would have extensions this year. Vice-Chair Niwao said she wasn't sure.

Dr. Bonham moved to adopt 5.5% for revenue growth this fiscal year and all remaining fiscal years in the budget window. Dr. Grandy seconded the motion.

Vice-Chair Niwao asked about the growth projection from the preliminary monthly report, indicating growth of only 5.1%. Dr. Rousslang said that was the projection if we grow the rest of the year at the rate we did, cumulatively, through the end of February and if refunds are caught up by the end of the fiscal year. Dr. Bonham noted that it was not a magic number. Dr. Suyderhoud said it was just the number as of the end of February. Dr. Grandy said it was according to Dr. Rousslang's estimate. Dr. Suyderhoud noted that refund processing might not get caught up by the end of the year. Vice-Chair Niwao asked if there was further discussion, or if Mr. Kawafuchi wanted to take over and chair the remainder of the meeting. Mr. Kawafuchi said the members could finish up the forecast for the current year. Dr. Bonham said his motion was for all years in the budget. Dr. Grandy noted that the growth rates were supposed to be forecast separately according to the agenda. Dr. Bonham apologized and withdrew his motion and moved instead to adopt 5.5% growth for FY 2015. Dr. Grandy seconded the motion. Vice-Chair Niwao asked for further discussion. Ms. Cambra said she had no questions. Vice-Chair Niwao called for the vote. The motion carried.

Dr. Bonham made a motion that the general fund tax revenues growth rate be at 5.5% for FY 2015 (below-the-line). Dr. Grandy seconded. The Vice-Chair called for the vote, and the motion passed with the following votes:

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|----------------------------|----------------|
| Kurt Kawafuchi | Abstain |
| Marilyn Niwao | Abstain |
| Jack P. Suyderhoud | Yes |
| Carl S. Bonham | Yes |
| Christopher Grandy | Yes |
| Elizabeth P. Cambra | Yes |
| Kristi L. Maynard | Absent |

GENERAL FUND REVENUE FORECAST FOR FISCAL YEARS 2016 THROUGH 2021:

(Mr. Kawafuchi takes over as Chair.) Dr. Grandy moved that the forecast for FY 2016 through 2021 be 5.5% in each year. Ms. Cambra seconded the motion. Ms. Niwao noted that increasing the forecast for FY 2015 automatically increased the forecasts for the out years. Dr. Grandy said the discussion was about growth rates, which he felt more comfortable forecasting than levels.

Chair Kawafuchi noted that inflation hasn't been as strong as people were expecting, which also affected growth rates, because gross receipts are nominal amounts. Ms. Niwao also noted that the Federal Reserve may increase interest rates. Dr. Bonham commented that interest rates will be going up. Dr. Suyderhoud said yes, but precisely for the reasons that the growth forecast was for 5.5%. Dr. Bonham said, yes, namely that the economy would be improving, new construction and job growth would be strong, and the visitor industry would prosper.

Ms. Niwao said the dollar would become stronger, whereas other countries would lower their interest rates, reinforcing the effect on the exchange rate. Dr. Suyderhoud noted that the motion had been made and seconded. Chair Kawafuchi asked if there was further discussion. He noted that increasing the forecast for the first year automatically increased the forecasts for the out

years. Dr. Suyderhoud said yes, but the people who made the motion understood that and anyway forecast growth of 5.5% for the out years.

Ms. Niwao asked for the source of growth in the next year. Dr. Bonham said it was wage growth. Dr. Grandy said tourism was also starting to grow again. Dr. Bonham said the Council's mean forecast for growth in calendar year wages averaged about 3.5% per year from 2015 to 2021 and the mean forecast for the Consumer Price Index is just under 2% for FY's 2015 and 2016 and about 2.1% or 2.2% for the out years. Putting together the real and nominal figures yields nominal growth forecasts of about 5%. He noted that tax revenues typically grow faster than income.

Chair Kawafuchi asked Ms. Cambra for her opinion. Ms. Cambra said she had seconded the motion. Chair Kawafuchi asked for Dr. Bonham's opinion. Dr. Bonham said he had moved for 5.5% growth for the out years earlier. He said he saw no reason to change it from the previous meeting.

Dr. Bonham noted that the econometric models yielded average growth forecasts of about 5%. Ms. Niwao asked about the money from the tax case with the online travel companies. Dr. Rousslang said he would apprise the Council immediately when the case was settled. Chair Kawafuchi noted that a lot of money was at stake. Ms. Niwao said that's why she would like to start monitoring that case and see what happens. Dr. Suyderhoud asked if they could vote on the motion before them. Chair Kawafuchi asked Ms. Niwao if she had concerns over the forecast in the motion. Ms. Niwao said she thought the dollar appreciation might adversely affect tourism. Chair Kawafuchi said he had not seen cheap airfares in a while. Ms. Cambra said airfare is down \$200 to \$300. Chair Kawafuchi noted that it was hard to get even \$400 airfares. Ms. Cambra said the price is down \$200 to \$300 from the mainland. Dr. Bonham said there were West Coast roundtrips to San Jose or Bellingham or places like that in the \$300 to \$400 range. Chair Kawafuchi said the Los Angeles and San Francisco fares were still \$500 and sometimes \$600. Ms. Cambra said those prices were down though. Chair Kawafuchi said yes, at one point the airfares were \$800. He asked if growing inflation was enough to push up the out years to 5.5% straight across.

Dr. Suyderhoud said 2.5% growth in inflation and real personal incomes gives you 5% nominal growth. Chair Kawafuchi noted that construction was forecast to fall off after FY 2017. Dr. Suyderhoud said yes, but that was built into the forecast. Chair Kawafuchi asked if nominal income growth was 5%, what would push revenue growth up to 5.5%? Dr. Suyderhoud said because traditionally revenues grow faster than personal income does. Chair Kawafuchi asked if we could continue to grow at that rate. He said it was hard to grow at 5% for an extended period. Dr. Bonham agreed, but said it mattered greatly where we are in the business cycle. He said he would argue that between now and 2018, 2019, we're in the growth phase of this cycle still, but that growth would decline in the out years. Chair Kawafuchi agreed with this assessment. He said he could see growth of 5.5% for the next two or three years, but in the out years he was more pessimistic, although obviously it's harder to predict the out years too.

Dr. Grandy said if you plot the growth rates you see the swings in the business cycle, but the difficulty for him was predicting the next significant downturn. Given the uncertainties, he thought the most reasonable forecast was the long run growth in the past, which he thought was

5.5% to 5%. Ms. Niwao said she had one more question, about demographics. She said the baby boomers are about ready to retire in the next few years and traditionally when people retire, they don't spend as much as when they were working. She asked why not put something in the model to reflect the demographic shift.

Dr. Grandy said the forecast reflects the demographics that are built into the data. Dr. Bonham-said he thought the business cycle would swamp the secular trend of the demographics over the near term (to 2021). And, as Dr. Grandy pointed out predicting when that cycles going to end and when it doesn't is challenging. Dr. Suyderhoud asked what growth rate forecast Ms. Niwao preferred. Chair Kawafuchi said he would put down 5% for the last few years. Dr. Bonham said he did not think the difference was material and that he could agree with 5% for FY 2019, 2020 and 2021. Dr. Suyderhoud asked if the motion was to be changed. Dr. Grandy said he could change the motion. Chair Kawafuchi asked Ms. Niwao for her opinion. Ms. Niwao said she was more comfortable with the lower forecast. Dr. Grandy withdrew the motion he made and moved instead that the forecast for FY's 2016, 2017, 2018 be 5.5% and FY's 2019, 2020 and 2021 be 5%. Dr. Bonham-seconded the motion. Chair Kawafuchi called for a vote.

Dr. Grandy made a motion that the general fund revenue forecast for the remaining fiscal years be: 5.50% (2016); 5.50% (2017); 5.50% (2018); 5.0% (2019); 5.0% (2020); 5.0% (2021) below-the-line. Dr. Bonham seconded. The Chair called for the vote, and the motion passed with the following votes:

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|----------------------------|---------------|
| Kurt Kawafuchi | Yes |
| Marilyn Niwao | Yes |
| Jack P. Suyderhoud | Yes |
| Carl S. Bonham | Yes |
| Christopher Grandy | Yes |
| Elizabeth P. Cambra | Yes |
| Kristi L. Maynard | Absent |

NEXT MEETING:

The Council tentatively agreed to meet on Thursday, May 21, 2015 at 2pm; 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 3:28 p.m.