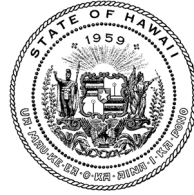


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COUNCIL ON REVENUES

STATE OF HAWAII
P.O. BOX 259
HONOLULU, HAWAII 96809-0259

January 8, 2021

The Honorable David Y. Ige
Governor, State of Hawaii
Executive Chambers
State Capitol, Fifth Floor
Honolulu, HI 96813

Dear Governor Ige:

The Council on Revenues held a virtual meeting to forecast revenue growth for the State General Fund on January 7, 2021. The Council changed its forecast to -6.5% from -11.0% for fiscal year (FY) 2021. The Council lowered its forecast for FY 2022 from 8.5% to 6.0%. The Council forecasted that General Fund revenues will slightly increase in the remaining years from its prior forecast, and grow by 6.0% in FY 2023 and 4.0% for FY 2024-2027.

The Council acknowledged significant uncertainty surrounding the forecasted figures for FY 2021 and FY 2022. The Council emphasized that their forecast was based on existing tax law and does not account for tax law changes that may arise from the conformity to the Federal tax code. Certain of those Federal tax law changes are significant.

The Council's FY 2021 forecast considered the fiscal impacts of the delay in the income tax filing deadline for tax year 2019 from April to July 2020, which resulted in a shift of \$308 million from FY 2020 to FY 2021. The Council acknowledged that economic activity had rebounded more than expected in the latter part of calendar year 2020 with the opening of tourism under the Safe Travels program. In November and December, tourism appeared to average roughly 25% of the pre-pandemic averages.

Members acknowledged that the COVID-19 pandemic continued to represent a serious risk to public health and the State's economy. Future tax revenues are highly dependent on the trajectory of the virus and the government's ability to simultaneously manage public health risks and economic activity.

The Council expressed concerns about the prolonged restrictions imposed on the Hawaii tourism economy and the potential effects of future shutdowns of non-essential businesses due to spikes in the COVID-19 infection rates. In addition, the Council discussed the impacts on the local economy of the Federal fiscal stimulus packaged that passed in December 2020 and the likelihood of additional Federal stimulus.

There are a number of unknowns that may significantly affect Hawaii's economic activity and State tax collections such as the trajectory of the virus, the availability of an effective vaccine and its distribution, rapid low-cost testing, the State, County and Federal government's response to the pandemic, travel restrictions, and the threat of new shutdowns. The Council noted that the State government's role in facilitating visitor arrivals in a safe and orderly manner is vital for the return of economic growth.

In discussing the economy, the Council also noted that certain local Hawaii businesses were severely affected or were forced to close due to the pandemic and restrictions on operations while other businesses appeared to be doing well. Similarly, certain individuals working in tourism-related industries, restaurants, and smaller retail shops were disproportionately negatively affected by the pandemic compared to others in Hawaii.

The new forecasts for the State General Fund tax revenues FY 2021 through FY 2027 are shown in the table below.

General Fund Tax Revenues

Fiscal Year	Amount (in Thousands of Dollars)	Growth From Previous Year
2021	\$6,259,645	-6.5%
2022	\$6,635,223	6.0%
2023	\$7,033,337	6.0%
2024	\$7,314,670	4.0%
2025	\$7,607,257	4.0%
2026	\$7,911,547	4.0%
2027	\$8,228,009	4.0%

The Council adopted specific adjustments recommended by the Department of Taxation to reflect effects on General Fund tax revenues due to tax law changes enacted by the Legislature. No laws were enacted that had significant impact on General Fund forecasts in 2020. However, laws from previous legislative sessions were considered including the following:

- Act 2, SLH 2019 deems marketplace facilitators the sellers of tangible personal property, intangible personal property, and services sold through the marketplace. The Act also deems sales of tangible personal property and services by sellers to the marketplace facilitator to be sales at wholesale. The Act is effective January 1, 2020. The estimated gain to the General Fund is \$4.0 million in FY2020, \$9.8 million in FY 2021, \$10.1 million in FY 2022, \$10.4 million in FY 2023, \$10.7 million in FY 2024, \$11.0 million in FY 2025, and \$11.3 million in FY 2026.
- Act 3, SLH 2019 establishes a new estate tax rate bracket for taxable estates exceeding \$10 million. The new bracket is 20%. The Act is effective April 4, 2019 and applies to decedents dying after December 31, 2019. The estimated gain to the General Fund is \$1.9 million in FY 2021, \$2.0 million in FY 2022, \$2.1 million in FY 2023, \$2.2 million in FY 2024, \$2.3 million in FY 2025, and \$2.4 million in FY 2026.
- Act 20, SLH 2019 imposes the transient accommodations tax on resort fees and defines resort fees as "any mandatory charge or surcharge imposed by an operator, owner, or representative thereof to a transient for the use of the transient accommodation's property, services, or amenities." The Act is effective July 1, 2019. The estimated revenue gain to the General Fund is \$9.1 million in FY 2020, \$10.3 million in FY 2021, \$10.7 million in FY 2022, \$11.1 million in FY 2023, \$11.6 million in FY 2024, \$12 million in FY 2025, and \$12.4 million in FY 2026.
- Act 260, SLH 2019 establishes a new ship repair industry tax credit which is intended to offset costs incurred in constructing and placing into service a purpose-built floating dry dock at Pearl Harbor for use by the United States Navy. The tax credit expires December 31, 2026. The Act also repeals the capital infrastructure tax credit. The Act is effective January 1, 2020 and applies to taxable years beginning after December 31, 2021. The expected net loss to the General Fund is \$6.0 million per year in FY 2023 to FY 2026.
- Act 261, SLH 2019 amends the tax credit for research activities such that references to the base amount contained in section 41 of the IRC do not apply, and credit may be taken based upon all qualified research expenses incurred in Hawaii without regard to the amount of expenses for previous years. The Act establishes an annual aggregate cap of \$5 million. The Act extends the tax credit from tax year 2020 through tax year 2024. The expected loss to the General Fund is \$5.0 million per year for FY 2021 to FY 2025.
- Act 275, SLH 2019 amends the motion picture, digital media, and film production income tax credit by increasing the credit annual aggregate cap from \$35 million to \$50 million. The Act is effective July 10, 2019 and applies to taxable years beginning after December 31, 2018. The tax credit expires December 31, 2025. The

expected loss to the General Fund is \$15.0 million per year for FY 2020 to FY 2026.

- Act 27, SLH 2018 selectively conforms Hawaii income tax laws and estate tax laws to the Internal Revenue Code as of February 9, 2018, and as of December 31, 2017, respectively. The Act is effective June 7, 2018 and applies to taxable years beginning and to decedents dying after December 31, 2017. The estimated gain to the General Fund is estimated to be \$9.2 million in FY 2019, \$14.2 million in FY 2020, \$20.1 million in FY 2021, \$26.9 million in FY 2022, \$34.9 million in FY 2023, \$37.9 million in FY 2024, and \$37.1 million in FY 2025.
- Act 39, SLH 2018 increases the aggregate amount of the GET cost exemption for developing affordable rental housing from \$7 million to \$30 million per year. Extends the exemption from June 30, 2022, to June 30, 2030. The Act is effective July 1, 2018 and applies retroactively to taxable years beginning after December 31, 2017. The estimated loss to the General Fund is estimated to be \$23.0 million in FY 2019, \$23.0 million in FY 2020, \$23.0 million in FY 2021, \$23.0 million in FY 2022, \$30.0 million in FY 2023, \$30.0 million in FY 2024, and \$30.0 million in FY 2025.
- Act 41, SLH 2018 provides that a person is engaging in business in the State for the purpose of the general excise tax law if, in the current or immediately preceding calendar year, the person has \$100,000 or more in gross income, or two hundred or more separate transactions, from the sale of tangible personal property delivered in the State, services used or consumed in the State, or intangible property used in the State. The Act is effective July 1, 2018 and applies to taxable years beginning after December 31, 2017. The estimated gain to the General Fund is estimated to be \$6.8 million in FY 2019, \$7.6 million in FY 2020, \$7.9 million in FY 2021, \$8.1 million in FY 2022, \$8.3 million in FY 2023, \$8.6 million in FY 2024, and \$8.9 million in FY 2025.
- Act 86, SLH 2018 reduces the allocations of TAT to the Convention Center Special Fund from \$26.5 million to \$16.5 million and the Tourism Special Fund from \$82 million to \$79 million. The Act is effective July 1, 2018. The estimated revenue gain to the General Fund is \$13 million per year from FY 2019 to FY 2025.
- Act 122, SLH 2018 increases the withholding on the amount realized from the disposition of Hawaii real property by nonresidents (HARPTA) from 5% to 7.25%. The Act is effective July 5, 2018 and applies to real estate dispositions that occur on or after September 15, 2018. The expected revenue gain is \$8.1 million in FY 2019 and \$2.6 million per year from FY 2020 to FY 2025.

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- Act 211, SLH 2018 imposes the TAT on transient accommodations brokers, travel agencies, and tour packages that enter into arrangements to furnish transient accommodations at noncommissioned negotiated contract rates on their share of the proceeds. The Act is effective July 1, 2018 and applies to taxable years beginning after December 31, 2018. The expected revenue gain to the General Fund is \$14.7 million in FY 2019, \$36.6 million in FY 2020, \$38.0 million in FY 2021, \$39.3 million in FY 2022, \$40.6 million in FY 2023, \$42 million in FY 2024, and \$45.6 million in FY 2025.

The Department of Taxation has prepared a report (attached) detailing line-item forecasts for various components of the General Fund, reconciled to the Council's forecast growth rate for total General Fund tax revenues. The line-item forecasts include components, such as revenues from the General Excise Tax and from the Individual Income Tax that the Council does not forecast separately. Also, the Department of Budget and Finance has prepared the attached report to update its projections for change in non-tax and special tax revenues from its September 2020 report.

Please advise us if we can be of further assistance or if we can answer any questions.

Very truly yours,



KURT KAWAFUCHI
Chair, Council on Revenues

Attachments