COUNCIL ON REVENUES

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

April 8, 2011

The Honorable Neil Abercrombie
Governor, State of Hawaii
Executive Chambers
State Capitol, Fifth Floor
Honolulu, HI 96813

Dear Governor Abercrombie:

At a special meeting on March 29, 2011 the Council on Revenues lowered its forecast for State General Fund tax revenue growth in fiscal year (FY) 2011 from 0.5 percent to –1.6 percent. Forecast growth rates for FY 2012 through FY 2017 remained the same as before.

Your request for this previously unscheduled meeting indicated specific interest in Hawaii State revenue impacts of three things: (1) the March 11, 2011 Sendai, Japan seismic event; (2) reduced federal “earmarked” expenditure; and (3) global petroleum price movements attributable to political upheaval in North Africa and the Middle East.

The Hawaii Department of Budget and Finance (B&F) was unable to provide additional insight regarding nearly $7 billion in annual general fund non-tax, special and other funds’ revenues in response to your questions, in the time elapsed since the March 10, 2011 Council on Revenues meeting. The Council neither entertained a motion to accept such information as is customarily reported to it by B&F, nor contemplated, in that report’s absence, impacts of those events on State revenues *other than* the $4-5 billion in General Fund, fiscal year tax revenues.

One of the three external factors for which you specifically requested consideration—recent geopolitical influences on global petroleum prices—already received consideration at the March 10, 2011 Council on Revenues meeting.

At the Chair’s request the Research and Economic Analysis Division of the Hawaii Department of Business, Economic Development and Tourism (DBEDT) submitted for distribution to Council members a spreadsheet estimating line-item, federal expenditure earmarks associated with Hawaii (or, perhaps, only with Hawaii’s Congressional delegation). The source of the data was the web site of a not-for-profit tax policy advocacy group. No timetable was associated with identified earmark expenditure reductions. The presumption that only private economic activity, and not public activity, was at risk could not be verified.

(Federal budget deficit reduction is already assumed in some members' economic forecast assumptions.) No insight was available, from the source, DBEDT, or Council members' inspection of the data, as to whether earmark-funded activities at risk were already being funded or simply were anticipating funding. Council members expressed an interest in acquiring more information associated with federal spending earmark changes of a material, economy-wide, macrodynamic character, if and when such information becomes available, but no forecast revisions could be associated with this information at the March 29 meeting.

With respect to the Sendai seismic event, five out of seven Council members *revised* their macroeconomic assumptions, five days before the March 29 meeting, from those prepared for the March 10 meeting. Two of those five—one of whom also prepared an independent macroeconometric State General Fund revenue forecast—assumed that Japanese visitor arrivals would decline in a range of 40-50 percent during the first quarter after the Sendai seismic event. They assumed that Japanese travel and tourism would converge gradually over the next several quarters to approximate the pre-Sendai arrivals benchmark within 4-5 quarters of total duration. A sixth member who did *not* submit revisions to macroeconomic assumptions for the March 29 meeting also prepared an independent revenue forecast based on a special enumeration of daily Japanese passenger arrivals from Friday, March 11 through Monday, March 28 made available by DBEDT the evening before the Council meeting. This sixth, individual forecast calibrated the initial visitor loss to the 25 percent reduction in passenger arrivals extant, converging to pre-Sendai volumes over the subsequent year. The various, possibly premature, estimates of Japanese tourism losses associated with the Sendai event framed small, potential, downward revisions to the earlier, pre-Sendai, March 10 revenue forecast estimates.[1] Sendai conjectures had impacts concentrated in the final quarter of the current fiscal year, but for technical reasons the uncertainties associated with the potential magnitudes of a revenue forecast revision outweighed the numerical adjustments to the forecast that could be attributed to a Sendai effect. Members expressed concern that outcomes of Fukushima nuclear power facility damage remained especially uncertain.

To this subject of uncertainty B&F *did* contribute insight at the Council meeting. Utilizing February tax revenue data that was not available at the time of the March 10 meeting, but became available in the interim prior to the March 29 special meeting, B&F conjectured that the March 10 forecast was implausibly high, based on certain assumptions associated with last fiscal year's refund delays. Largely as a consequence of the inference that the now-known February revenue results should *not* be interpreted as anomalous, but rather as reflecting a loss of economic recovery momentum, when combined with post-Sendai considerations the fiscal year 2011 General Fund revenue growth forecast was revised to −1.6 percent and a motion was adopted to adjust out-year revenue estimates accordingly.

Revised forecasts of State General Fund tax revenues for FY2011 through FY2017 are shown in the table below:

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[1] Because of the International Date Line, the March 10, 2011 Council on Revenues meeting occurred only hours before the March 11, 2011 Sendai, Japan earthquake and tsunami. Japanese passengers arriving in Honolulu the morning of March 11, 2011 (Hawaii time) may have been affected by the seismic event the same day (in Japan).

Fiscal Year	General Fund Tax Revenues Amount (in Thousands of Dollars)	Growth From Previous Year
2011	4,294,726	–1.6%
2012	4,767,146	11.0%
2013	5,053,175	6.0%
2014	5,356,366	6.0%
2015	5,677,748	6.0%
2016	6,018,413	6.0%
2017	6,379,518	6.0%

The Council Chair anticipated that the Department of Taxation, separately, would prepare a report for submission with this transmittal correspondence, detailing line-item forecasts for various components of the General Fund, reconciled to the growth rate for total General Fund Tax Revenues. These line-item component estimates typically include, for example, General Excise Tax and Income Tax revenues that the Council on Revenues does not forecast individually.

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

Sincerely,

Paul H. Brewbaker

PAUL H. BREWBAKER, Ph. D.
Chair, Council on Revenues

Attachment

GENERAL FUND TAX REVENUE: FY 2011 to FY 2017

Line-item projections generated by DOTAX, TRP consistent with COR total growth rate forecasts

(in thousands of dollars)

	BASE		ESTIMATE						
TYPE OF TAX	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017
General Excise & Use 2/ 7/ 12/	$2,417,580	$2,316,434	$2,424,512	$2,590,161	$2,770,545	$2,966,538	$3,173,832	$3,446,798	$3,701,594
Income - Individual 4/ 6/ 8/ 11/	1,338,451	1,527,619	1,224,381	1,486,882	1,571,396	1,661,884	1,749,492	1,875,537	1,967,890
Income - Corporation 6/ 11/	53,522	59,186	50,948	51,369	54,002	62,828	70,558	76,485	80,454
Public Service Company	126,069	157,661	184,395	208,207	229,718	249,458	267,857	286,469	305,091
Insurance Premiums 6/ 7/	93,720	104,721	130,523	125,752	132,701	139,011	142,227	145,474	147,503
Tobacco & Licenses 5/ 7/ 13/	76,955	85,503	103,694	102,318	92,004	67,598	58,608	51,584	44,933
Liquor & Permits 7/	47,242	44,074	42,662	39,491	37,578	35,888	34,441	33,201	32,159
Banks & Other Fin Corps	26,075	18,666	19,172	22,742	25,944	28,442	30,259	33,671	36,531
Inheritance & Estate 10/	274	0	8,200	19,600	19,600	19,600	19,600	19,600	19,600
Conveyance 3/	8,311	18,216	21,833	21,622	15,405	15,155	14,918	14,694	14,484
Miscellaneous 9/	536	781	13,985	13,972	13,959	13,947	13,936	726	717
Transient Accommodation Tax 1/ 7/	13,566	31,698	70,421	85,030	90,323	96,017	102,020	34,174	28,562
NET TOTAL	$4,202,301	$4,364,559	$4,294,726	$4,767,146	$5,053,175	$5,356,366	$5,677,748	$6,018,413	$6,379,518
GROWTH RATE (COR FORECAST)	-9.5%	3.9%	-1.6%	11.0%	6.0%	6.0%	6.0%	6.0%	6.0%

Notes:

1/ Deposits of 44.8% of TAT revenues to counties (Act 156, SLH 1998); 32.6% to the tourism special fund and 5.3% to the TAT trust fund (Act 250, SLH 2002); 17.3% to the convention center enterprise fund (Act 253, SLH 2002); all net of general fund deposits of excess of fund ceilings. Act 235, SLH 2005, increases allocation to the tourism special fund to 34.2% and repeals the TAT trust fund. Effective on July 1, 2007. Act 209, SLH 2006, increases ceiling on allocation to the convention center enterprise fund to $33 million. Effective on July 1, 2006. Act 61, SLH 2009, temporarily imposes an additional 1.0% TAT for the period 7/1/2009 through 6/30/2010, and an additional 2.0% TAT for the period 7/1/2010 through 6/30/15. These additional amounts will be deposited into the general fund. Act 5, Special Session Laws of Hawaii 2009, allocates 12.5% of the revenues derived from Act 61 to the tourism special fund for one fiscal year (FY 2011).

2/ Act 209, SLH 2007, exempts gross income received from the sale of alcohol fuel from the general excise tax. Effective on July 1, 2007, provided that the exemption repeals on June 30, 2009. Act 40, SLH 2009, reduces the interest rate on overpayments due to taxpayers from 2/3 of 1% to 1/3 of 1% per month or fraction thereof.

3/ Due to the expiration of Act 222, SLH 2007, on June 30, 2008, the amount of conveyance tax deposited into the General Fund increased from 15% to 35%. Act 59, SLH 2009, increased the conveyance tax rates for properties valued $1 million or more.

4/ Act 60, SLH 2009, temporarily increases the standard deduction and personal exemption amounts for taxable years beginning after 12/31/10, and also temporarily creates new 9%, 10%, and 11% tax brackets for certain individuals with high taxable income beginning with taxable years beginning after 12/31/08. Act 60, SLH 2009, will be automatically repealed on December 31, 2015.

5/ Act 58, SLH 2009, taxes "little cigars" in the same manner as cigarettes beginning 9/30/09; increases the tax on tobacco products other than cigarettes, little cigars, and cigars from 40% to 70% beginning 9/30/09; imposes a 50% tax on cigars. Act 56, SLH 2009, increases the cigarette tax from 11¢ to 13¢ on 7/1/09, from 12¢ to 14¢ on 7/1/10, and from 13¢ to 15¢ on 7/1/11; and also amends the dates on which changes in the allocation of cigarette tax revenues changes. Act 59, SLH 2010, increases the tax on cigarettes and little cigars by 1¢ for sale after June 30, 2010. The additional collections will be deposited into the general fund.

6/ Act 21, SLH 2010, provides for the statutory ordering of income tax credits, which requires the claiming of refundable credits first, followed by nonrefundable credits. Applies to taxable years beginning after 12/31/09.

7/ Act 22, SLH 2010, amends the due dates for miscellaneous tax types from the last day of the calendar month to the 20th day of the calendar month, and amends the due date for filing and payment of periodic insurance premiums taxes from quarterly to monthly. Effective on July 1, 2010.

8/ Act 59, SLH 2010, repeals the deduction from taxable income for amounts given as political contributions. Effective on January 1, 2011.

9/ Act 73, SLH 2010, temporarily increases environmental response tax from $0.05/barrel to $1.05/barrel for the period 7/1/2010 through 6/30/2015. Sixty cents of the tax collected per barrel will be deposited into the general

10/ Act 74, SLH 2010, retains the State's ability to "pick-up" the state death tax credit as it existed in the Internal Revenue Code on 12/31/2009. Applies to property interests of persons who die after 4/30/10.

11/ Delay in paying out Tax Year 2009 income tax refunds

12/ Act 155, SLH 2010, precludes taxpayers from using a general excise tax benefit, including exemptions, deductions, lower rates, or income splitting, unless the taxpayers follow all administrative requirements, subject to exemptions. The Act also creates trust liability for revenues collected by a business as a tax recovery whether such amount is separately stated or not. Effective on July 1, 2010.

13/ Act 192, SLH 2010, amends the disposition of revenues collected pursuant to tobacco tax law. Effective on July 1, 2010.