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COUNCIL ON REVENUES

STATE OF HAWAII
P.O. BOX 259
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June 2, 2014

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

Dear Governor Abercrombie:

At its meeting on May 29, 2014, the Council on Revenues lowered its forecast for growth in State General Fund tax revenues in fiscal year (FY) 2014 from 0.0% to -0.4%.

The Council was concerned that the cumulative general fund tax revenue collections so far this fiscal year were lower than expected. In particular, the general fund revenue through the end of April 2014 declined by 1.0% and Hawaii general excise tax (GET) collections through the same period declined by 2.0% (before allocating the $55.5 million to the Hurricane Relief Fund). Part of the reason for the decline in GET revenues this year is that processing delays caused some City and County of Honolulu surcharge payments from liabilities incurred in the latter months of FY 2013 to be paid out in the first month of FY 2014.

The Council thought that the shortfall in tax revenues was due to a number of factors, including declining visitor spending and the effects of federal fiscal austerity on spending by residents. In addition, anticipated increases in federal income tax rates after 2012 may have caused taxpayers to recognize capital gain income in 2012 and to move income forward from tax year 2013 into tax year 2012. This would have caused tax collections to increase in FY 2013 and would have adversely affected collections in FY 2014. Also, replenishing the Hawaii Hurricane Relief Fund reduced general fund tax revenues by about 1% in FY 2014 and will do so again in FY 2015. The members also noted that real U.S. GDP fell at an annual rate of 1% in the first quarter of 2014.

The Council maintained its March 11, 2014 forecasts for FY 2015 through FY 2020, since it remained optimistic about the economy in coming years due to the amount of anticipated construction activity. Although the Council believed that the economy is still growing, and cited an expected increase in visitor arrivals due to additional airline seats and a number of major construction projects, the members expressed much uncertainty about the economy.

Revised forecasts of State General Fund tax revenues for FY 2014 through FY 2020 are shown in the table below. As in all multi-year forecasts, the estimates for the later years are subject to greater uncertainty.

Fiscal Year	General Fund Tax Revenues Amount (in Thousands of Dollars)	Growth From Previous Year
2014	5,445,055	- 0.4%
2015	5,744,533	5.5%
2016	6,031,760	5.0%
2017	6,381,602	5.8%
2018	6,777,261	6.2%
2019	7,143,233	5.4%
2020	7,528,968	5.4%

In producing its forecasts, the Council adopted specific adjustments recommended by the Department of Taxation to reflect effects on General Fund tax revenues of tax law changes enacted by the 2013 Legislature, including the following:

- 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, 2016 to January 1, 2019. The Act is estimated to raise the annual cost of the tax credit by about $21 million over the level in FY 2013.

- Act 160 eliminates the General Excise Tax (GET) exemption for liquor, tobacco and food sold to common carriers. The Act is estimated to raise GET collections by about $6 million per year.

- Act 161 makes permanent the Transient Accommodations Tax (TAT) rate of 9.25% and the caps on TAT allocations to the special funds. The Act raises the cap on the allocation to the Tourism Special Fund by $11 million. Act 161 is estimated to reduce General Fund revenues by $11 million in FY 2014 and FY 2015, but is expected to increase General Fund revenues by amounts ranging from $177 million in FY 2016 to $246 million in FY 2020.

- 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 claimed. The Act is estimated to reduce GET collections by about $20 million in FY 2014 and by about $13 million annually thereafter.

The Council also took into account provisions from earlier legislation, including the following:

- Act 105, SLH 2011, eliminated certain GET exemptions. The Act expired June 30, 2013. Its expiration is estimated to reduce GET collections by about $70 million annually relative to the level in FY 2013.

- Act 62, SLH 2011, allocates GET revenues directly to the Hurricane Relief Fund to replace amounts that were taken from the Fund in prior years. The Act will reduce GET allocations to the General Fund by $55.5 million in each of FY 2014 and FY 2015.

The Department of Taxation has prepared a report for submission with this transmittal correspondence, 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 report on March 11, 2014.

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

Very truly yours,

Marilyn M. Niwao

MARILYN M. NIWAO, J.D., CPA
Vice-Chair, Council on Revenues

Attachments