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COUNCIL ON REVENUES

STATE OF HAWAII
P.O. BOX 259
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March 15, 2018

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

Dear Governor Ige:

At its meeting on March 13, 2018, the Council on Revenues (the "Council") raised its fiscal year (FY) 2018 revenue forecast for the General Fund from 4.5% to 5.3%. This was due in part to a greater than expected increase in General Fund revenue collections for the first eight months of FY 2018. Higher General Fund revenue collections appear to have resulted from robust economic activity and the stimulus effects of the Tax Cuts and Jobs Act passed in December 2017. The Council also raised its growth forecast from 4.3% to 4.5% in FY 2019 but left FY 2020 to FY 2024 forecasts unchanged at 4.0%.

Members expressed concern, however, about the amount of economic and political volatility as well as evidence of stagnant personal income growth. In addition, concern was expressed that part of the growth rate increase was likely due to higher prepayment of estimated state income taxes due to the 2018 Federal limitations on State and Local Tax ("SALT") deductions and possible prepayments of certain itemized deductions due to other changes in Federal tax laws.

The Council discussed the state of the economy for the rest of FY 2018. Their consensus was that the economy is performing well in FY 2018 and will likely continue to do so into FY 2019, but the economic conditions in the out years remain uncertain. Growing visitor arrivals, a strong national economy, and the tax cuts associated with the Tax Cuts and Jobs Act are contributing to a stronger economy. Concerns were expressed that the economy may be nearing the end of its current expansionary cycle during the seven-year budget window. The increased chance of an economic downturn is reflected in the lower growth numbers for FY 2020 to FY 2024. The Council noted the re-adoption of higher income tax rates for the top income brackets of individual taxpayers, which increased taxes from 8.25% to 11%, should also boost revenue in FY 2019.

The new forecasts of State General Fund tax revenues for FY 2018 through FY 2024 are shown in the table below.

General Fund Tax Revenues

Fiscal Year	Amount (in Thousands of Dollars)	Growth From Previous Year
2018	$6,649,921	5.3%
2019	$6,949,167	4.5%
2020	$7,227,134	4.0%
2021	$7,516,219	4.0%
2022	$7,816,868	4.0%
2023	$8,129,543	4.0%
2024	$8,454,725	4.0%

- Act 107, SLH 2017 reinstates three tax rates and brackets (9.0%, 10.0%, and 11.0%) for the highest-income taxpayers imposed by Act 60, SLH 2009, for taxable years beginning after December 31, 2017. The estimated gain to the General Fund is estimated to be $50.7 million in FY 2019, $53.3 million in FY 2020, $55.9 million in FY 2021, $58.7 million in FY 2022, $61.6 million in FY 2023, and $64.7 in FY 2024.

- Act 107, SLH 2017 establishes a nonrefundable earned income tax credit (EITC) equal to 20 percent of the federal EITC. The tax credit applies to tax years 2018 through 2022. The estimated loss to the General Fund is estimated to be $16.7 million in FY 2019, $20.4 million in FY 2020, $23.8 million in FY 2021, $27.1 million in FY 2022, $30.1 million in FY 2023, and $0.0 in FY 2024.

- Act 107, SLH 2017 repeals the sunset date (December 31, 2017) for the amendments to the refundable food/excise tax credit by Act 223, SLH 2015. The estimated loss to the General Fund is estimated to be $6.5 million per year from FY 2019 to FY 2024.

- Act 143, SLH 2017 amends the motion picture, digital media, and film production tax credit by limiting total amount of credit to $35 million/year and extending the credit to January 1, 2026. Total tax credits claimed per qualified production shall not exceed $15 million. The estimated revenue loss to the General Fund is $35 million from FY 2020 to FY 2024.

- Act 54, SLH 2017 exempts certain affordable rental housing projects from the general excise and use tax. The legislation limits total amount of exemptions to $7 million/year starting July 1, 2017 through June 20, 2022. The expected revenue loss is $7 million in FY 2019-2022.

- Act 1, SLH 2017 increases the TAT rate from 9.25% to 10.25%, effective January 1, 2018 through December 31, 2030, and allocates the tax revenue generated from the increase to the Mass Transit Special Fund. The Act also increases the annual allocation to the counties from $93 million to $103 million, beginning in FY 2018. The expected revenue loss to the General Fund is $10 million from FY 2018 to FY 2024.

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

- Acts 117 and 121, SLH 2015 changed allocations of the TAT. According to Act 121, TAT allocations for FY 2016 and later are as follows: Tourism special fund $82 million; Counties $93 million (except $103 million in FY 2016 and FY 2017); Convention Center special fund $26.5 million; and Turtle Bay conservation easement $1.5 million. Act 117 allocated $3 million annually to the Special Land Development fund starting in FY 2017. The changes in allocations are expected to yield $2 million in additional General Fund tax revenues in FY 2017 and thereafter. Note that Act 107, SLH 2017 directs $103 million from FY 2018 and beyond.

- Act 120, SLH 2015 provides a tax credit for converting cesspools to a septic system or connecting to a wastewater system. The tax credit expires December 31, 2020 and is estimated to reduce General Fund tax revenues by $5 million annually from FY 2017 through FY 2021.

- Act 223, SLH 2015 modifies the food/excise tax credit (an increase for certain taxpayers) for tax years 2016 and 2017. The Act is estimated to reduce General Fund tax revenues by $6.5 million in FY 2017 and in FY 2018.

- Act 89, SLH 2013 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.

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 report on January 8, 2018.

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