

COUNCIL ON REVENUES

Meeting Minutes, Thursday, January 9, 2020 (2pm)

Tax Conference Room
Princess Ruth Keelikolani Building
830 Punchbowl Street, Second Floor
Room 223
Honolulu, Hawaii 96813

Thursday, January 9, 2020
2:00 p.m.

PRESENT:

Council Members:

Kurt Kawafuchi (Chair), Marilyn M. Niwao (Vice-Chair), Carl S. Bonham,
Jack Suyderhoud, Kristi L. Maynard, Jessica Gluck, Scott Hayashi

Staff Members:

Department of Taxation (DOTAX): Seth Colby, Baybars Karacaovali,

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

Others:

Rona M. Suzuki, Director of Taxation
Neal Miyahira, Budget of Finance
John Roberts, Hawaii Association of Public Accountants

CALL TO ORDER:

Chair Kawafuchi called the meeting to order at 2:00 p.m. A quorum was present.

COMMUNICATIONS TO THE COUNCIL AND PUBLIC COMMENT:

There was no communication to the Council and there was no public comment.

APPROVED MINUTES OF THE MEETING OF NOVEMBER 1, 2018:

Chair Kawafuchi asked if there was any discussion on any item in the minutes. There were none mentioned. Chair Kawafuchi called for a motion to approve the minutes for the meeting of October 31, 2019.

It was moved by Dr. Suyderhoud and seconded by Ms. Maynard that the minutes of the October 31st meeting be approved. The Chair called for the vote, and the motion passed with the following votes:

Kurt Kawafuchi	Yes
Marilyn Niwao	Yes
Jack P. Suyderhoud	Yes
Carl S. Bonham	Yes
Jessica Gluck	Yes
Kristi L. Maynard	Yes
Scott Hayashi	Yes

GENERAL FUND REVENUE FORECAST FOR FISCAL YEAR 2020:

Dr. Colby from the Department of Taxation presented results of the Preliminary Comparative Report for December 2019, which had not yet been released. General Fund revenues were up 6.1% for the first half of fiscal year (FY) 2020. Dr. Colby highlighted notable trends in the report, including the fact that declared estimated taxes for individual income tax payments were up 27% compared to the last fiscal year, and payments with returns were up 29%.

Dr. Colby noted that the increase in taxes was due to the rate increase on high income earners that went into effect January 1, 2018. This is because these taxpayers finally understood their new tax liability as a result of the rate increase when they filed their 2018 tax return in April 2019. These taxpayers have adjusted to the higher liability and now filing higher estimated taxes. The other issue that may be contributing to the bump is increased dividend payments due the repatriation of foreign earnings that were caused by the Tax Cut and Jobs Act passed in 2017.

The other unexpected result was larger than expected collections from the Insurance Premium Tax. This tax is not collected by the Department of Taxation, and he did not understand what happened to the tax. Dr. Colby noted that this tax is often lumpy in terms of collections.

Dr. Bonham noted that the General Excise Tax (GET) collections came in at 3.3%, which is within the expected range given the underlying economy of the State. He also noted that distributed corporate earnings would have come in the form of dividends and stock buybacks. The dividend component in 2018 Hawaii Total Personal Income grew by 6%, and thus far it has grown less in 2019, around half as much. Ms. Niwao mentioned that increase in dividends could be related to the conversion of A&B (Alexander & Baldwin) from a corporation to a REIT (Real Estate Investment Trust). Dr. Bonham said that corporations are normally reluctant to reduce dividends. Chairman Kawafuchi said that this dividend repayment is more likely to be a one-time event because corporations were incentivized to repatriate corporate earnings due to the 2017 federal tax law changes. Ms. Niwao said that as of 2019, one trillion dollars of foreign earning have been repatriated to the United States.

Dr. Suyderhoud noted that withholding taxes on wages was up 5%. Ms. Niwao noted that fewer people prepaid their state income taxes prior to the end of the calendar year 2018 since the 2017 federal tax law capped the State and Local Tax deduction, which lowered the incentive for early prepayment. Instead, these taxpayers paid according to the normal schedule or when they filed their 2018 tax return, which resulted in a big increase in collections in April 2019. People are

now paying their taxes throughout the year via declared estimated taxes, and thus it is unlikely that there will be the same spike in April 2020 that was seen in April 2019. This implies that the revenue numbers for individual income tax are shifted forward compared to last year, and the fiscal year-end of individual income tax collections will likely be lower.

Dr. Bonham noted that the 4.8% in withholding taxes seems high given the low levels of Total Personal Income growth and job growth that Hawaii has seen lately. Ms. Niwao mentioned that you could increase withholding instead of declared estimated taxes.

AT 2:16 PM THE FIRE ALARM WENT OFF IN THE BUILDING. THE COUNCIL TOOK A TEMPORARY RECESS WHILE THE MEMBERS EVACUATED THE PREMISES ALONG WITH OTHER PERSONNEL. THE COUNCIL MEETING WAS RECONVENED AT 2:51 PM.

Dr. Suyderhoud said that the 3.3% increase in GET and the 4.8% increase in withholding taxes is consistent with the Council's FY 2020 forecast of 4.1%. In spite of a spike in estimated tax payments and TAT, which he finds surprisingly high, he is comfortable with something like 4.0%.

It was moved by Dr. Suyderhoud that the General Fund tax revenues growth rate would remain at 4.1% for FY 2020. Ms. Maynard seconded. The Chair called for the vote, and the motion passed with the following votes:

Kurt Kawafuchi	Yes
Marilyn Niwao	Yes
Jack P. Suyderhoud	Yes
Carl S. Bonham	Yes
Jessica Gluck	Yes
Kristi L. Maynard	Yes
Scott Hayashi	Yes

GENERAL FUND REVENUE FORECAST FOR FISCAL YEARS 2021 THROUGH 2026:

Next, the Council discussed the General Fund revenue forecast for fiscal years 2021 through 2026.

Dr. Suyderhoud noted that the Council is on record for 3.0% for FY 2021 and 2022 and 4.0% for FY 2023 to 2026.

Ms. Niwao asked if there would be a downturn after the election. Dr. Suyderhoud said that sometime in the future there would be a downturn, and sometime in the future growth would surpass the Council's forecast.

Ms. Maynard asked Dr. Bonham if the economy has turned a corner. Dr. Bonham responded that UHERO revised the outlook for 2019 slightly up. They believe that 2018 represented the low point for economic growth until the next recession comes. They believe that 2020 will be better because the global economy is a little better due to Fed easing and reduced tensions in the trade war between the US and China. They do not think the dollar will continue to strengthen.

In addition, it seems that the Oahu Ordinance's increasing enforcement capacity on transient vacation rentals (TVR) is not having a drastic effect on the listing of TVRs. In fact, the number of listings at the state level are up compared to the same time last year. In Oahu, the number of listings declined 30% after the ordinance passed in August 2019, but the number has started to creep back up since then. The ordinance is not having the economic drag on the economy that was expected. They expect a 1.5% increase in visitor plant in 2020, which is higher than expected. The air seat numbers are increasing substantially, partly due to the Southwest's entrance into the market and Japanese airlines switching to larger capacity airplanes. They believe real visitor spending will continue to decline, and nominal real visitor spending will stay flat.

UHERO forecasted that population growth would decline by 0.1%. They believe that the population will not rebound until the mainland economy cools down. They believe that Hawaii residents are leaving for the mainland to take better professional opportunities. Even when the mainland economy cools, UHERO expects population growth to be low, in the range of 0.2% or 0.3%.

Chairman Kawafuchi asked about construction. Dr. Bonham said that in contrast to the state economist, UHERO believes the outlook for construction to be positive, better than in 2019. They acknowledge that the permitting data was terrible, but a lot of that came from government. From talking with contractors, developers, and other people in the industry, they are all extremely busy developing new projects. They do not expect a boom, but they expect solid performance for the next several years. Dr. Bonham noted that a number of large government projects are in the pipeline like the Blaisdell, the stadium, and the new prison. He does not believe the construction sector will be a big boon or a big drag for the state economy. He believes if Hawaii has just a little bit of job growth and a little bit of income growth, the economy will out perform relative to the previous year.

Ms. Niwao expressed concern about the retail sector. Dr. Bonham countered that the drag in the retail sector has been a trend for several years. Ms. Niwao expressed concern about the cost of living in Hawaii, which prompts people to move to the mainland. Another concern of Ms. Niwao's is that Hawaii is not collecting taxes from wealthy part-time residents. The wealthy residents often opt to declare residency in another state due to the perceived tax burden in Hawaii relative to other states. Ms. Niwao says that the estate tax in Hawaii is dissuading people from declaring residency in the state.

Ms. Maynard noted that the slow permitting process in the construction sector is dragging down the sector. Dr. Bonham said that UHERO had done some research on this topic and found that the delays in permitting have increased over the last five years, and he agrees that is a big problem. Mr. Hayashi noted that the City of Honolulu brought back the informal review process, which helps speed up permitting. Dr. Bonham acknowledged that bringing back this process will help, but it will not solve the problem. There was a recent audit on Honolulu's Department of Permitting and Planning, and it found that there were large deficiencies in capacity and execution. Mr. Hayashi said his clients in the construction sector remain bullish about the future.

Ms. Maynard asked if there was any reason to change the current forecast of 3.0%, 3.0%, 4.0%, 4.0%, 4.0%. Dr. Bonham said that the current forecast implied a downturn in the two years. He suggested that it may be prudent to push back that downturn further into the future given the

relatively positive outlook in the calendar year 2020. Ms. Maynard suggested that they could adjust the forecast to 4.0% and then 3.0%. Ms. Gluck noted that this approach would more closely reflect the models produced by Tax Department which were made using the members' forecasts. Dr. Bonham noted that there was more pessimism when they made that forecast nine months ago, citing examples like the uncertainty about the Fed, issues in the bond market, and trade disputes. The consensus view is more positive for the economic outlook of the national economy. Few economists are calling for a recession in 2020.

Ms. Niwao asked about the impacts of a skirmish with Iran. Dr. Bonham noted that these scenarios would have negative impacts. However, Mr. Hayashi noted that these risks have always been there. Dr. Suyderhoud noted that the current forecast is for a relatively subdued economy. He said that the forecast implies low growth and a recession at some point in the future.

Dr. Bonham proposed that forecast should be shift to 4.0%, 3.0%, 3.0%, 4.0%, 4.0%, 4.0%. Ms. Niwao said that this forecast implied a relatively more positive outlook in calendar year in 2020.

A motion was made by Ms. Maynard that the General Fund revenue for the remaining out years remain the same: 4.0% (2021); 3.0% (2022); 3.0% (2023); 4.0% (2024); 4.0% (2025) and 4.0% (2026). Dr. Suyderhoud seconded. The Chair called for the vote, and the motion passed with the following votes:

Kurt Kawafuchi	Yes
Marilyn Niwao	Yes
Jack P. Suyderhoud	Yes
Carl S. Bonham	Yes
Jessica Gluck	Yes
Kristi L. Maynard	Yes
Scott Hayashi	Yes

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

Significant Changes from September 2018 Report

Mr. Donovan Chun provided the Council with a report of revised projections of General Fund non-tax revenues, non-General Fund tax and non-tax revenues since the August 29th, meeting. Mr. Chun said although the report includes a summary of significant changes, there are several changes he wanted to highlight:

Special Tax Revenues

Transfer of General Excise Tax – The net decreases in FYs 20-26 reflect revised estimates of general excise tax transfers to the Mass Transit Special Fund (B&F) based on the Council's forecast from the meeting held on August 29, 2019.

Other Than Special Fund Non-Tax Revenues

Use of Money and Property – The new increase in the FYs 20-26 reflects the selling of a housing system portfolio and defeasing of related bonds (Department of Business, Economic Development and Tourism (DBEDT)).

Charges for Current Services – The net increase in FY 20 reflects an estimated increase in rebates on prescription drug plans, Consolidated Omnibus Budget Reconciliation Act medical and dental plans, and rate credits or experience gains from insurance carriers to the Hawaii Employer-Union Health Benefits Trust Fund (B&F).

Repayments – The net increases in FYs 20-21 are reflective of Act 189, SLH 2019, which appropriated \$50,000,000 for the Rental Housing Revolving Fund for each fiscal year (DBEDT).

Mr. Hayashi moved to accept the B&F report as submitted. Dr. Bonham seconded. The Chair called for the vote, and the motion passed with the following votes:

Kurt Kawafuchi	Yes
Marilyn Niwao	Yes
Jack P. Suyderhoud	Yes
Carl S. Bonham	Yes
Jessica Gluck	Yes
Kristi L. Maynard	Yes
Scott Hayashi	Yes

NEXT MEETING:

The Council tentatively agreed to meet on Tuesday, March 11, 2020 at 10 a.m.; however, the date and time will be confirmed by e-mail. The Council staff will attempt to secure the Tax Conference Room.

The Chair adjourned the meeting.

ADJOURNMENT:

The meeting adjourned at 3:36 p.m.