LINDA LINGLE
GOVERNOR
THEODORE E. LIU
DIRECTOR
MARK K. ANDERSON
ACTING DEPUTY DIRECTOR

DEPARTMENT OF BUSINESS, ECONOMIC DEVELOPMENT & TOURISM

No. 1 Capitol District Building, 250 South Hotel Street, 5th Floor, Honolulu, Hawaii 96813
Mailing Address: P.O. Box 2359, Honolulu, Hawaii 96804
Web site: www.hawaii.gov/dbedt

Telephone: (808) 586-2355
Fax: (808) 586-2377

Statement of
THEODORE E. LIU
Director
Department of Business, Economic Development, and Tourism
before the
HOUSE COMMITTEE ON FINANCE

Wednesday, February 6, 2008
1:30 PM
State Capitol, Conference Room 308

In consideration of

HB 2942
RELATING TO TAX CREDITS

Chair Oshiro, Vice Chair Lee, and members of the House Committee on Finance.

The department supports the intent of HB 2942, which would repeal (sunset) more that 50 State tax credits and exemptions periodically over the next five years. The Department of Business, Economic Development and Tourism (DBEDT) and the Department of Human Services are directed to conduct evaluations of these tax credits and exemptions prior to their sunset date and recommend whether the legislature should take action to repeal the applicable sunset provision. Without action the particular tax provision would sunset. Most of the credits/exemptions (about 45) are to be evaluated by DBEDT. DBEDT has supported efforts to increase accountability for the use of tax credits and efforts to determine their beneficial impact on the State's economy. In 2007, Act 206 (SLH 2007) directed the Department of Taxation to measure the effectiveness of one major tax credit provision; that being the high technology business investment tax credit.

The tax credits repealed by HB 2942 range from research and investment tax credits relating to qualified high technology businesses, to credits for lifeline telephone service subsidies. The first group of tax provisions would be repealed on December 31, 2010 and the last group on December 31, 2013. Prior to sunset, DBEDT is required to evaluate its assigned credits/exemptions, determine if they are achieving their purpose, are consistent with public policy and finally, make recommendations as to whether these tax credits or exemptions should be reauthorized by the Legislature and Governor. For DBEDT, this is a particularly serious responsibility, since these tax provisions will completely disappear without a sound basis for legislative intervention.

While DBEDT would be an appropriate agency to conduct such an evaluation program, the effort would face challenges. First, to determine the benefit of tax credits, such a program would need to review a considerable amount of detailed tax data and look at the behavior of firms and individuals using the credit. Much of this information would likely be confidential data related to individual tax returns. However, DBEDT does not have direct access to the confidential tax data that would be needed to accomplish the evaluations. While HB 2942 requires the Department of Taxation to assist by collecting and reporting data required for the evaluation, it would be difficult for DBEDT to determine what information is required without initial access to detailed and probably confidential data.

Secondly, this task will require the evaluation of about 10 tax credits and exemptions per year, on average, over the next four and a half years. This will add significant new responsibilities for DBEDT's research staff. We believe additional resources will be needed to fulfill this important obligation. We note that HB 2942 proposes no additional resources to accomplish the new program nor was such a provision made in the Executive's Supplemental Budget. Should the Legislature propose an appropriation we would request that it not displace the priorities contained in the Executive Budget.

Thank you for the opportunity to provide comments on this bill.

LINDA LINGLE
GOVERNOR

JAMES R. AIONA, JR.
LT. GOVERNOR

KURT KAWAFUCHI
DIRECTOR OF TAXATION

SANDRA L. YAHIRO
DEPUTY DIRECTOR

STATE OF HAWAII
DEPARTMENT OF TAXATION
P.O. BOX 259
HONOLULU, HAWAII 96809

PHONE NO: (808) 587-1510
FAX NO: (808) 587-1560

HOUSE COMMITTEE ON FINANCE

TESTIMONY REGARDING HB 2942
RELATING TO TAXATION

TESTIFIER: KURT KAWAFUCHI, DIRECTOR OF TAXATION (OR DESIGNEE)
DATE: FEBRUARY 6, 2008
TIME: 1:30PM
ROOM: 308

This bill repeals certain net income tax credits and exemptions from the General Excise Tax (GET), and it expands the current responsibilities for the Department of Business, Economic Development and Tourism and the Department of Human Services to evaluate certain of Hawaii's income tax credits and exemptions. The bill takes effect upon approval, with various tax credits and GET exemptions set to expire between December 31, 2010 and December 31, 2014.

The Department of Taxation **opposes** this measure, on grounds that it is in the best position to serve as the lead agency for economic studies on the effects of Hawaii's net income tax credits and exemptions from the General Excise Tax (GET). There are several reasons for this.

I. DEPARTMENT IS IN THE BEST POSITION TO STUDY TAX MATTERS.

- **APPROPRIATE AGENCY**—The Department is already charged with performing an economic study on the effectiveness of the largest of the net income tax credits, the high technology business investment tax credit. A new study of the credit by another agency would involve unnecessary duplication of effort.

- **ACCESS TO INFORMATION**—The Department of Taxation is the only agency with access to the detailed tax data needed to properly study net income tax credits. For a competent study of these credits, state tax returns must be matched with federal income tax returns to obtain a comprehensive picture of a company's income or of an individual's income. The State is unable to provide access to federal income tax returns to any of its other agencies.

- **KNOWLEDGE OF THE TAX LAW**—The Department of Taxation is the only agency with in-depth knowledge of how the State's income tax credits and exemptions from the GET actually operate. It has people that know the legal tax issues and that know how to perform solid economic analysis. As evidence of these abilities, you may refer to the Report of the

2005-2007 Tax Review Commission. Department of Taxation staff performed four of the six economic studies contained in the report. In addition, it performed an in-depth examination of the revenue cost of existing GET exemptions.

- **CONFIDENTIALITY**—The Department operates under strict confidentiality laws that preclude it from sharing confidential tax information. Tax information is very personal and the fewer people that have access to it the better. After aggregating the data, however, the Department will work with others to fully study the impact of Act 221 and other income tax credits.

In short, the Department of Taxation is in the best position to lead studies of income tax credits or exemptions from the GET. This would allow the studies to benefit from the most detailed tax information available and, at the same time, prevent exposure of taxpayer information.

II. AUTOMATIC REPEAL OF TAX INCENTIVES IS DANGEROUS

As a general consideration, automatic repeal of the magnitude contemplated by this legislation needs to be approached cautiously.

The current bill contains a number of items that are listed as exemptions from the GET that probably do not merit consideration. These exemptions are necessary for the GET to have a sensible structure that minimizes economic distortions – they are not exceptions from a uniform and consistently administered excise tax. Examples are:

- The exemptions for property and services shipped out of the State in sections 237-29.5 and 237-29.53 of the Hawaii Revised Statutes (HRS) (it is inconsistent to impose a broad-based excise tax on both exports and imports);
- The exemption of public service companies in section 237-23(1), HRS (their gross income is taxed in chapter 239, HRS);
- The exemption for insurance companies in section 237-29.5, HRS (insurance companies are subject to a tax on insurance premiums);
- The exemption for income of financial institutions in section 237-24.8, HRS (it is impractical to attempt any gross income taxation of financial services income); and
- The exemption for amounts collected as tax in section 237-24, HRS (to the extent that it can be avoided, excise taxes should not pyramid on other excise taxes).

Any study of GET exemptions should begin with a list of aberrations from an ideal, uniformly applied tax.

Also, the income tax credits listed in the bill for sections 241-4.5, 241-4.6 and 241-4.8, HRS need not be repealed separately – they would disappear automatically with the elimination of the corresponding credits in chapter 235.

III. REVENUE ESTIMATE

With these caveats in mind, the Department of Taxation estimates that the current direct annual revenue gain from the credits and exemptions set to expire on December 31, 2010, will be about $28 million by 2011; the annual revenue gain from the credits and exemptions set to expire December 31, 2011 will be about $140 million by 2012; the annual revenue gain from the provisions set to expire December 31, 2012 will be about $1.2 billion by 2013; the annual revenue gain from the provisions set to expire December 31, 2013 will be about $160 million by 2014; and the annual revenue gain from the provisions set to expire December 21, 2014 will be about $12 million by 2015.

The Department emphasizes that these estimates are very tentative. For example, an annual growth factor of 4 percent per year has arbitrarily been assumed for all provisions for all years. However, the estimates do not include the revenue gains from eliminating the GET exemptions for insurance companies given by section 237-29.7, HRS or for eliminating the GET exemption for certain income of financial institutions given by section 237-24.8, HRS.

LINDA LINGLE
GOVERNOR

LILLIAN B. KOLLER, ESQ.
DIRECTOR

HENRY OLIVA
DEPUTY DIRECTOR

STATE OF HAWAII
DEPARTMENT OF HUMAN SERVICES
P. O. Box 339
Honolulu, Hawaii 96809-0339

February 6, 2008

MEMORANDUM

TO: Honorable Marcus R. Oshiro, Chair
House Committee on Finance

FROM: Lillian B. Koller, Director

SUBJECT: H.B. 2942 – RELATING TO TAXATION
Hearing: Wednesday, February 6, 2008, 1:30 p.m.
Conference Room 308, State Capitol

PURPOSE: The purpose of this bill is to require the Department of Business, Economic Development, and Tourism (DBEDT) and the Department of Human Services (DHS) to evaluate certain tax credits and tax exemptions and report to the Legislature as to whether they should be modified, reenacted, or repealed. Provides automatic repeal of the tax credits and tax exemptions unless extended by the Legislature..

DEPARTMENT'S POSITION: The Department of Human Services cannot support this bill as written. This bill would require DHS to evaluate certain tax credits and tax exemptions and report to the Legislature as to whether they should be modified, reenacted, or repealed. We request that this function be given to a Department that has this expertise and to whom we will gladly provide any information necessary for its evaluation.

The tax credits listed for DHS to evaluate are not DHS tax credits. Section 235-15 regarding child passenger seats is a Department of Health program. Section 235-110.2 for school repair and maintenance is administered by the Department of Education. Section 239-

6.5 is for telephone service under the Public Utilities Commission. Sections 235.110.8 and 2337.29 are under the Hawaii Housing Finance and Development Corporation that is attached to DBEDT. Section 241.4.7 is an income tax credit with the Department of Taxation better able to provide information.

We defer to DBEDT as to the placement of the evaluation function in DBEDT as proposed in this bill and respectfully request that the passage of this bill does not replace nor adversely impact the priorities in the Executive Supplemental Budget.

Thank you for this opportunity to testify on this bill.

Linda Lingle
GOVERNOR

ORLANDO "DAN" DAVIDSON
EXECUTIVE DIRECTOR

STATE OF HAWAII
DEPARTMENT OF BUSINESS, ECONOMIC DEVELOPMENT AND TOURISM
HAWAII HOUSING FINANCE AND DEVELOPMENT CORPORATION
677 QUEEN STREET, SUITE 300
Honolulu, Hawaii 96813
FAX: (808) 587-0600

IN REPLY REFER TO

Statement of
Orlando "Dan" Davidson
Hawaii Housing Finance and Development Corporation
Before the

HOUSE COMMITTEE ON FINANCE

February 06, 2007, 1:30 p.m.
Room 308, State Capitol

In consideration of
H.B. 2942
RELATING TO TAXATION

The HHFDC is opposed to H.B. 2942, as it would eliminate affordable housing development incentives that have resulted in the construction or substantial rehabilitation of thousands of affordable housing units statewide. We defer to the appropriate state departments and agencies with respect to the remainder of the bill. Our comments on specific portions of this bill follow.

H.B. 2942 repeals section 235-110.8, Hawaii Revised Statutes (HRS) as of December 31, 2010. This section establishes the State Low Income Housing Tax Credit (LIHTC) for eligible affordable rental housing projects. It also repeals section 241-4.7, HRS as of December 31, 2010, which makes the state LIHTC applicable to banks and financial corporations. All LIHTC-financed rental units are targeted at low-income seniors and families earning 60 percent or less of the area median income. Without the LIHTCs, it is unlikely that such projects could be developed given the high cost of land and construction.

This bill also repeals section 237-29, the general excise tax exemption for certified affordable housing projects. The Legislature's intent in creating this exemption was to assure the economic feasibility in the development of a housing project which will encourage and enable the production of as many lower cost housing units as possible. The GET exemption has been a successful incentive for the development and preservation of affordable housing, and should be allowed to continue.

Finally, this bill requires the Department of Human Services to prepare an evaluation of the LIHTC and GET exemption pursuant to new section 235-B. We note that subsequent to the bifurcation of state housing programs in Act 179, SLH 2005, as amended by Act 180, SLH 2006, responsibility for these tax exemptions and credits was transferred to the HHFDC, which is attached to the Department of Business, Economic Development and Tourism (DBEDT) for administrative purposes, and, accordingly, DBEDT should be the agency responsible for any such review.

We urge the Committee to delete these provisions from this bill, because they will adversely affect affordable rental housing development statewide. Thank you for the opportunity to testify.

HAWAII RENEWABLE ENERGY ALLIANCE

46-040 Konane Place #3816, Kaneohe, HI 96744 – Telephone/FAX: 247-7753 – Email: wsb@lava.net

TESTIMONY OF WARREN BOLLMEIER ON BEHALF OF THE HAWAII RENEWABLE ENERGY ALLIANCE BEFORE THE HOUSE COMMITTEE ON FINANCE

HB 2942, RELATING TO TAXATION

February 6, 2008

Chair Oshiro, Vice-Chair Lee and members of the Committee, I am Warren Bollmeier, testifying on behalf of the Hawaii Renewable Energy Alliance (HREA). HREA is a nonprofit corporation in Hawaii, established in 1995 by a group of individuals and organizations concerned about the energy future of Hawaii. HREA's mission is to support, through education and advocacy, the use of renewables for a sustainable, energy-efficient, environmentally-friendly, economically-sound future for Hawaii. One of HREA's goals is to support appropriate policy changes in state and local government, the Public Utilities Commission and the electric utilities to encourage increased use of renewables in Hawaii.

The purposes of HB 2942 are to: (1) require the department of business, economic development, and tourism, and the department of human services to evaluate certain tax credits and tax exemptions and report to legislature as to whether they should be modified, reenacted, or repealed, and (2) provide automatic repeal of the tax credits and tax exemptions unless extended by the legislature. HREA ***strongly opposes*** this bill as it proposes the repeal of the Renewable Energy Technologies Income Tax Credit ("RETITC"). We take no position on the merits of the other tax credits contained in the bill.

HREA strongly supports continuation of the RETITC:

(1) The RETITC is a cost-effective incentive for <u>encouraging private investment in wind and solar technologies in Hawaii</u>. Over 100,000 solar hot water heaters are installed and operational in Hawaii, in large part due to the RETITC and its predecessor, the Energy Conservation Income Tax Credit. Currently, over 5,000 solar systems are being installed annually, and RETITC is also leveraging private investment in wind energy systems Furthermore, <u>energy generation and savings</u> from solar and wind contribute to the utility's Renewable Portfolio Standard;

(2) The RETITC help <u>protect our environment</u> by reducing our use of imported fossil energy and greenhouse gas emissions. ; and

(3) It has been shown after years of analysis and discussion (Energy Efficiency Policy Task Force and supporting analysis to the Task Force from economist Dr. Tom Loudat) that the RETITC stimulates new <u>economic benefits</u>, including creation and sustenance of new jobs, and net return of state revenues over time.

In short, HREA recommends continuation of the RETITC as it is replete with energy, environmental and economic benefits. Therefore, we do not believe it is necessary for DBEDT to conduct a study of the RETITC, as proposed in Section 1, §235-B Evaluation; report.

Thank you for this opportunity to testify.

SciTech
HAWAII SCIENCE & TECHNOLOGY COUNCIL

HOUSE BILL 2942: RELATING TO HIGH TECHNOLOGY: Requires DBEDT to review tax credits.

DATE: February 6, 2008
1:30 p.m., Conference Room 308

TO: House Committee on Finance
The Honorable Marcus Oshiro, Chair
The Honorable Marilyn B. Lee, Vice Chair

FROM: Lisa H. Gibson
President
Hawaii Science & Technology Council

RE: **No Position on DBEDT Tax Credit Review With the Exception of Opposition with Regard to Act 221/215**

Aloha Chair, Vice Chair, and Members of the Committee:

The HSTC takes no position on the review of tax incentives in this bill with the exception of opposition to DBEDT's evaluation of Act 221/215. First, we believe that the agency with the expertise to conduct any study of tax credits is the State Department of Taxation. Secondly, the recently issued DoTax report produced pursuant to Act 206, SLH clearly establishes that the high technology investment tax credit has been productive and beneficial. Statistical highlights from the October, 2007 DoTax report on Act 221/215 include:

- Number of Act 221/215 companies (2002-2006): 287
- Average annual technology salary (2006): $67,000
- Expenditures by QHTBs in Hawaii (ie salaries, capital improvements, etc 2002-2006): More than $1 billion
- Salaries Paid: More than $500 million
- Jobs created (2002-2006): 5,383
- Investment Tax credits claimed (2002-2005): Less than $195 million
- Research & Development Tax Credits Claimed by Companies 2001 – 2004: $47 million

The Hawaii Science & Technology Council is a 501(c)6 industry association with a 28-member board. The council serves Hawaii companies engaged in ocean sciences, agricultural biotechnology, astronomy, defense aerospace, biotech/life sciences, information & communication technology, energy, environmental technologies, and creative media.

Thank you for the opportunity to testify on this important bill.
Lisa H. Gibson
President

735 Bishop Street, Suite 401 Honolulu, Hawaii 96813
808.536.4670 *phone* | 808.536.4680 *fax* |

Hawaii Solar Energy Association
Serving Hawaii Since 1977

TESTIMONY OF THE HAWAII SOLAR ENERGY ASSOCIATON IN REGARD TO H.B. 2942, RELATING TO TAXATION BEFORE THE HOUSE COMMITTEE ON FINANCE ON WEDNESDAY, FEBRUARY 6, 2008

Chair Oshiro, Vice-Chair Lee my name is Rick Reed and I represent the Hawaii Solar Energy Assn. (HSEA). HSEA opposes the intent of this bill which would require DBEDT or the Department of Human Services to evaluate **all** State of Hawaii tax credits for merit over the next few years and then make recommendations as to whether or not each individual credit should be reenacted, modified, or permitted to expire.

Our opposition is largely based on the fact some of this very expensive work, for which adequate staffing does not exist, already has been done. HSEA believes that specific credits that have been the subject of prior DBEDT-related analyses should be exempt from this bill.

In 2002, DBEDT issued, "The Report of the Energy-Efficiency Policy Task Force", a 217 page study of the then titled energy conservation income tax credits (HRS 235-12). The report included a detailed and comprehensive analysis conducted by Dr. Thomas Loudat, and peer reviewed by Dr. Leroy Laney, of the economic and fiscal impacts of this specific credit.

Dr. Loudat found that these tax incentives produced both the desired behavior, i.e. the purchase of renewable energy devices that would not have been installed absent the incentive, and also provided significant fiscal benefits to the state over the useful operating life of the equipment Dr. Loudat's work has been praised as a model that might profitably be applied to the analysis of other State of Hawaii tax credits.

The work of the Energy Efficiency Policy Task Force was conducted when world oil prices were under $30/bbl. The fiscal and economic impacts of the tax credits are now, if anything, far more favorable to the State than when the analysis was first conducted.

It is the stated public policy of the State of Hawaii to reduce our dependence on imported and polluting fossil fuel. HRS 235-12.5 has been the SINGLE MOST IMPORTANT policy tool we have to date to accomplish this goal. Clearly there is much more we must do to accelerate the commercialization of renewable energy devices, but eliminating this essential tax incentive would be a grave disservice to Hawaii's taxpayers and ratepayers.

Thank you for the opportunity to present this testimony. .

P.O. Box 37070 Honolulu, Hawaii 96837
SOLAR HOTLINE (808)521-9085

Testimony before the
House Committee on
Finance

H. B. 2942 - Relating to Taxation
Wednesday, February 6, 2008
1:30 p.m., Conference Room 308

By Patsy Nanbu
Controller
Hawaiian Electric Company, Inc.

Chair Oshiro, Vice Chair Lee and Members of the Committee:

My name is Patsy Nanbu and I am testifying on behalf of Hawaiian Electric Company, Inc., and its subsidiaries, Maui Electric Company (MECO) and Hawaii Electric Light Company, Inc. (HELCO).

Hawaiian Electric acknowledges House Bill 2942's intent to review and evaluate the multitude of income tax and general excise tax exemptions and credits that have been enacted over time. The effectiveness of and accountability for these benefits are of concern and should be evaluated periodically. However, we are concerned with the manner by which this bill proposes to accomplish this formidable task.

A blanket repeal of exemptions and credits creates tremendous uncertainty with regards to the cost of doing business in Hawaii since it would require the Legislature to affirmatively re-enact the particular exemption or credit, if deemed necessary and appropriate. This widespread uncertainty makes it extremely difficult for businesses to plan and budget for the future and would inevitably impact Hawaii's economy.

Many of these exemptions and credits have developed over time to address double taxation of specific industries. In the case of Hawaiian Electric, a public utility exemption from the general excise tax exists because revenues are already subject to the public service company tax. This exemption avoids additional taxes which would unfairly increase the cost of electricity to all Hawaii residents.

HB 2942 will place at risk many perfectly reasonable exemptions that have evolved to prevent double taxation. Irrespective of the eventual re-enactment of an exemption or a credit, the uncertainty created by this bill will be disruptive and is likely to increase the cost of doing business for all taxpayers. Consequently, Hawaiian Electric respectfully opposes HB 2942.

Thank you for this opportunity to testify.

Testimony before the
House Committee on
Finance

H. B. 2942 - Relating to Taxation
Wednesday, February 6, 2008
1:30 p.m., Conference Room 308

by Keith Block
Director, Customer Efficiency Programs
Hawaiian Electric Company, Inc.

Chair Oshiro, Vice Chair Lee and Members of the Committee:

My name is Keith Block and I am testifying on behalf of Hawaiian Electric Company, Inc., and its subsidiaries, Maui Electric Company (MECO) and Hawaii Electric Light Company, Inc. (HELCO).

Hawaiian Electric acknowledges the bill's intent to examine the efficacy of tax credits, but is concerned about the automatic repeal provision included in HB 2942.

Hawaiian Electric has been successfully encouraging the use of renewable energy through its residential solar water heating program for over 11 years. In that time the companies have provided rebates to over 39,000 customers for the installation of solar water heating systems on their homes.

State tax credits have been instrumental in the success of this program and in fact many bills have been introduced this year to increase the state tax credit for solar water heating systems. If HB 2942 is passed this tax credit, the Renewable Energy Technologies Income Tax Credit could automatically be repealed on December 31, 2010, if not acted on before then.

In the past this tax credit did have a sunset date. Just the uncertainty associated with a sunset date can have a detrimental affect on the industry as businesses try to plan their future. The legislature recognized this last year and removed the sunset date.

Increasing the penetration of renewable energy systems is consistent with State energy policy. Passage of this bill could adversely affect the penetration of solar water heating systems in Hawaii.

Thank you for this opportunity to testify.

HBA / HAWAII BANKERS ASSOCIATION
1000 BISHOP ST., SUITE 301B • HONOLULU, HAWAII 96813-4203
PHONE: (808) 524-5161 • FAX: (808) 521-4120

Presentation to the House Committee on Finance
Wednesday, February 6, 2008
1:30 p.m.
Conference Room 308

February 6, 2008

Testimony in opposition to HB 2942 Relating to Taxation

TO: The Honorable Marcus R. Oshiro, Chair
The Honorable Marilyn B. Lee, Vice Chair
Members of the House Finance Committee

My name is Stafford Kiguchi with Bank of Hawaii testifying on behalf of the Hawaii Bankers Association. While we understand the desire to further evaluate the impact of certain tax credits and exemptions, we are opposed to the automatic repeal of these credits and exemptions.

We specifically oppose clause 9 on page 4, lines 14 and 15, clauses 6, 7 and 8 on page 6 of the bill, lines 12 through 17.

I believe that the current system of bank taxation was carefully crafted following a study by the Tax Review Commission so no further study is necessary.

Specifically, banks already pay a 7.92 percent franchise tax, which is higher than the corporate tax rate. To lose the banking exemptions would essentially subject banks to what would be comparable to an unfair double tax. In addition, we believe certain credits and exemptions provide meaningful incentive for private investments that may otherwise not occur in their absence. We respectfully encourage the Legislature to delete the provisions related to banks as referenced above.

Thank you for this opportunity to testify.

Hawaii Association of REALTORS®
www.hawaiirealtors.com

The REALTOR® Building
1136 12th Avenue, Suite 220
Honolulu, Hawaii 96816

Phone: (808) 733-7060
Fax: (808) 737-4977
Neighbor Islands: (888) 737-9070
Email: har@hawaiirealtors.com

February 6, 2008

The Honorable Marcus R. Oshiro, Chair
House Committee on Finance
State Capitol, Room 308
Honolulu, Hawaii 96813

RE: H.B. 2942 Relating to Taxation
Hearing Date: February 6, 2008 @ 1:30 a.m., Room 308

Dear Chair Oshiro and Members of the House Committee on Finance:

On behalf of our 10,000 members in Hawaii, the Hawaii Association of REALTORS® (HAR) , **opposes proposed HRS Section 235-A(b)(11) and proposed HRS Section 235-A(b)(12) as set forth in Section 1 of H.B. 2942** – which respectively repeals the low-income housing tax credit under HRS §235-110.8 and GET exemptions for certified or approved housing projects under HRS §237-29 on December 31, 2010.

Smart Growth is our road map to sustaining and enhancing the quality of life in our communities and we believe that this bill ***does not*** align with our core principle of ***providing housing opportunities that are affordable.***

In November 2002, the National Association of REALTORS® (NAR) created the Housing Opportunity Program to address the nation's housing opportunity crisis. According to the NAR, the lack of available and affordable housing is reflected in several ways, including access to employment, education, a good environment and safe neighborhoods. This problem impacts all segments of the real estate market, including first-time purchasers, low-income purchasers, seniors, the disabled, single family buyers and renters, as well as rental property owners and developers. To promote housing opportunities at the state and local levels, the NAR believes that there is a need for greater legislative emphasis to:

1. Preserve the existing housing stock through grants, loans and **financial incentives**.

2. Streamline the zoning and planning approval process.

3. Utilize density bonus features that encourage the development of units priced to sell and rent at the lower end of the market.

4. Establish housing trust funds in order to build affordable housing.

Hawaii Association of REALTORS®
www.hawaiirealtors.com

The REALTOR® Building
1136 12th Avenue, Suite 220
Honolulu, Hawaii 96816

Phone: (808) 733-7060
Fax: (808) 737-4977
Neighbor Islands: (888) 737-9070
Email: har@hawaiirealtors.com

5. Better coordinate services and eliminate duplication.

6. **Make better use of low-interest loans, block grants, low-income housing tax credit programs and deferred loan programs to provide both homeownership and rental housing opportunities.**

HAR strongly believes that the State's present course of increasing the supply of rental housing and owner occupied for sale housing is by far the better long-term solution to the present workforce and affordable housing shortage. HAR believes that the low-income housing tax credit and GET exemptions for certified or approved housing projects provide much needed financial incentives for affordable housing, and that their repeal will hurt the State's present program for increasing the supply of affordable housing.

HAR looks forward to working with our state lawmakers in building better communities by supporting quality growth, seeking sustainable economies and housing opportunities, embracing the cultural and environmental qualities we cherish, and protecting the rights of property owners.

Mahalo for the opportunity to testify.

Sincerely,

Craig K. Hirai, Member
Subcommittee on Taxation and Finance
HAR Legislative Committee

FINtestimony

From: Ann Thornock on behalf of Rep. Marilyn Lee
Sent: Monday, February 04, 2008 1:37 PM
To: FINtestimony
Subject: FW: HB2942 Testimony, 2/6/08 1:30pm

From: Kevin Carney [mailto:kcarney@eahhousing.org]
Sent: Monday, February 04, 2008 1:15 PM
To: reposhiro@capitol.hawaii.gov; Rep. Marilyn Lee; Rep. Karen Awana; Rep. Della Belatti; Rep. Tom Brower; Rep. Mele Carroll; Rep. Faye Hanohano; Rep. Sharon Har; Rep. Jon Karamatsu; Rep. Michael Magaoay; Rep. Joey Manahan; Rep. John Mizuno; repnakason@capitol.hawaii.gov; Rep. Karl Rhoads; Rep. Roland Sagum; Rep. James Tokioka; Rep. Colleen Meyer; Rep. Kymberly Pine; Rep. Gene Ward
Cc: Kevin Carney
Subject: HB2942 Testimony, 2/6/08 1:30pm

Dear Representative Oshiro and Members of the Finance Committee:

A sure fire way to negatively impact the development and operation of low-income rental housing is to include the automatic repeal of Low Income Housing Tax Credits (LIHTCs) and GET exemptions in this proposed legislation. EAH Housing vehemently opposes any such action.

EAH Housing is a non-profit low-income rental housing (family & senior) developer, owner and manager in both California and Hawaii. In the islands, we currently have over 1,400 units under management, 192 units in various stages of development and 72 units in acquisition. This includes Kukui Gardens, a property I am sure that everyone is familiar with. We have operations on Oahu, Maui and Kauai. We depend on both LIHTCs and GET exemptions to make low-income rental housing viable.

LIHTCs are the most powerful tools we have available to us for the development of low-income rental housing. In a nutshell, they provide free equity to us thereby reducing debt and enabling us to keep rents low. GET exemptions help to reduce the cost of construction for low-income rental properties by excluding the tax in calculating fees paid to our contractors and sub-contractors. GET exemptions are also a key component in the on-going financial viability of both the properties we own and the properties we manage for others. The exemption is on rental income only and does not include income from parking, laundry facility or vending machines.

It is extremely difficult and time consuming to develop low-income rental housing and a constant balancing act once the property is completed to be able to keep our rents low with the rising costs of services and utilities. With development it is particularly important to know years in advance that the funding will be there when the time comes to draw it down. For the sake of those in our state who have the greatest need for housing, those at 50% and below of the Area Medium Income, please do not include LIHTCs and GET exemptions in this legislation.

Sincerely yours,

Kevin

Kevin R. Carney, (B)
Vice President, Hawaii
EAH Housing
841 Bishop Street, Suite 2208
Honolulu, Hawaii 96813
Phone: 808-523-8826
Fax: 808-523-8827
Email: kcarney@eahhousing.org
Website: www.eahhousing.org

PACIFICAP
GROUP

PACIFICAP GROUP, LLC
820 Mililani Street, Suite 600
Honolulu, HI 96813
Direct: 808.237.5388 Fax: 808.537.2188

February 6, 2008

To: FINtestimony@capitol.hawaii.gov
Testimony for Hearing before the
House Committee on Finance
Wednesday, February 6, 2008, 1:30 pm

State Capitol, Conference Room 308
415 South Beretania Street
Honolulu, Hawaii 96813

Re: Testimony in Strong Opposition to HB 2942—Relating to Taxation

Chair Oshiro, Vice Chair Lee, and Committee Members:

Thank you for the opportunity to submit testimony in STRONG OPPOSITION to HB 2942, which requires the Department of Business Economic Development and Tourism ("DBEDT") to evaluate certain tax credits and exemptions.

I am Jeff Au, Managing Director and General Counsel of PacifiCap, Hawaii's largest locally based venture capital firm. Since 2000, PacifiCap affiliates have invested in more than two dozen Hawaii companies, and we have led or co-invested in financing rounds totaling more than $400 million. Our investor base of more than 100 institutional, corporate and high net worth individual investors from Hawaii demonstrates the widespread support that innovation, capital formation and economic diversification have across our community.

As a supporter of Hawaii's Act 221/215 tax credits, I support the intent of more study and analysis of these credits since I firmly believe that with more study and analysis, more evidence can and will be provided to the Legislature, and to the general public, of how tremendously successful these tax incentives have been. For this reason, I testified yesterday before the House EDB Committee in favor of HB 2961, which requires further study and analysis of Act 221/215 tax incentives by the Department of Taxation.

The 2007 study conducted by the Department of Taxation, as the Legislature required last year under Act 206, found that between 2002 and 2006, as a result of Act 221/215 tax credits, more than $820 million was invested in more than 287 Hawaii companies, which have already spent more than $1 billion in Hawaii and paid more than $500 million in salaries, at a cost to the State over this five year period of less than $200 million. These data clearly suggest that the benefits have already far exceeded the costs.

However, any further study of these tax incentives must be done by a State agency that has the requisite professional training, legal access to relevant data, institutional integrity and integrity of leadership that will engender the confidence and trust of both the public and the Legislature.

I strongly believe that at the present time, the Department of Taxation is the most appropriate State agency that fulfills these requirements, and NOT the Department of Business Economic Development and Tourism ("DBEDT").

You can see from the attached October 19, 2007 letter to Governor Lingle from Tax Director Kurt Kawafuchi that completing an accurate study of Act 221/215 tax credits, as mandated by Act 206, required the participation of at least **TEN** DoTax staff members. How DBEDT or any other State agency, that may have no professionally trained tax experts currently on staff, can even start to imagine how it could do an accurate analysis of tax incentives, without a sufficient understanding of the specific tax laws that it is supposed to be analyzing, and without legal access to the relevant data, is beyond my comprehension. No State agency other than the Department of Taxation can get full access to all relevant taxpayer data without violating State and federal laws and regulations protecting taxpayer confidentiality.

As a practicing corporate attorney for almost twenty years, now, I can tell you first hand that taxation is a highly specialized area. I would estimate that at least 85% of the lawyers, and even many of the CPA's whom I know, have a very limited understanding, if any, of tax law. Although I have worked on quite a few tax related transactions over the years, when it comes to tax law, I still consider myself to only know enough to be dangerous. I repeatedly remind people that I am a corporate lawyer, and not a tax lawyer, and anyone who has done business with our firm will tell you that for all of our investment transactions, I always insist that all tax issues be independently analyzed, reviewed and approved by our outside tax lawyers or CPA's, who are the real tax experts.

When we, as members of the public see an administrative agency such as DBEDT lobbying the Legislature, whether publicly or behind closed doors, to give it statutory authority to review subject matter such as tax credits for which it has virtually no professionally qualified staff, we have to ask ourselves, what is motivating these DBEDT officials? Is it arrogance? Is it ignorance of not knowing what they don't know? Is it bureaucratic empire building? Or worse, is there another motive or political agenda?

All of the professional tax expertise in the world, however, still would have little value without public trust and confidence in the institutional integrity and leadership of the administrative agency that is conducting the study.

While many of us in this room may have honest disagreements over tax credits and other policy issues, one thing that all of us should be able to agree upon is that Tax Director Kurt Kawafuchi would make a lousy politician. His primary problem is that he is too honest. I think those of you who know Kurt well would agree that it is very difficult for him to tell a lie, be hypocritical or to take a disingenuous policy position for political reasons.

Kurt Kawafuchi is not very good at creating slick sound bites, or "putting lipstick on a pig" to tell you what you want to hear, in spite of the facts, and he is not always right (particularly when he disagrees with me), but if there is a disagreement, with Kurt, at least we all know that it is an honest disagreement, and not one motivated by political or other ulterior motives.

DBEDT, on the other hand, is currently under investigation by the State Office of Procurement and Hawaii State Senate for noncompliance and possible violations of State procurement laws in connection with its awarding of the State Hydrogen Fund contract, which the State Procurement Office ordered DBEDT to rescind, as well as other procurement matters being investigated by the Senate (pursuant to SR 2). This seriously undermines public confidence in the objectivity and credibility of any study on tax credits conducted by DBEDT. A January 23, 2008 *Honolulu Advertiser* report the procurement investigations of DBEDT is attached for your reference.

I respectfully suggest that you, as members of the House Finance Committee, consider the QUANTITATIVE financial numbers in your deliberations over Act 221/215, as well as other tax credits and exemptions. For example, HB 1629 was heard yesterday before the House EDB Committee to repeal the state Corporate Income Tax, primarily because it is "too small" in generating tax revenues to be worth the trouble. The estimated amount is on average about $80 million per year. The estimated cost of Act 221/215 credits, however, is only about $40 million a year and has proven to stimulate at least twice that amount in salaries and more than 5 times that amount of spending in Hawaii each year. How is it that we can afford $80 million per year to repeal the corporate income tax but not $40 million for Act 221/215, particularly when Act 221/215 requires re-investment in our state, while corporations could simple take their tax savings to the mainland with no re-investment in Hawaii if the corporate income tax is repealed?

I also respectfully ask that you be cognizant of the disruptive effect on our entire economy that may result from uncertainty created by this bill. Aside from jeopardizing the financial stability of hundreds of Hawaii's most promising high tech and media companies and the livelihoods of their thousands of employees, what would be the effect on union negotiations and all employees in our state if the General Excise Tax exemption for wages (of almost $1 billion each year) is repealed? What will be the impact on our healthcare systems if our largest hospitals, most of which are non-profits and are already struggling financially, have an additional General Excise Tax liability of more than 4% of their revenues because the GE Tax exemption for nonprofits is repealed? What will happen to the stock prices of Hawaii's largest banks that are publicly traded, if they have to disclose in their SEC filings that the Legislature is considering requiring them to pay, on top of their franchise taxes, an additional GE Tax of more than 4%, which may be more than their total annual profits? What will happen to local real estate values if the stock prices and financial stability of our local banks start to collapse?

Thank you very much for the opportunity to submit this testimony.

Respectfully submitted,

Jeffrey K. D. Au
Managing Director and General Counsel
PacifiCap Group, LLC

020508JAUTestimonyinOppositiontoHB2942

JAMES R. AIONA, JR.
LT. GOVERNOR

KURT KAWAFUCHI
DIRECTOR OF TAXATION

SANDRA YAHIRO
DEPUTY DIRECTOR

STATE OF HAWAII
DEPARTMENT OF TAXATION
P.O. BOX 259
HONOLULU, HAWAII 96809

PHONE NO: (808) 587-1440
FAX NO: (808) 587-4145

October 19, 2007

The Honorable Linda Lingle
Governor
State of Hawaii

Dear Governor Lingle:

I am pleased to present you with this **Report on the Operations of Qualified High Technology Businesses From 2002 Through 2006** as required by Act 206, SLH 2007.

On June 21, 2007, House Bill 1631 HD2, SD2, CD 1, was signed into law as Act 206. The purpose of Act 206 is to measure the effectiveness of the Act 178/221/215 business investment tax credit. The act requires any qualified high technology business (QHTB) that accepts an investment for which a credit may be claimed under Section 235-110.9, Hawaii Revised Statutes (HRS), to complete a survey that must be provided to the Department of Taxation by June 30 of each year for each of the five years following the year of investment.

The survey is to be filed electronically through the Department's website. The Department is required to report the information by providing summary statistical information. The report is due by September 1 of each year. The Department is currently finalizing the survey form, which should be ready for implementation early in 2008. This on-line survey will be used to gather information for the 2007 and later calendar years.

Act 206, SLH 2007 also requires that the Department prepare a report by October 31, 2007 summarizing the data submitted by QHTBs on Form N-317 prior to Act 206, SLH 2007. The report is to include summary statistics of the information provided, to date. The present report was compiled in order to satisfy this requirement.

Some highlights:

- A total of 287 separate QHTBs filed Form N-317 at one time or another over the period from 2002 through 2006.
- Total expenses incurred in Hawaii by the QHTBs totaled $1.043 billion over the period from 2002 through 2006.
- Investments received by the QHTBs totaled $821.6 million over the same period.
- QHTBs that reported operations solely in the Performing Arts sector received about 35 percent of the investments received by all QHTBs ($284.7 million) over the same period.
- Computer Software is the most frequently listed activity of the QHTBs.

A

- In 2006, the 157 QHTBs that filed Form N-317 reported paying 2,322 employees that year; the average of the employee salaries was $56,262.
- In 2006, the 157 QHTBs that filed Form N-317 reported that they created 5,383 jobs since their inceptions.
- Total High Technology Business Investment Tax Credit claimed by Hawaii residents totaled $195.6 million over the period from 1999 through 2005.

This report was prepared under the direction of Dr. Tu Duc Pham, Tax Research and Planning Officer, with the assistance of the Tax Research and Planning Office's staff: Glenn Ifuku, High Technology Study Technical Coordinator; Yvonne Chow, Economist; Lynn Ma, Research Statistician; the Rules Office's staff: Johnnel Nakamura, Rules Officer; Jason Healey, Rules Specialist – who compiled the summary and history of the High Technology Business Investment Tax Credit and Tax Credit for Research Activities; Betty Lam, Rules Specialist; Donald Rousslang, Tax Specialist – who compiled the tables and drafted the initial report; and Titin Sakata, Special Assistant to the Director.

Respectfully submitted,

KURT KAWAFUCHI
Director of Taxation

8

HonoluluAdvertiser.com

Posted on: Wednesday, January 23, 2008

$8.7M hydrogen technology contract held up by dispute

By Sean Hao
Advertiser Staff Writer


The state has until the end of this month to decide whether to award a contract to manage an $8.7 million hydrogen technology investment fund. Pictured, DBEDT Director Ted Liu.

The state has until the end of this month to decide whether to award a contract to manage an $8.7 million hydrogen technology investment fund.

The fund was authorized by lawmakers in 2006 to help finance companies working to develop clean-burning hydrogen fuel from renewable resources such as wind and water. However, the fund's launch has been held up by a dispute over who should manage the project.

The state Procurement Office ruled in September that a contract to manage the fund should have been awarded to the highest-ranking bidder, which was Kolohala Holdings LLP. Earlier this month the Department of Business, Economic Development and Tourism requested more time to decide whether to award the contract to Kolohala or cancel the contract outright.

DBEDT requested more time because the agency has entered into discussions with the U.S. Department of Energy that could encumber some of the same hydrogen fund money sought by Kolohala. Further details surrounding that new renewable energy partnership will be announced next week, said DBEDT Director Ted Liu.

Yesterday, the Procurement Office said DBEDT cannot cancel its original request for proposals based on the new federal partnership. Procurement Office Administrator Aaron Fujioka also said DBEDT should award the hydrogen fund contract to Kolohala or provide justification for not awarding the contract by Jan. 31.

"While you have determined that a change in circumstance has delayed the award as required in my Sept. 25, 2007 memorandum, there does not appear to be sufficient justification to support this," Fujioka wrote in a letter to Liu dated yesterday. "If the DBEDT's determination that the federal partnership will result in no longer requiring the services of the RFP, then a request with sufficient justification should be submitted by the above date for my review and approval."

The hydrogen fund and the contents of the letter were discussed during a state Senate Tourism and Government Operations Committee hearing yesterday.

"This federal partnership I believe is in the best interest of the state," Liu told the committee. "If it happens, and it sounds like there's a very good chance it will happen, it's going to impact how the hydrogen fund is implemented."

Senate Vice President Donna Kim, D-14th (Halawa, Moanalua, Kamehameha Heights), said DBEDT has an obligation to follow through and award the contract to Kolohala. DBEDT mistakenly awarded the contract to third-ranked bidder H2 Energy LLC in August. In September the Procurement Office ordered DBEDT to rescind the award because H2 Energy was the lowest-ranking choice of an evaluation committee that reviewed three qualifying proposals. Kolohala was the top-ranked bidder.

"That (federal partnership) is great but that has no bearing on this RFP," Kim told Liu.

"You put out an RFP. We are bound by that RFP. In good faith people applied for it and went through the process of being evaluated.

"The only reason we are here, Mr. Liu, is because you wanted to give it to the No. 3 bidder."

Reach Sean Hao at shao@honoluluadvertiser.com.

Back

Hawaii Solar Energy Association
Serving Hawaii Since 1977

TESTIMONY OF THE HAWAII SOLAR ENERGY ASSOCIATON
IN REGARD TO H.B. 2942, RELATING TO TAXATION
BEFORE THE
HOUSE COMMITTEE ON FINANCE
ON
WEDNESDAY, FEBRUARY 6, 2008

Chair Oshiro, Vice-Chair Lee my name is Rick Reed and I represent the Hawaii Solar Energy Assn. (HSEA). HSEA opposes the intent of this bill which would require DBEDT or the Department of Human Services to evaluate **all** State of Hawaii tax credits for merit over the next few years and then make recommendations as to whether or not each individual credit should be reenacted, modified, or permitted to expire.

Our opposition is largely based on the fact some of this very expensive work, for which adequate staffing does not exist, already has been done. HSEA believes that specific credits that have been the subject of prior DBEDT-related analyses should be exempt from this bill.

In 2002, DBEDT issued, "The Report of the Energy-Efficiency Policy Task Force", a 217 page study of the then titled energy conservation income tax credits (HRS 235-12). The report included a detailed and comprehensive analysis conducted by Dr. Thomas Loudat, and peer reviewed by Dr. Leroy Laney, of the economic and fiscal impacts of this specific credit.

Dr. Loudat found that these tax incentives produced both the desired behavior, i.e. the purchase of renewable energy devices that would not have been installed absent the incentive, and also provided significant fiscal benefits to the state over the useful operating life of the equipment Dr. Loudat's work has been praised as a model that might profitably be applied to the analysis of other State of Hawaii tax credits.

The work of the Energy Efficiency Policy Task Force was conducted when world oil prices were under $30/bbl. The fiscal and economic impacts of the tax credits are now, if anything, far more favorable to the State than when the analysis was first conducted.

It is the stated public policy of the State of Hawaii to reduce our dependence on imported and polluting fossil fuel. HRS 235-12.5 has been the SINGLE MOST IMPORTANT policy tool we have to date to accomplish this goal. Clearly there is much more we must do to accelerate the commercialization of renewable energy devices, but eliminating this essential tax incentive would be a grave disservice to Hawaii's taxpayers and ratepayers.

Thank you for the opportunity to present this testimony. .

P.O. Box 37070 Honolulu, Hawaii 96837
SOLAR HOTLINE (808)521-9085