

LINDA LINGLE
GOVERNOR



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Testimony of Linda L. Smith
Senior Policy Advisor to the Governor

Before the

SENATE COMMITTEE ON ECONOMIC DEVELOPMENT AND TAXATION
on
SENATE BILL No. 2164 Senate Draft 1

Tuesday, February 12, 2008
1:15 P.M.

Chair Fukunaga, Vice Chair Espero, and members of the committee, thank you for the opportunity to testify on Senate Bill 2164 SD1.

The Administration has several concerns with this bill, including advice from the Attorney General that this bill is unconstitutional. While the intent is commendable, as drafted, the Administration cannot support Senate Bill 2164 SD1 and urges the committee to address our concerns and provide meaningful facilities support to charter schools.

This bill provides a tax credit for eligible taxpayers who contribute in-kind services for the repair, maintenance, acquisition, predevelopment, rehabilitation, construction, and other capital improvements of charter schools. The income tax credit is also available for in-kind services for facilities administered, operated, or developed by a nonprofit corporation for the benefit of a charter school. The tax credit is set at ten per cent of the value of in-kind goods and services contributed to the Hawaii charter school facilities fund. This bill directs the Department of Accounting and General Services to determine and certify the "value of contributions of in-kind goods and services" based on the fair market value of the services or labor. The Charter School Review Panel is charged with maintaining records of the names of taxpayers eligible for the tax credit offered by this bill and the total value of in-kind goods and services that were contributed by the taxpayer or nonprofit corporation; the Panel must verify all contributions and issue certificates to the taxpayer. The taxpayer submits the certificate to the Department of Taxation with their tax return, and the department and must prepare any forms to carry out the administration of this tax credit.

The Administration has severe concerns about the tax credit established in this bill and the administrative implementation of the credit. We draw your attention to critical comments

presented by both the Department of the Attorney General and the Department of Taxation in the Senate Education Committee hearing. Most notably, the bill defines the tax credit to be ten per cent of the value of in-kind goods and services contributed to the Hawaii charter school facilities fund. However, the fund cannot accept services or goods, only appropriations and cash contributions or grants. Further, it would be difficult to determine the value of goods and services that are contributed after the fact of work performed, and even more difficult to verify these amounts. As the Department of Taxation points out, there is a concern with regard to over-inflation and the possibility of fraud.

We are also concerned with the Hawaii charter school facilities fund established under this bill that would be controlled by Kanu o Ka Aina. The bill appropriates \$2.5 million in general revenues into the fund. The Attorney General testified in the Senate Education Committee that this provision violates Article VII, Section 4 of the Hawaii State Constitution. The Department of Budget and Finance provided similar comments in their testimony. This fatal flaw in the bill should be addressed.

It appears in the purpose section of this bill that the intent is to foster a public-private sector partnership that will benefit charter school facilities support similar to the relationship Hawaii 3Rs has with the Department of Education. This begs the question then why the legislature would be given the authority to restrict moneys in the Hawaii charter school facilities fund? The legislature should not be able to decide which projects to fund. This also calls into question the relationship between goods and services provided, the administration of the fund, the role of the legislature in deciding how to spend monies in the fund via restrictions, and the dynamic of the tax credit.

We are also concerned with the language regarding the matching funds that Kanu o Ka Aina must contribute to a project funded by the Hawaii Charter School Facilities fund. This bill allows federal funds that would otherwise flow directly to charter schools from the Department of Education (SEA designee/recipient) to be used by, and presumably received, Kanu o Ka Aina as their dollar for dollar match to the project. We do not support this provision.

In general, the Administration supports the recommendations of the Proviso 193 workgroup which was convened this interim and presented its findings and recommendations to the Legislature earlier this year. The recommendations included debt service funding equal to a per pupil amount based on the Department of Education's debt service funding, and a capital improvement projects budget request to be approved by the Charter School Review Panel.

Attached are the comments of the Departments of Budget and Finance, Attorney General, and Taxation from the Senate Education Committee Hearing.

As the session moves forward we would like to work with the Committee and affected individuals to assist in crafting legislation that best achieves the goal of providing charter school facilities funding. We do not support this bill as drafted.



TESTIMONY OF THE STATE ATTORNEY GENERAL TWENTY-FOURTH LEGISLATURE, 2008

ON THE FOLLOWING MEASURE:

S.B. NO. 2164, RELATING TO EDUCATION.

BEFORE THE:

SENATE COMMITTEE ON EDUCATION.

DATE: Monday, January 28, 2008 **TIME:** 1:15 PM

LOCATION: State Capitol, Room 225

Deliver to: Conference, Room 225, 1 copy

TESTIFIER(S): Mark J. Bennett, Attorney General
OR Holly T. Shikada, Deputy Attorney General
OR Melissa Chee, Deputy Attorney General

Chair Sakamoto and Members of the Committee:

The Department of the Attorney General takes no position on what the bill is trying to accomplish, but testifies to suggest several revisions to address the legal problems contained in the bill.

The purpose of this bill is to augment state funding for public charter school facilities by providing a tax credit to encourage private individuals to provide goods and services to build, repair, and maintain charter school facilities, and establishing a fund that is to be administered by a private nonprofit corporation to receive and distribute the donations that the tax credit generates to the charter schools. In its present form, the bill has several legal problems that would affect its implementation.

First, section 2 of the bill, on page 6, line 1, creates "a tax credit for charter school repair, maintenance, acquisition, predevelopment, rehabilitation, construction, and other capital improvements" is ambiguous. Subsection (a), on page 6 line 3, and subsection (b), on page 7, line 6, state that qualified contributions in the form of services and goods qualify for the credit and subsection (c), on page 7, line 17, states how to calculate the tax credit. In explaining how to calculate the tax credit, subsection (c) states, "[t]he amount of the tax credit established under this section shall be

equal to ten per cent of the value of the contributions of in-kind goods and services to Hawaii charter school facilities fund for that taxable year. . ." However, the "Hawaii charter school facilities fund," as established in section 3, on page 11, line 18, can generally accept money, not services or goods. Therefore, a taxpayer would not be able to claim a credit for contribution of goods and services, as the fund is only allowed to accept only money. Furthermore, even if the fund was able to accept goods and services, section 3 of the bill is silent as to how these items will be accepted, allocated, distributed, or stored.

Third, section 3, at line 18 on page 11 of the bill, adds a new section in chapter 302B, Hawaii Revised Statutes, creating a "Hawaii charter school facilities fund" as a separate fund to be controlled and used for Kanu o ka aina, a private nonprofit organization. Section 4 on page 17 appropriates \$2,500,000 to the "Hawaii charter school facilities fund." This appears to be a violation of article VII, section 4 of the State Constitution, which prohibits appropriations for private purposes or grants made without complying with standards provided by law.

The Attorney General respectfully requests that if this bill is passed, it be revised in accordance with the above.

TESTIMONY BY GEORGINA K. KAWAMURA
DIRECTOR, DEPARTMENT OF BUDGET AND FINANCE
STATE OF HAWAII
TO THE SENATE COMMITTEE ON EDUCATION
ON
SENATE BILL NO. 2164

January 28, 2008

RELATING TO EDUCATION

Senate Bill No. 2164, among other provisions, establishes a Hawaii charter school facilities fund to be administered by Kanu O Ka Aina Learning Ohana to provide grants, loans or contracts to charter schools, nonprofit corporations, or private vendors for the purpose of providing facilities for charter schools. Further, the bill provides tax credits for taxpayers who contribute in-kind services to charter schools and appropriates \$2,500,000 in general funds for FY 08-09 for deposit into the Hawaii charter school facilities fund.

We do not support this bill. Kanu O Ka Aina Learning Ohana is not a State agency and, as such, should not be a recipient of State funds without undergoing the appropriate procedures. Also, as a matter of general policy, this department does not support the creation of any special or revolving fund which does not meet the requirements of Section 37-52.3 of the Hawaii Revised Statutes. Special or revolving funds should: 1) reflect a clear nexus between the benefits sought and charges made upon the users or beneficiaries of the program; 2) provide an appropriate means of financing for the program or activity; and 3) demonstrate the capacity to be financially self-sustaining. It is difficult to determine whether the fund will be self-sustaining.

LINDA LINGLE
GOVERNOR

JAMES R. AIONA, JR.
LT. GOVERNOR



KURT KAWAFUCHI
DIRECTOR OF TAXATION

SANDRA L. YAHIRO
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SENATE COMMITTEE ON EDUCATION

TESTIMONY REGARDING SB 2164 RELATING TO EDUCATION

TESTIFIER: KURT KAWAFUCHI, DIRECTOR OF TAXATION (OR DESIGNEE)
DATE: JANUARY 28, 2008
TIME: 1:15PM
ROOM: 225

This legislation provides a tax credit for persons that make contributions to charter school repairs, maintenance, or development.

The Department of Taxation (Department) provides comments on this legislation.

I. THE DEPARTMENT SUPPORTS CHARTER SCHOOL FACILITIES IMPROVEMENTS

Encouraging the development of charter schools is an important public policy. As the Administration has stated time and again, charter schools are a vibrant, vital, and successful alternative to traditional public schools. Legislation such as this, which seeks to direct support to the charter school movement, are important measures that deserve consideration.

II. A CHARITABLE DEDUCTION CAN ALREADY BE CLAIMED FOR GOODS.

The Department points out that a charitable tax deduction is already allowed for donations of goods to qualifying educational institutions. This legislation would result in a double tax benefit. No deduction is allowed for services. Correspondingly, however, no income tax is paid by the donor.

III. DONORS OF SERVICES WILL BE CHARGED INCOME TAX.

Under this bill, persons that donate services will be entitled to a credit for services performed. This credit will be considered income for their services and will be subject to income tax. The Department questions the attractiveness of such credits where the benefit will be diluted because income tax will have to be paid.

IV. THE DEPARTMENT POINTS OUT ADMINISTRATIVE CONCERNS

The Department's primary concern with this legislation is the administrative difficulty that may arise based upon how the credit is currently drafted.

CONCERN OVER INFLATED IN-KIND SERVICES—The Department recognizes that this legislation requires that the in-kind services must be certified by the Department of Accounting & General Services. However, the concern that in-kind services will not be grossly over-inflated for purposes of claiming the credit may not be sufficiently tempered as written. The Department suggests the Committee further discern the issue of potential fraud and abuse. The Department is also concerned about the level of resources necessary to administer this component of the credit.

DETERMINATION OF DELINQUENT TAXES—The Department is also concerned about administering the delinquency status of taxpayers. The number of taxpayers that may seek to claim the credit may overwhelm the determination of delinquent status. The Department is concerned about the level of resources that will be necessary to administer this component of the credit.

OTHER AGENCY INVOLVEMENT—The Department very much appreciates that this legislation delegates determination matters to the experts involved, namely the Department of Accounting & General Services and Kanu o ka 'aina learning Ohana.

V. REVENUE ESTIMATE

This legislation will result in a revenue loss of \$250,000 based upon the cap of credits that can be issued.

WRITTEN ONLY

TESTIMONY BY GEORGINA K. KAWAMURA
DIRECTOR, DEPARTMENT OF BUDGET AND FINANCE
STATE OF HAWAII
TO THE SENATE COMMITTEE ON
ECONOMIC DEVELOPMENT AND TAXATION
ON
SENATE BILL NO. 2164, S.D. 1

February 12, 2008

RELATING TO EDUCATION

Senate Bill No. 2164, S.D. 1, among other provisions, establishes a Hawaii charter school facilities fund to be administered by Kanu O Ka Aina Learning Ohana to provide grants, loans or contracts to charter schools, nonprofit corporations, or private vendors for the purpose of providing facilities for charter schools. Further, the bill provides tax credits for taxpayers who contribute in-kind services to charter schools and appropriates \$2,500,000 in general funds for FY 08-09 for deposit into the Hawaii charter school facilities fund.

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- 1) reflect a clear nexus between the benefits sought and charges made upon the users or beneficiaries of the program;
- 2) provide an appropriate means of financing for the program or activity; and
- 3) demonstrate the capacity to be financially self-sustaining.

It is difficult to determine whether the fund will be self-sustaining.



KAMEHAMEHA SCHOOLS

Testimony to the Senate Committee on Economic Development and Taxation
Hearing Date: Tuesday, February 12
1:15p.m. – Conference Room 224

Shawn Malia Kana'iaupuni, PhD
Director, Public Education Support (PEdS) Division
Kamehameha Schools

Tuesday, February 12, 2008

Re: SB 2164, SD1 Relating to Education

Good afternoon Chair Fukunaga, Vice Chair Espero and members of the Senate Committee on Economic Development and Taxation. My name is Shawn Malia Kana'iaupuni, PhD, Director, Public Education Support (PEdS) Division of Kamehameha Schools. Thank you for this opportunity to testify on SB 2164, SD1.

Kamehameha Schools has been a collaborator in the charter school movement for more than six years. As part of our Education Strategic plan, KS hopes to significantly impact more Hawaiian children ages 0-8 and grades 4-16+, and their families/ caregivers over the next five years, in collaboration with others whenever possible.

Currently, Kamehameha Schools collaborates with nonprofit tax-exempt organizations, including `Aha Pūnana Leo, OHA, KALO and Ho`okāko`o Corporation, to assist a total of 14 start-up and 3 conversion charters. Kamehameha Schools believes that this collaboration provides more positive educational choices and ultimately academic achievement for Hawaiian students. Through these collaborations, Kamehameha Schools currently assists more than 2,300 students in 13 communities statewide within the public education system.

In a recently released report entitled, "Longitudinal Outcomes for Hawaiian-focused charter schools," the Kamehameha Schools research team concluded that Hawaiian-focused charter schools are implementing viable educational strategies, making significant gains over time for the lowest-achieving students. Supporting and replicating the successful strategies found in Hawaiian-focused charter schools may generate a promising return on investment for Hawaiian education throughout the public school system.

Kamehameha Schools supports the SB 2164, SD1 which is to provide a greater measure of support for charter schools.

We appreciate this opportunity to submit comments on SB 2164, SD1 and support the initiatives of the legislature to further enhance charter schools.

L E G I S L A T I V E

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SUBJECT: INCOME, Credit for charter school repair and maintenance

BILL NUMBER: SB 2164, SD-1

INTRODUCED BY: Senate Committee on Education

BRIEF SUMMARY: Adds a new section to HRS chapter 235 to allow a taxpayer subject to HRS chapter 235 and: (1) licensed under HRS chapters 444, 448E, 454, 460J, 464, 466K, or 467; (2) is a member of the Hawaii state bar association; (3) is an employee of entities regulated under title 22; or (4) provides environmentally sustainable goods or services; to claim a tax credit for contributions of in-kind services for the repair, maintenance, acquisition, predevelopment, rehabilitation, construction, and other capital improvements of charter schools provided by the licensed taxpayer in Hawaii or facilities administered, operated, or developed by nonprofit corporations for the benefit of charter schools. The credit shall be 10% of the value of contributions of in-kind goods and services to the Hawaii charter school facilities fund for that taxable year up to an annual maximum of \$40,000.

Credits in excess of tax liability may be applied to subsequent tax liability until exhausted. Requires claims, including any amended claims, to be filed on or before the end of the twelfth month following the taxable year for which the credit may be claimed.

Directs the charter school review panel to maintain records of taxpayers eligible for the credit and the total value of in-kind goods and services contributed by eligible taxpayers. Delineates the provisions relating to the verification of contributions and issuance of a certificate to qualified taxpayers to be filed with the department of taxation. When the total amount of certified contributions reaches \$2.5 million, the charter school review panel shall cease the issuance of certificates.

Directs the director of taxation to prepare the necessary forms to claim the credit, may require proof to claim the credit, and adopt rules pursuant to HRS chapter 91 to carry out this section.

Adds a new section to HRS chapter 302B to establish the Hawaii charter school facilities fund as a separate fund of the kanu o ka aina learning ohana, a Hawaii nonprofit corporation.

Appropriates \$2.5 million for fiscal 2009 for the Hawaii charter school facilities fund, effective July 1, 2008.

EFFECTIVE DATE: Tax years beginning after December 31, 2007

STAFF COMMENTS: This measure proposes to allow attorneys, banks and financial institutions, providers of environmentally sustainable goods and services, contractors, electricians, plumbers, pest control operators, architects, surveyors, engineers, mortgage brokers and solicitors, real estate brokers and salesman, and real estate appraisers to claim a credit for contributions of in-kind goods and services made for the benefit of charter schools.

SB 2164, SD-1 - Continued

It should be recognized that the tax system is not an efficient means to accomplish this goal. It should also be noted that since contributions to agencies of the federal, state or county governments under both state and federal income tax laws are deductible against gross income, it would appear that the adoption of this measure is unnecessary.

Care should be exercised in this area. Note well that there is no standard for determining the value of the "in-kind" contributions. While there is a cap on the amount of the credit set at \$40,000 per year per taxpayer, how much work that represents is not clear. At a rate of 10%, the maximum credit would represent \$400,000 of in-kind services contributed to this program. Does that represent one hundred hours of work or ten hours of work? It will all depend on what the taxpayer estimates as the value of his in-kind services. That time may not represent very much in the scheme of things.

On the other hand, inasmuch as the proposed credit would be granted only for contributions to public charter schools in the state, it discriminates against non-public institutions of learning. Since the current allowance for deduction of contributions made to educational institutions does not differentiate between public or private entities, the deduction is more equitable.

One of the complaints filed by charter schools is the allocation of resources from the department to run such schools does not take into account the capital necessary for facilities. As a result, the allocation of public funds merely recognizes operating costs and what funds are available must cover both the cost of programs and facilities. This is the advantage enjoyed by the traditional public school. All of the public school facilities were built with public funds, usually debt financed and generally are charged against operating costs. One alternative to addressing this disparity is to allow charter schools to use public facilities. Many of the educational facilities in the Honolulu urban core and East Honolulu go vacant or are occupied by education administrators because of declining enrollment as the center of the population moves out west or to Central Oahu. Consideration might be given to allowing charter schools to utilize these facilities as an alternative to renting or building their own facilities. Since these are students who would otherwise have been in the traditional public school, it only makes sense to utilize these facilities and ease the burden on charter schools' operating costs.

The irony of these proposals is that it proposes to reward some, but not others, for volunteering of their time and skills. The spirit of the bill is based on "volunteerism" with all parties coming together to solve this problem. If that is the case, it is questionable why some who participate will get a tax credit while others will not be compensated in a similar manner. If indeed this bill represents an effort from the community, then there is no reason to provide a tax credit for some and not others who are giving of their time, talents and materials to improve the schools and the community as a whole. Why are only these professionals singled out? Is it because they want to be paid while others volunteer? At the crux of it all, that is what the credit represents, is payment for contributions of "in-kind services." Obviously volunteerism no longer comes from the heart, but rather it comes from the pocketbook.

Digested 2/11/08



KALO

Kanu o ka 'Āina Learning 'Ōhana

Honors the Past, Addresses the Present, Serves the Future

February 11, 2008

President

*Kū Kahakalau
Ph.D.*

For the Senate Committee on Economic Development and Taxation

Vice President

Darryl Wise

February 12, 2008 hearing, 1:15 p.m., room 224

Treasurer

Nancy Levenson

Testimony in strong support of SB 2164 SD1 RELATING TO EDUCATION with proposed amendments

Secretary

Maile Zsupnik

Chair Fukunaga and members of the committee:

Member

*Barbara
Robertson*

In spite of a clear obligation under Article X, section 1 of the State Constitution to provide equitable funding for charter school facilities, this goal continues to elude the State of Hawaii. The intent of this measure is to begin constructing the fiscal, administrative and statutory infrastructure needed to facilitate innovative public-private partnerships that can leverage modest public investment and begin to address this pressing need.

Member

*Guy Kaulukukui
Ph.D.*

The Hawaii Charter School Facilities Fund is modeled after the successful Hawaii 3Rs program (and national best practices in charter school facility finance), although expanded to include capital improvement projects as well as repair and maintenance. It is intended to serve all charter schools without partiality. The language in the bill tracks that of the existing Hawaii 3Rs statute.

We would also like to offer amendments designed to address the concerns of the Attorney General and the Charter School Review Panel that the tax reporting function could pose an undue burden on the Charter School Review Panel and staff. Upon further review of tax law, it would appear that the responsibility for reporting the value of charitable donations to non-profit organizations is the responsibility of the taxpayer. Therefore, the panel should play no role in this area. Furthermore, the panel had an additional concern that they should be empowered to appoint a member to the advisory board instead of the Charter School Administrative Office. We would

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Kanu o ka 'Āina Learning 'Ōhana

Grows womb-to-tomb models of education that advance Hawaiian culture for a sustainable Hawai'i

support this change as well.

As we developed these potential amendments late on Monday, February 11, it may be too late for the Attorney General and the Charter School Review Panel to offer their formal approval for them in hearing on February 12. However, it is our hope and intention that as this measure and the House companion (HB 2561) move forward, that these changes will garner the support of these state agencies for this bill.

Technical language to implement the changes mentioned above follows.

- 1) Delete the definition of "value of contributions of in-kind goods and services" at the end of section 2, paragraph d.
- 2) Delete section 2, paragraph g in its entirety.
- 3) Section 3, paragraph d: [~~and the office shall appoint~~]
and the charter school review panel shall appoint.

Sincerely,

Taffi Wise
Executive Director