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 ECONOMIC REVITALIZATION, BUSINESS & MILITARY AFFAIRS
TESTIMONY REGARDING HB 1567
RELATING TO SKILLED NURSING FACILITIES

TESTIFIER: KURT KAWAFUCHI, DIRECTOR OF TAXATION (OR DESIGNEE)
DATE: FEBRUARY 17, 2009
TIME: 8:30AM
ROOM: 312

This measure seeks to create skilled nursing facilities to be qualify as businesses for the Enterprise Zones administered by the Department of Business, Economic Development & Tourism.

The House Committee on Health passed this measure unamended.

The Department of Taxation (Department) takes **no position** on this measure; however must **oppose the revenue loss** anticipated by this measure.

NOT FACTORED INTO EXECUTIVE BUDGET

The Department initially points out that this legislation has not been factored into the Executive Budget and has not been prioritized as a means of tax relief this legislative session. The Department cannot support the tax provision in this measure because it is not factored into the budget. The Department must be cognizant of the biennium budget and financial plan. This measure has not been factored into either. Given the forecasted decrease in revenue projections, this measure would add to the budget shortfall.

REVENUE IMPACT

The tax component of this measure will result in the following revenue losses:

- $120,000 in FY2010;
- $320,000 in FY2011:
- $400,000 in FY2012;
- $480,000 in FY2013;
- $331,800 inFY2014; and
- $51,800 in FY2015

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

REVISED: February 14, 2009

Statement of
THEODORE E. LIU
Director
Department of Business, Economic Development, and Tourism
before the
HOUSE COMMITTEE ON ECONOMIC REVITALIZATION, BUSINESS, & MILITARY AFFAIRS

Tuesday, February 17, 2009
8:30 A.M.
State Capitol, Conference Room 312

in consideration of
HB 1567
RELATING TO SKILLED NURSING FACILITIES

Chair McKelvey Vice-Chair Choy and Committee members:

The Department opposes this measure that would treat each new skilled nursing facility or facility expanding its operations outside an enterprise zone as operating within an enterprise zone for purposes of eligibility to receive benefits provided in enterprise zones. Given the current fiscal difficulties it would not be prudent to pursue enactment at this time. We defer to the Department of Taxation to ascertain the financial impact of this measure.

Hawaii's Enterprise Zones (EZ) Partnership Program was established by the Legislature in 1986 to help stimulate certain types of businesses to locate and provide employment in areas where they are needed most. At the end of 2007, a total of 199 companies were enrolled in the

EZ program. Of those enrolled companies, one percent was involved in medical research, while another half percent was involved in medical equipment repair or maintenance of assistive technology equipment used by disabled persons. Nursing homes and medical facilities are underrepresented in enterprise zones.

While we recognize the need to support medical and health care services, allowing each new skilled nursing facility or facility expanding their operations <u>outside</u> an enterprise zone to be considered as operating within an enterprise zone for purposes of eligibility to receive EZ benefits, contradicts the original intent of the program which is to stimulate business development and job creation in areas where they are needed most.

We note that the purpose of this measure is to help stimulate the development of nursing home care facilities. We would like to point out that the job creation requirement of 10% or more per year required by the Enterprise Zone law might not be met by nursing homes, thereby precluding them taking advantage of the GET exemption benefit. In addition, the GET exemption benefit are savings to customers and does not add to the nursing home's bottom line. Similarly, EZ income tax credits only apply to the bottom line if the facility is making a profit. Finally, this measure supersedes the "home rule" requirement of enterprise zones being nominated by the counties.

Should the Legislature want to extend zone benefits to new or expanding nursing home facilities, we recommend that nursing home facilities be included as an allowable business within the current Enterprise Zone Program laws. Again, should this be the case, we defer to the Dept. of Taxation to ascertain the financial impacts.

Thank you for the opportunity to offer these comments.

TESTIMONY ON BEHALF OF HB1567

Faye Lincoln, Vice-President
Policy & Government Relations
Avalon Health Care, Inc.

Hearing Date: February 17, 2009

Hearing Time: 8:30 am

Measure # 1567 Skilled Nursing Facilities; Enterprise Zone Benefits

Honorable Committee Members:

Thank you for the privilege of providing testimony on behalf of Avalon Health Care, Inc., a large provider of skilled nursing home services in Hawaii. Avalon operates and manages three facilities with 490 beds. Two facilities operate in Honolulu and one facility is managed in Hilo, Hawaii.

We are writing in **support of HB 1567 Skilled Nursing Facilities; Enterprise Zone Benefits** which proposes to create an enterprise zone for skilled nursing facilities operating in Hawaii.

This bill creates an enterprise zone for a skilled nursing facility which begins operations as a new facility or an existing facility which expands its operations. Such operations would benefit by being exempted from paying Hawaii General Excise Tax.

This bill would provide an appropriate tax incentive to develop new skilled nursing facility beds through the Certificate of Need process. Presently, the majority of facilities in the islands run an occupancy capacity between 95% and 97%. This is generally indicative of an under-bedded situation for residents who require this level of service.

Many hospitals have a back-log or waiting list of residents with general or specialty skilled nursing facility needs. They are unable to admit to such facilities when the beds are already filled to capacity. There is also a need for providing services to behavioral

health residents requiring long term care – either from community-based psychiatric hospitals, the state hospital or acute hospitals holding patients with medical needs co-existing with a psychiatric diagnosis. There are not enough available beds to provide incentives for the development of specialty services.

Skilled nursing facility (SNF) operators are interested in building new facilities or renovating old facilities into new SNF operations, but the availability of land and the cost of new construction or renovation restricts the ability to establish financially sound programs. New construction in the islands currently runs between $400 - $450 per sq. ft. A smaller 150 bed facility may be approximately 130,000 – 140,000 sq. ft. This brings the cost of a new facility between $50 - $60 million and greater for a facility with more spacious rooms and greater square footage to the building. Creation of an Enterprise Zone for SNFs would be extremely beneficial by 100% exemption from the General Excise Tax for both the Developer / Operator and Contractor.

Given the limited Medicare and state MedQuest reimbursement rates, SNFs will have extreme difficulty developing a financially viable program unless some tax incentives are available for newly created programs. Start-up SNFs also must carry a large amount of losses in the early years of operation as they build up their census to full occupancy levels. Exemption from the GET will strengthen a start-up facility financially.

Ultimately, the demand for building new beds is controlled by the State Health Development Agency (SHPDA) through their Certificate of Need program. This Division under the Department of Human Services ensures that the total number of new or expanded beds which are built is based on the current and future need of SNF capacity in the state.

Additional benefits of creating an Enterprise Zone for SNFs include:

- An 80% reduction of state income tax the first year of operations, which reduces by 10% each year for six or more years*
- An additional income tax reduction equal to 80% of annual Unemployment Insurance premiums the first year, which is reduced by 10% each year for six or more years*
- Priority building permit processing
- Zoning or building permit waivers or variances as appropriate
- Property tax adjustments
- Priority consideration for federal job training or community development funds

This bill helps to provide a needed incentive to create new beds by exempting such facilities from the excise tax. While this incentive alone will not guarantee financial success of a new facility, it will be a good start towards this goal.

- Income tax adjustments are no greater than 100% of tax due

Thank you for the opportunity to provide this testimony. If you have any further questions, please do not hesitate to contact me at (801) – 518-6565.

Sincerely,

Faye Lincoln, Vice-President