

NEIL ABERCROMBIE
Governor

MIKE MCCARTNEY
President and
Chief Executive Officer

Hawai'i Tourism Authority

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Testimony of
Mike McCartney
President and Chief Executive Officer
Hawai'i Tourism Authority
on
S.B. 769, S.D. 1
Relating to Economic Recovery

House Committee on Tourism
Monday, March 21, 2011
9:15 a.m.
Conference Room 312

The Hawaii Tourism Authority (HTA) supports S.B. 769, S.D.1, which proposes an income tax credit for hotel and resort property construction and renovation.

The HTA supports measures that provide the private sector with investment incentives to improve visitor facilities including hotel and resort facilities throughout the state. This measure would provide incentives for the owners of qualified hotel facilities to revitalize Hawaii's visitor product, and create new jobs in Hawaii's construction industry.

The HTA is guided by its Hawai'i Tourism Strategic Plan: 2005-2015, which identifies nine strategic initiatives needed to implement a shared vision of a sustainable visitor industry. The Tourism Product Development initiative includes the following direction, "develop new, and rejuvenate existing physical elements of the tourism product by supporting those who undertake such efforts through tax incentives, land use and planning policies...and other like programs." As such, the HTA supports these efforts that share a similar direction.

Thank you for the opportunity to testify on this measure.



THE RESORT GROUP

TO THE HOUSE COMMITTEE ON TOURISM

**TWENTY SIXTH LEGISLATURE
Regular Session of 2011**

**Testimony of Abbey S. Mayer, Vice President, Government Relations
THE RESORT GROUP**

In Support of SB 769, SD1, Relating to Economic Recovery

Monday, March 21, 2011, 9:15 AM -- Room 312

Aloha Chair Brower, Vice-Chair Tokioka, and Members of the Committee,

The Honolulu-based The Resort Group (TRG) acquires, master develops, repositions and markets domestic and international mixed-use and master-planned resort communities. Led by Jeffrey R. Stone, TRG's resort development projects are carefully designed to balance resident, visitor and employee needs with community interests, local cultural values and adjacent land use requirements. Current projects include Ko Olina Resort & Marina and Makaha Valley Country Club on O'ahu, Princeville at Hanalei (Kaua'i), Lands of Kapua (Big Island), the Newport Beach Hotel in California and Cape Eleuthera, Bahamas.

BACKGROUND

In 2009, in response to the 'Great Recession' and economic crisis that began in mid-2008, Senate Concurrent Resolution No. 132 (SCR 132) established a Construction Industry Task Force, composed of sixteen industry leaders and community representatives. SCR 132 requested that the Task Force determine the economic contributions of the construction industry in Hawaii and to propose actions that would help preserve and create new jobs in the local construction industry.

Recommendation 1 (Hotel/Timeshare Construction and Remodeling Tax Credit) of the SCR 132 Final Report, noted that the attacks of September 11, 2001 had a devastating effect on the Hawaii Economy. In October 2001, the Hawaii Legislature met in a special session to approve emergency measures in response to the attacks. One such measure was the enactment of Act 10, Third Special Session Laws of 2001. It amended the construction and remodeling tax credit (ACT 195 passed in 2000) from 4% refundable to 10% nonrefundable for construction and renovation costs

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incurred between January 1, 2001 and July 1, 2003 for hotels, hotel condos, timeshare facilities, apartment owner associations, and residential sectors. After July 1, 2003, the credit reverted back to the 4% refundable credit until its repeal in 2007.

Act 10 was an additional incentive to push development forward during a 36-month window by rewarding those who did with an increased credit. The purpose of this credit was to assist the visitor industry in creating and renovating projects in tourist destination areas throughout the state and to provide employment opportunities. This Act was crucial in Hawaii's economic recovery after September 11, 2001.

On March 17, 2003, Hospitality Advisors, LLC of Honolulu, Hawaii published "*Overview Analysis of the Hotel Renovation Credit*", in response to a proposal to extend the Act 10 benefits for an additional 5-year period to July 1, 2008. The Findings of this report were:

- The hotel tax credit did spur much-needed hotel renovation;
- Hotel tax credits generated additional benefits beyond tax credit given; and
- Act 195 and Act 10 helped transform and reposition Hawaii's hotel and visitor industry.

Undertaken at the request of the SCR 132 Task Force, an updated report by Premiere Realty Advisors of Honolulu, Hawaii dated November 15, 2009, presented a quantitative economic analysis of the Act 10 as a 10% refundable tax credit. The summary findings of this report were that a reenactment of Act 10:

- Would be greatly successful in instigating new construction, renovating existing projects, and generating employment;
- The State and Counties would continue to benefit far beyond the period of reenactment from the residual effects of such a measure, as the projects and improvements created would continue to generate tax revenues to the State and Counties; and
- Act 10 was previously a law and therefore, will be an easier and timelier remedy than creating a new program.

SB 769 SD1, RELATING TO ECONOMIC RECOVERY:

The original draft of SB 769 proposed a nonrefundable seven to ten percent tax credit for construction and renovations costs on hotel property incurred after December 31, 2010, through December 31, 2016. The credit, if not exhausted in the year claimed, can be carried over as credit for future years until exhausted.

The amount of credits claimed under this section would have been:

- Seven percent of the construction or renovation costs between \$1 and \$10 million; and
- Ten percent of the construction or renovation costs over \$10 to a maximum of \$100 million.

SB 769, SD1 was amended to blank out the percentage amounts and cost ranges, while shortening the effective period by two years, making the tax credit claimable on costs incurred between December 31, 2010 through December 31, 2014.

Discussion:

TRG notes that the original draft of SB 769 would reduce both the cost to the State resulting from 'lost tax revenues' and also the quantity of induced construction from the SCR 132, 10% refundable proposal.

SB 769, SD1 further reduces these potential costs of this measure to the State, by shortening the effective period of the tax credit (should credit percentages and cast ranges remain equal). TRG would note that because the bill is retroactive to December 31, 2010, the 'ramp up period' in which hotel owners and developers commit to construction and renovation projects based on the stimulus provided by the tax credit is severely reduced. Resultantly, while costs of the measure are reduced by SB 769, SD1, also reduced will be the economic stimulation that the bill is intending to provide.

TRG stands in strong support of SB 769 and notes that the incentivized induction of increased economic activity is absolutely essential for achieving long-term economic recovery and sustainability. While TRG does not now have any pending projects that would qualify for this credit, we understand through direct experience the efficacy of Act 195 and Act 10 in helping to revitalize Hawaii's construction industry at a time of historic lows. SB 769 will also lead to tourism industry improvements which will serve the entire State for years to come.

Additionally, TRG feels this measure would bring relief to a battered construction industry, especially on Neighbor Islands, that will not directly benefit from the Rail construction spending on Oahu. At a time when financing for construction and renovation projects continues to be particularly challenging, TRG feels this legislation will be a key incentive to ensure the implementation and viability of shovel-ready projects.

TRG thanks the committee for the opportunity to testify on this measure.

NEIL ABERCROMBIE
GOVERNOR

BRIAN SCHATZ
LT. GOVERNOR



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DEPARTMENT OF TAXATION
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FREDERICK D. PABLO
DIRECTOR OF TAXATION

RANDOLF L. M. BALDEMOR
DEPUTY DIRECTOR

HOUSE COMMITTEE ON TOURISM

TESTIMONY OF THE DEPARTMENT OF TAXATION REGARDING SB 769, SD 1 RELATING TO ECONOMIC RECOVERY

TESTIFIER: FREDERICK D. PABLO, DIRECTOR OF TAXATION (OR
DESIGNEE)
COMMITTEE: TOU
DATE: MARCH 21, 2011
TIME: 9:15AM
POSITION: SUPPORT INTENT

This measure provides a nonrefundable hotel and resort remodeling and renovation tax credit.

The Department of Taxation (Department) supports the intent of this measure.

The Department supports the tourism industry and the importance of the economic activity this important industry brings to Hawaii. The Department acknowledges that having modern and newly renovated rooms are an important factor in maintaining the flow of tourists to this State.

The Department supports efforts to stimulate the economy. This measure targets tax incentives at the construction industry, which is a large segment of Hawaii's economy. However, the Department opposes the aggregate for all taxpayers as difficult to administer, and lacks the resources to administer it. If an aggregate cap for all taxpayers is provided, the bill must also provide how the credit should be allocated: pro-rata, first-come, first-served, etc.

The revenue impact is indeterminate due to the amounts being blanked out. The Department presents the following historical data, which may aid the committee:

In 2005, the amount claimed for the hotel renovation tax credit was \$15.3 million (at that time the credit was a 4% refundable credit). The estimated base was \$382.5 million. Assuming that the expanded definition of "qualified hotel facility" would increase the base by 25%, the estimated new base is \$478.1 million. Applying a credit of 8.75% to the base (the average of the two rates in the original version of the bill, before the amounts were blanked out), the estimated revenue loss is \$41.8 million/year. However, the bill also contains a blanked-out aggregate cap which would be factored into any revenue loss projections.

TAXBILLSERVICE

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SUBJECT: INCOME, Hotel construction or renovation tax credit

BILL NUMBER: SB 769, SD-1

INTRODUCED BY: Senate Committee on Tourism

BRIEF SUMMARY: Adds a new section to HRS chapter 235 to allow taxpayers subject to HRS chapter 235 and HRS chapter 237D to claim a tax credit for the construction or renovation costs incurred before 1/1/15. The credit shall be ___% of the construction and renovation costs between \$___ and \$___ in the aggregate; and ___% of the construction or renovation costs over \$___ to a maximum of \$___ in the aggregate. The credit shall not be applicable to costs of construction or improvements for which another income tax credit was claimed for the taxable year. Establishes a total annual cap of tax credits of \$___ million.

The tax credit shall be available for tax years beginning after December 31, 2010 and shall not be available for tax years beginning after December 31, 2014. Renovation or construction costs financed with funds that represent government grants, government-issued loans, or property assessed clean energy financing shall not be eligible for the credit.

In the case of a partnership, S corporation, estate or trust, association of apartment owners of a qualified hotel facility, time share owners' association, or any developer of a time share project, the credit shall be based on qualified costs incurred by the entity with costs on which the credit is computed determined at the entity level. To qualify for the credit, the taxpayer shall be in compliance with all applicable federal, state, and county statutes, rules, and regulations. If a deduction is taken under IRC section 179 (with respect to election to expense depreciable business assets), no tax credit shall be allowed for such qualified costs for which the deduction was taken. The basis of eligible property for depreciation or accelerated cost recovery system purposes shall be reduced by the amount of credit allowable and claimed.

Credits in excess of a taxpayer's income tax liability shall be applied to subsequent tax liability. Claims for the credit, including any amended claims, must be filed on or before the end of the twelfth month following the close of the taxable year.

Defines "construction or renovation cost," "net income tax liability," "qualified hotel facility" and "qualified resort area" for purposes of the measure.

EFFECTIVE DATE: July 1, 2050; applicable to tax years beginning after December 31, 2010

STAFF COMMENTS: The legislature by Act 195, SLH 2000, enacted a hotel construction and renovation tax credit of 4% for hotel renovations effective for tax years beginning after 12/31/98 but before 12/31/02. Act 10 of the Third Special Session of 2001 increased the hotel renovation tax credit to 10% for construction costs incurred before 7/1/03. Act 10 also provided that the credit shall revert back to

4% on 7/1/03 and sunset on 12/31/05. This measure proposes a similar credit for construction or renovation costs incurred after December 31, 2010 and before January 1, 2015.

The original tax credit was promoted on the argument that the tax credit would be an incentive for hotels to refurbish their properties in order to remain competitive with other destinations around the world. The credit amount was set at 4% to seemingly offset the 4% general excise tax. When 9/11 hit, the momentum of the crisis fostered support for an increase in the credit to 10% to supposedly keep projects that were already in progress going. However, the governor objected and threatened to veto the sweetened credit. The legislature compromised and provided that the 10% credit would be nonrefundable.

While this measure proposes to reestablish a hotel renovation tax credit, it should be noted that no evaluation has been done to validate the effectiveness of this credit in spurring substantial renovations of hotel resort properties. While some may argue that this credit is necessary to make their upcoming renovations pencil out, one must ask whether or not it is the role of government to subsidize private investments. While the credit might be viewed as critical to a taxpayer's project or to the continued renovation of the resort plant, one must ask how long must all other taxpayers suffer the heavy burden of taxation so that this subsidy can be extended to a few?

It would be a very different picture if those who are asking for the subsidy would be willing to forgo other public services or make recommendations on how government can rein in spending, but that is not the case. Now, more than ever, lawmakers need to recognize that they need to set priorities for what precious few dollars taxpayers can part with to run state and local government. One must ask how lawmakers can provide subsidies like these while they raised the general excise tax on all other taxpayers to pay for a transit system in Honolulu? Taking care of a few taxpayers at the expense of all other taxpayers is certainly a cavalier attitude.

More importantly, if the intent of this measure is to entice hotel owners to undertake major renovations, then the sponsors do not understand what is happening to the nation's economy. In order to undertake large scale construction or renovations, either the hotel owner has to be cash rich or else have access to the credit markets. As the nation now knows, the credit markets froze beginning in late 2007 and hit a crisis at the end of 2008. The phenomenon was a major reason for the demise of Aloha Airlines and ATA which were highly dependent on credit lines to meet on-going expenditures. When the credit markets froze, there was no way to secure cash advances to meet current liabilities and the two airlines, along with thousands of other businesses, had to shut their doors.

Despite herculean efforts to thaw those credit markets and to cajole corporations that are still sitting on over a trillion dollars worth of cash to loosen up and spend that money, all has been for naught as there are still jitters about how firm a recovery is being had. Given that fact, it is doubtful that any hotel owner will undertake new renovation projects, in fact, some who had such projects underway have pulled back or completely shut down those projects for the time being. Thus, the sponsors of this and similar proposals may find this incentive useless in this environment.

That said, much to the credit of the Senate Committee on Tourism, it has called for an assessment of what hotel projects are already in the pipeline of planning, development, and financing that could take advantage of this incentive. If there is no indication that any of those projects will be able to secure the necessary credit, then a measure such as this would tie up resources that could be more effectively

allocated to other core services.

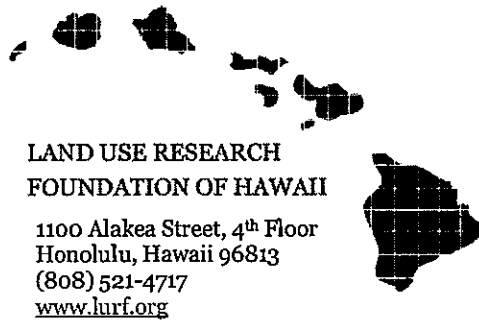
Instead of subsidizing construction in order to get construction workers off the bench, government can assist in a number of other ways. For private projects, the permitting and planning process can be accelerated. One developer recently reported that it had taken two years to subdivide two parcels into seven house lots in rural Oahu at which time the planning and permitting department deferred approval citing eight issues to be addressed regarding subdivision approval. The interest on the seller has amounted to more than \$500,000 to this point and going forward, both the buyer and seller are shelling out more than \$27,000 a month for interest alone, not to mention the other planning and engineering costs. These are costs that could be mitigated if permitting officials would just work with developers and owners in streamlining these requirements. Apparently officials are reticent to make decisions in fear that they might make the wrong decision. The result is costly delays while construction work goes begging.

In the public arena, both the state and counties need to take advantage of this window of opportunity of readily available labor and exceptionally low interest rates to undertake a massive capital improvement program. As economists on the Council on Revenues noted recently, when adjusted for inflation, the amount of public construction projects in the state is at its lowest level since statehood. Apparently the current administration has been apprised of this and has now submitted an ambitious plan to undertake a massive CIP program. Because of the length of the lead time needed to issue the debt and do the planning and engineering, it would be most beneficial if the administration implemented those projects which have already been approved and/or for which debt has already been issued by accelerating the implementation of those projects.

Finally given recent world events, the economic picture for Hawaii may be dramatically and negatively affected. Should visitor arrival from Japan take a nosedive as a result of the recent earthquake/tsunami/nuclear meltdown, Hawaii's visitor count may take a nose dive given that one out of every five visitors to Hawaii is from Japan. Given that outlook, investors may be leery of investing in the visitor plant at this time. If that is the case and credit is not available, this measure probably will have little impact in spurring on hotel construction and renovation.

Thus, rather than tinkering with the economy, lawmakers should rein back the role of government, or in other words, get out of the way and let the market lead the way to recovery. If nothing else, this measure demonstrates that lawmakers do not understand what makes the economy run and how businesses make their decisions. It is certainly sad that groups of people who have little, if any, business experience are attempting to tell business how it should be run.

Digested 3/17/11



LAND USE RESEARCH
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March 21, 2011

Representative Tom Brower, Chair and Representative James Tokioka, Vice Chair
House Committee on Tourism

Strong Support of SB 769, SD 1, Relating to Economic Recovery.
**(Establishes a tax credit for qualified hotel and resort property
construction and renovation costs incurred through December 31, 2014.)**

Monday, March 21, 2011 at 9:15 a.m. in CR

My name is Dave Arakawa, and I am the Executive Director of the Land Use Research Foundation of Hawaii (LURF), a private, non-profit research and trade association whose members include major Hawaii landowners, developers and a utility company. One of LURF's missions is to advocate for reasonable, rational and equitable land use planning, legislation and regulations that encourage well-planned economic growth and development, while safeguarding Hawaii's significant natural and cultural resources and public health and safety.

LURF is in **strong support of SB 769, SD 1**, which provides a nonrefundable tax credit for qualified hotel and resort property construction and renovation costs incurred through December 31, 2014.

BACKGROUND. SB 769, SD 1 is one of the measures recommended by the Construction Industry Task Force (CITF), established in 2009 pursuant to Senate Concurrent Resolution (SCR) No. 132 (2009) to determine the economic contributions of Hawaii's construction industry and to develop proposals for state actions to preserve and create new jobs in the local construction industry. This bill proposes a nonrefundable tax credit for construction and renovation costs on hotel and resort property incurred after December 31, 2010 and before January 1, 2015. Any credit exceeding the taxpayer's tax liability in the year claimed, may be carried over as credit for future years until exhausted. SB 769, SD 1 was patterned after Act 10 (2001 Special Session).

LURF'S POSITION. LURF strongly supports SB 769, SD 1, as the bill is intended to provide incentives to boost Hawaii's construction and visitor industries. The implementation of this legislation is necessary and warranted, as substantiated by the following:

- **SCR 132 (2009) CITF Recommendations and Justifications for the Bill.** In 2009, the chair of the CITF's Resort/Hospitality/Private Sector Committee supported a draft bill which was anticipated to be introduced in 2010 (and was conceptually identical to SB 769, SD 1), based on the following justifications:
1. The hotel and resort tax credits were successful in instigating new construction, renovating existing projects, and generating employment which contributed to the prompt economic recovery after September 11, 2001;
 2. The measure was also a profitable investment for the State and counties of Hawaii;
 3. The State and counties continue to benefit from the residual effects of Act 10 (2001) as the projects and improvements created during this time period continue to generate tax revenues; and
 4. Tax credits similar to SB 769, SD 1 were previously implemented by law (Act 10 in 2001), and will therefore be an easier and more timely remedy than creating a new program.
- **2009 Independent Quantitative Economic Analysis by Premiere Realty Advisors of Honolulu.** In 2009, Premiere Realty Advisors of Honolulu was retained to prepare an economic impact study of the CITF's proposal to re-enact Act 10 (2001). Act 10 (2001) differed from SB 769, SD 1 in the amount of the tax credit and its nonrefundable nature (the CITF proposed a 10 percent "refundable" tax credit in Act 10, while SB 769, SD 1 proposes a "non-refundable" tax credit in an amount yet to be determined, which could be carried over as credit for future years until exhausted). Despite these technical differences, the two bills are virtually identical in concept, and LURF understands that the estimated economic impact of the bills would also be similar.

The following is a summary of the analysis prepared by Premiere Realty Advisors, estimating the impact on this State resulting from the CITF proposal to reenact Act 10 (2001) as a 10% "refundable" tax credit for the period from 2010 through 2015:

- Induced construction spending estimated at \$2,002,500,000.
- Net tax cost estimated at \$46,725,000.
- Induced jobs estimated at 23,630.
- Net tax cost per induced job estimated at \$1,977.

CONCLUSION. As evidenced by the findings of the CITF and independent realty advisors, the investment incentive provided by SB 769, SD 1 are anticipated to assist greatly with the revitalization of both the visitor and construction industries in Hawaii. LURF therefore believes that the implementation of this legislation is necessary and warranted, and that the objective of this measure (i.e., to create construction jobs and improve tourism), would be well satisfied and furthered by its enactment.

Based on the above, LURF respectfully requests that **SB 769, SD 1 be favorably considered and approved by your Committee.**

Thank you for the opportunity to testify in **strong support** of this bill.



Testimony of C. Mike Kido
External Affairs
The Pacific Resource Partnership

Committee on Tourism
Representative Tom Brower, Chair
Representative James Tokioka, Vice Chair

SB 769, SD1 – RELATING TO ECONOMIC RECOVERY
Monday, March 21, 2011
9:15 AM
Conference Room 312

Chair Brower, Vice Chair Tokioka and Members of the Committee on Tourism:

My name is C. Mike Kido, External Affairs of the Pacific Resource Partnership (PRP), a labor-management consortium representing over 240 signatory contractors and the Hawaii Carpenters Union.

PRP supports SB 769, SD1 – Relating to Economic Recovery which provides a tax credit for qualified hotel and resort property construction and renovations incurred after December 31, 2010, and before January 1, 2015.

Senate Concurrent Resolution No.132 (2009) established a Construction Industry Task Force to determine the economic contributions of the construction industry in Hawaii and to develop a series of proposals for state actions to preserve as well as to create new jobs.

As an active participant in the Construction Industry Task Force, PRP believes it was and still is crucial to jump start Hawaii's economy with active pursuit construction and renovation plan that would otherwise be delayed by the prevailing financial climate.

With our economy in recession, stimulus and other initiatives are needed to counteract the negative impact on our state. A hotel construction and remodeling tax credit can provide excellent means to boost Hawaii's tourism and construction industries.

Thank you for the opportunity to share our views with you and we respectfully ask for your support on SB 769, SD1 – Relating to Economic Recovery.