

LAND USE RESEARCH
FOUNDATION OF HAWAII

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January 28, 2013

Representative Rida T.R. Cabanilla, Chair
Representative Justin H. Woodson, Vice Chair
House Committee on Housing

Comments and Concerns Relating to HB 935, Relating to the Conveyance Tax. (Increases Conveyance Tax; increases Conveyance Tax proceeds to the Rental Housing Trust Fund and Natural Area Reserve Fund.)

Monday, February 11, 2013, 10:00 a.m., in House Conference Room 329

The Land Use Research Foundation of Hawaii (LURF) is 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 appreciates the opportunity to provide **comments, concerns and opposition** to this bill.

HB 935, HD1. Originally, HB 935 proposed to:

- Substantially increase the amount of Conveyance Tax charged on all transfers or conveyance realty or any interest therein with a value of over \$2 million (including sales, leases, subleases, assignments, etc.);
- Reduce by fifteen percent the percentage of Conveyance Tax to be used and expended for general fund purposes, decreasing its total only twenty five percent;
- Direct an additional five percent to the Rental Housing Trust Fund ("RHTF"), increasing its total thirty percent; and
- Direct an additional ten per cent of Conveyance Tax proceeds to the Natural Area Reserve Fund ("NARF") for watershed protection and invasive species control, increasing its total to thirty-five percent.

The stated purpose of this bill is to increase the amount of Conveyance Tax on transfers or conveyances of certain realty or interests in realty to increase the portion of the tax's revenues directed toward NARF's watershed protection and invasive species control programs. According to the bill, the Department of Land and Natural Resources' ("DLNR") plan to protect watershed areas will require approximately \$11 million a year.

Recently, the House Committee on Water and Land amended this measure as a HD1, by:

- (1) Inserting unspecified amounts for the conveyance tax imposed on real property transactions for properties valued at \$2,000,000 or more;
- (2) Inserting unspecified amounts for the percentage of conveyance tax proceeds to be allocated to the RHTF and NARF, respectively;
- (3) Providing that the amendments relating to the amount and allocation percentage of the conveyance tax shall be repealed on June 30, 2016; and
- (4) Making technical, nonsubstantive amendments for the purposes of clarity and consistency.

LURF's Position. Over the past several decades, LURF's members are the State's leaders in providing affordable housing and are also the foremost partners with the Nature Conservancy and other organizations in setting aside, partnering and serving as stewards of natural lands for conservation and watershed purposes.

Nevertheless, while LURF strongly supports affordable housing, natural area reserves, preserving watersheds and controlling invasive species, LURF is in **strong opposition to HB 935 and recommends that it be held by this Committee**, based on, among other things, that the Legislature and Administration is on notice that it is illegal to continue the funding of these programs through the conveyance tax, which is paid by sellers of real property and has "no clear nexus or benefit-user linkage."

It appears that the intent of HB is to find additional sources of funding for RHTF and NARF by increasing Conveyance Tax revenues for the transfer of "luxury" properties. However, it changes the Conveyance Tax rates for certain transfers or conveyance of realty, without a "clear nexus"; there are other alternatives to increase the funding for RHTF and NARF; it unfairly targets and imposes substantial unintended negative consequences on local families that own land and other large *Kama`aina* landowners who have significant interests in Hawaii's real estate community; and creates a major disincentive for businesses which wish to expand or relocate their operations in Hawaii.

The proposed increases in the conveyance tax on the transfer of real estate are inappropriate, improper, and illegal, given that:

1. The Hawaii Conveyance Tax was never intended as a revenue-generating tax.

Hawaii Revised Statutes ("HRS"), Chapter 247 (Conveyance Tax), was purposefully enacted in 1966 to provide the State Department of Taxation ("DoTax") with informational data for the determination of market value of properties transferred, and to assist the DoTax in establishing real property assessed values. In short, the sole intent of the conveyance tax was originally to cover the administrative costs of collecting and assessing said informational data, which necessarily entails the recording of real estate transactions, as performed by the Bureau of Conveyances.

Since the enactment of HRS Chapter 247, however, the State Legislature has proposed, and has successfully implemented changes to the law 1) to allow application of conveyance tax revenue to a number of non-conveyance type uses (land conservation fund; rental housing trust fund; and natural area reserve fund) to the point where there is no longer any clear nexus between the benefits sought by the original Act and the charges now proposed to be levied upon property-holding entities transferring

ownership; and 2) also to increase the tax rates to the point where said revenues now appear to far exceed the initially stated purpose of the Act.

These expansions and deviations which go beyond the scope of the original intent of the conveyance tax law are concerning since the proposed bills, particularly if unlawfully targeting recent transactions involving the sale of interests in private entities which own real property in the State, could be characterized as imposing an improper penalty, hidden tax, or surcharge, which may be subject to legal challenge.

- 2. HB 935 appears to be illegal and in violation of Sections 37-52.3 and 37-52.4, Hawaii Revised Statutes (“HRS”), because it attempts to use the Conveyance Tax to increase the NARS and other similar funds which do not have a clear nexus between the benefits sought and charges made upon the users or beneficiaries of the program.** The NARF is a special fund which is subject to Sections 37-52.3 and 37-52.4 HRS. Criteria for the establishment and continuance of special and revolving funds were enacted by the 2002 Legislature through Act 178, SLH 2002, Sections 37-52.3 and 37-52.4, HRS. To be approved for continuance, a special fund must:
- serve the purpose for which it was originally established;
 - reflect a clear nexus between the benefits sought and charges made upon the users or beneficiaries of the program, as opposed to serving primarily as a means to provide the program or users with an automatic means of support that is removed from the normal budget and appropriation process;
 - provide an appropriate means of financing for the program or activity; and
 - demonstrate the capacity to be financially self-sustaining.

The first and second criteria are nearly identical to those in Act 240, SLH 1990, codified in Section 23-11, HRS, requiring the Auditor to review all legislative bills in each session to establish new special or revolving funds. The 1990 Legislature determined it was fiscally prudent to establish a review for all proposed special and revolving funds and to have the Auditor perform a one-time review of existing funds.

- 3. HB 935 is inconsistent with the recommendation of the State Auditor’s report to the Governor and legislature, which recommended the termination of the NARF.** The following information is from a report to the Governor and Legislature, entitled *“Study of the Transfer of Non-General Funds to the General Fund” A Report to the Governor and the Legislature of the State of Hawaii (“2012 Auditor’s Report”)*.

The *2012 Auditor’s Report* was prompted by House Concurrent Resolution No. 166, which requests the Auditor to conduct a study regarding the transfer of non-general funds to the general fund in light of the Hawai’i Supreme Court decision, *Hawaii Insurers Council v. Linda Lingle, Governor, State of Hawai’i, et al.* (“*Insurers Council lawsuit*”) In December 2008, the court ruled that the Legislature violated the Separation of Powers doctrine in an unconstitutional raid of an insurance special fund.

In House Concurrent Resolution No. 166, the 2011 Legislature asked the Auditor to look at the appropriateness of transferring non-general funds, including special and revolving funds, to the general fund, determine the source of the moneys, and determine whether the moneys are used for a public purpose. However, for purposes of this study, the

Auditor limited its focus to the appropriateness of using special and revolving funds as a means of financing particular programs and directing moneys accumulated in these types of funds to the general fund to address budget shortfalls in a sluggish economy.

In July 2012, the Office of the State Auditor issued its *2012 Auditor's Report* to the Governor and Legislature, which applied the criteria in Sections 37-52.3 and 37-52.4, HRS, to forty-seven (47) funds and accounts that were the subject of general fund transfer authorizations during FY2009, FY2010, and FY2011, including the NARF.

The 2012 Auditor's Report included the Auditor's analysis of the NARF and stated:

“...the Natural Area Reserve Fund has minimal linkage between the benefits and the fund revenue, which comes from conveyance taxes paid on real estate transactions. The fund supports programs such as the Natural Area Partnership and Forest Stewardship programs, projects undertaken in accordance with watershed management plans, and the Youth Conservation Corps. Individuals that pay this tax may benefit from the Natural Area Reserves program, but so do other Hawai'i residents and visitors to the state.”

The *2012 Auditor's Report* further concluded that the NARF did not meet the criteria for continuance, because was no clear link between the benefits sought and user or beneficiary charges. The Auditor further concluded that the NARF fund earmarked by the Legislature should be repealed and that the unencumbered balance should lapse to the General Fund.

In a letter dated June 18, 2012 commenting on the draft *2012 Auditor's Report*, the State Director of Finance has stated that “In general, we agree with your recommendations” and did not dispute or object to the Auditor's conclusion that the NARF did not meet the criteria for continuance as a special fund, and that the NARF should be repealed and the unencumbered balance should lapse into the General Fund.

Likewise, in a letter dated June 22, 2012 commenting on the draft 2012 Auditor's Report, the State Attorney General did not dispute or object to the Auditor's conclusion that the NARF did not meet the criteria for continuance as a special fund, and that the NARF should be repealed and the unencumbered balance should lapse into the General Fund.

4. **If HB 935, HD1 is enacted, it could result in a class action lawsuit against the State.** As noted above, the Auditor has concluded that the NARF did not meet the criteria for continuance of a special fund, because was no clear link between the benefits sought and user or beneficiary charges; and that the NARF should be repealed. Also, the State Budget Director and Attorney General, appear to concur with the Auditor's findings and recommendations regarding the NARF. If the Legislature disregards the recommendations of the State Auditor to repeal the NARF, the State could be faced with a class-action lawsuit by all persons who have paid conveyance taxes.
5. **The NARF and RHTF are so important, that they deserve annual funding through broad taxes on the public and the State General Fund – rather than through the Conveyance Tax, which targets few, is unreliable and fluctuates with the housing market.** The *2012 Auditor's Report* included the following explanation:

“Designating revenue for specific purposes flows from the “benefit theory” of public finance, which postulates that those who benefit from a program should pay for it. Revenue earmarking is more defensible when there is a clear benefit-user charge as opposed to when there is no such linkage and earmarking is used solely as a political shield to protect a program by providing it with an automatic means of support.”

The *2012 Auditor’s Report* also found that the NARF fell into the category of a “revenue earmark” with “no clear benefit-user charge” and that the NARF “is used solely as a political shield to protect a program by providing it with an automatic means of support.”

The State Auditor also found that the beneficiaries of such conservation and preservation programs are state residents as a whole, and such programs are so important that they should be supported by funding from a broader tax on all state residents, because of the broad state benefit.

6. **HB 935 is too vague and ambiguous for this Committee to approve.** HB 935 does not include any specific amounts or percentages of increases or decreases in the conveyance tax, but instead refers to “unspecified amounts.” The lack of specific amounts and percentages do not give sufficient notice or information to the public to allow it the opportunity to submit testimony for or against the bill.
7. **HB 935 may have unintended consequences**, especially to our island families who own large properties and may want to transfer property within their family. The measure will also have major negative consequences for many of Hawaii’s large *kama`aina* landowners who may be transferring large properties for agricultural farms, housing developments, environmental programs, or other developments which would serve the community and create needed employment.
8. **The proposed measure creates a significant disincentive for business in Hawaii.** At a time where Hawaii is attempting to encourage business expansion in, and attract business operations to Hawaii, HB 935 actually creates a disincentive, and will have a substantial negative impact on persuading new and existing businesses to open or expand in Hawaii, or to relocate their operations to this State. The proposed additional cost of doing business in Hawaii as a result of these bills would certainly appear to negatively outweigh any positive revenue impact resulting from the imposition of conveyance taxes pursuant to the measures.
9. **The imposition of increased conveyance taxes as proposed by HB 935 will drive up the cost of lands for agricultural production, affordable and market homes, and commercial development.**
 - The proposed imposition of the conveyance tax on transfers which affect **agricultural lands** will be passed on to farmers and other agricultural operators, making it even harder for agriculture to survive in Hawaii.
 - The proposed imposition of the conveyance tax on transfers which affect **land intended for housing developments** will be passed on to home buyers, will increase the price of homes, and will exacerbate the affordable housing problem in Hawaii.

- The proposed imposition of the conveyance tax onto transfers which affect **commercial properties** will also be passed on to small businesses, creating yet another substantial financial burden on them.

Understanding the importance of the Conveyance Tax issues raised by HB 935 and the above-referenced major unintended and overall negative impacts, **LURF respectfully requests that this bill be held in this Committee** to allow stakeholders, including, but not limited to government agencies, the public, private landowners, legal experts and other interested parties to meet and work together to come to a consensus regarding the bill's provisions and consequences.

Thank you for the opportunity to provide comments and concerns relating to this proposed measure.



Sierra Club Hawai'i Chapter

PO Box 2577, Honolulu, HI 96803
808.538.6616 hawaii.chapter@sierraclub.org

HOUSE COMMITTEE ON HOUSING

February 11, 2013, 10:00 A.M.
(Testimony is 1 page long)

TESTIMONY IN SUPPORT OF HB 935, HD1

Aloha Chair Cabanilla and Members of the Committee:

The Sierra Club, Hawaii Chapter, with over 10,000 dues paying members and supporters statewide, *supports* HB 935, HD1. This bill would provide funding for the protection of priority watershed forests and protection of Hawai'i's environmental heritage. We do ask, however, that the expiration date be removed from the measure.

The forests that provide our drinking water are just one example of "free services" that are provided by nature and consumed by the human economy--services that have immense economic value, but that go largely unrecognized and uncounted until they have been lost. Many of those services are indispensable to the people who exploit them, yet are not counted as real benefits, or as part of GNP.

Janet Abramovitz writes in WorldWatch's State of the World 1997, "A forest's watershed protection values alone can exceed the value of its timber. Forests also act as effective water pumping and recycling machinery, helping to stabilize the local climate. And through photosynthesis, plants generate life-giving oxygen and hold vast amounts of carbon in storage, which stabilizes the global climate." Unfortunately, these services aren't "free." Without proper management and protection, they will fail to provide the products we require: clean water, topsoil, and scenic areas, fresh air, and habitat.

Hawaii's watersheds also contain some of the best native Hawaiian ecosystems on state-managed land. While programs to protect these areas struggle for budget appropriations annually, resource experts estimate that at least \$11 million is needed annually to maintain the integrity of the watersheds for our children and future generations.

Our natural resource areas protect unique Hawaiian plants, animals, and ecosystems on 109,000 acres of public-trust lands. These areas include habitat for threatened and endangered species, and portions of essential watersheds that support our economy and way of life. Protection for these areas is seriously underfunded and understaffed. The result is increasing encroachment by invasive species, decrease in healthy habitat for native plants and animals, and the loss of the native essence of Hawai‘i.

We appreciate that this bill proposes a source of permanent funding and would provide support in future years. Please move this measure forward.

Mahalo for the opportunity to testify.

Ben Dyre Family Limited Partnership

Namahana Farms

Testimony of Ben Dyre Family Limited Partnership
Supporting H.B. 935 HD1 Relating to the Conveyance Tax.
House Committee on Housing
Monday, February 11, 2013, 10:00AM, Room 329

I support H.B. 935 HD1, particularly its proposal to use revenue to support watershed protection programs.

Our family is a member of the Kauai Watershed Alliance and we recognize the necessity of natural resource stewardship even during challenging financial times. We understand that the source of our pure water is a system of healthy forested watersheds which capture rain and cloud moisture and deliver it efficiently to aquifers and surface sources for subsequent consumption in our daily lives and for the benefit of our island economy.

We are a big supporter of TNC and a member of the KWA because of all the significant efforts that have been made in helping preserve our State's precious natural resources.

This bill proposes to provide additional funding for the protection of our native forests, which are the source of nearly all the islands' supply of fresh water. The watershed protection and invasive species programs supported with state funds and leveraged several times over with matching funds from county, federal and private sources help to ensure healthy, managed natural resources that are critical for isolated island chains such as Hawaii.

Hawaii's Natural Resources are unique and provide value for our people and our economy; and thus would make them a reasonable beneficiary to a portion of the funds generated by the Conveyance Tax.

Thank you for your support.

Sincerely,

Holly Dyre
General Partner
Ben Dyre Family Limited Partnership



Water has no substitute.....Conserve it

Testimony of
David R. Craddick, P.E., C.E.M.
Manager and Chief Engineer

Before the House Committee on Housing
Monday, February 11, 2013
10:00 a.m.
State Capitol, Conference Room 329

Honorable Representative Cabanilla and Members of the Committee on Housing,

I am writing to you in support of House Bill 935 HD1, particularly its proposal to use revenue to support watershed protection programs.

Our company is a member of the Kauai Watershed Alliance and we recognize the necessity of natural resource stewardship even during challenging financial times. We understand that the source of our pure water is a system of healthy forested watersheds which capture rain and cloud moisture and deliver it efficiently to aquifers and surface sources for subsequent consumption in our daily lives and for the benefit of our island economy.

This bill proposes to provide additional funding for the protection of our native forests, which are the source of nearly all the islands' supply of fresh water. The watershed protection and invasive species programs supported with state funds and leveraged several times over with matching funds from county, federal and private sources help to ensure healthy, managed natural resources that are critical for isolated island chains such as Hawaii.

Hawaii's Natural Resources are unique and provide value for our people and our economy; and thus would make them a reasonable beneficiary to a portion of the funds generated by the Conveyance Tax.

Your favorable consideration and support of HB 935 would be appreciated. Thank you for the opportunity to testify.

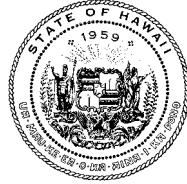
Sincerely,

A handwritten signature in black ink, appearing to read "DR Craddick".

David. R. Craddick, P.E., C.E.M.
Manager and Chief Engineer

NEIL ABERCROMBIE
GOVERNOR

SHAN TSUTSUI
LT. GOVERNOR



STATE OF HAWAII
DEPARTMENT OF TAXATION
P.O. BOX 259
HONOLULU, HAWAII 96809
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FREDERICK D. PABLO
DIRECTOR OF TAXATION

JOSHUA WISCH
DEPUTY DIRECTOR

To: The Honorable Rida T.R. Cabanilla, Chair,
and Members of the House Committee on Housing

Date: Monday, February 11, 2013

Time: 10:00 A.M.

Place: Conference Room 329, State Capitol

From: Frederick D. Pablo, Director
Department of Taxation

Re: H.B. 935, H.D. 1 Relating to the Conveyance Tax

The Department of Taxation (Department) supports H.B. 935, H.D. 1.

This measure increases the Conveyance Tax on transfers of real property with values of at least \$2 million. This measure also increases amounts deposited in the rental housing trust fund and the natural area reserve fund.

The Department defers to the Department of Budget and Finance in regards to the allocation of revenue in section 3 of this bill.

Thank you for the opportunity to provide comments.



House of Representatives
Committee on Housing
February 11, 2013
10:00 a.m., Conference Room 325
State Capitol

Testimony in Support of HB 935 HD1

Aloha Chair Cabanilla, Vice Chair Woodson, and Members of the Committee,

The Coordinating Group on Alien Pest Species (CGAPS) **supports HB 935 HD1**, *Relating to the Conveyance Tax*, which would provide critical funding for watershed protection and adds invasive species control as a specific fundable area. Watershed protection has been chronically underfunded for decades.

With more people and more industry, demand for fresh water is growing, while exponential increases in water-wasting invasive species like strawberry guava and changing climate patterns threaten the ability of forests to deliver water. Funding to increase protection for priority watersheds by fencing, ungulate and invasive plant removal is key. As high a priority is the long-term invasive species control work that is provided by biocontrol, and the preventative work done by the Invasive Species Committees and other groups. We must recognize the true cost of protecting watersheds and move the bar accordingly, and HB 935 HD1 is a great step in the right direction.

Mahalo for your consideration.

Aloha,

Christy Martin
Coordinating Group on Alien Pest Species (CGAPS)
Ph: (808) 722-0995

HOUSE COMMITTEE ON HOUSING

February 11, 2013, 10:00 A.M.

TESTIMONY IN SUPPORT OF HB 935, HD1

Aloha Chair Cabanilla and Members of the Committee,

Studies by UH professor Tom Giambelucca show that our rainfall patterns are starting to succumb to climate change. Bill Tam, the Deputy Director of the state Commission on Water Resource Management has repeatedly warned that our aquifers are not being recharged at the same rate as before and that they may be close to their maximum sustainable yield. Bill Aila, Chair of DLNR has warned that invasive species like strawberry guava are slashing the ability of the conservation forest lands to replenish the aquifers. In other words if our keiki are not to face a drinking water crisis, our watersheds desperately need money for conservation efforts – at a time when it is extremely hard to find funds for such efforts this bill would provide a guaranteed revenue stream.

Please pass this measure.

Mahalo
anthony aalto