HB 133

Provides an income tax credit for costs incurred in hotel construction or renovation

DAVID Y. IGE
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To: The Honorable Gilbert Kahele, Chair
and Members of the Senate Committee on Tourism and International Affairs

Date: Wednesday, March 18, 2015
Time: 2:45 P.M.
Place: Conference Room 225, State Capitol

From: Maria E. Zielinski, Director
Department of Taxation

Re: H.B. 133, H.D. 1, Relating to Taxation

The Department of Taxation (Department) provides the following comments regarding H.B. 133, H.D. 1 for your consideration.

H.B. 133, H.D. 1 creates a nonrefundable income tax credit of an unspecified percentage of construction or renovation costs incurred for hotel facilities, provided the construction or renovation costs are incurred during taxable years beginning after December 31, 2015, but not available for taxable years beginning after December 31, 2021.

The Department notes that the requirement under subsection (a), that the taxpayer be subject to both Hawaii Revised Statute chapters 235 (Income Tax) and 237D (Transient Accommodations Tax), may restrict the credit to a smaller number of taxpayers than the Committee intends. Many hotels are large operations with multiple subsidiaries, and it is possible that the entity incurring construction or renovation costs is not the same entity that operates the hotel as a transient accommodation.

The Department also notes that the current language of this measure would allow timeshare as well as non-timeshare accommodations to qualify for the tax credit.

Lastly, the Committee may want to consider adding pre-certification requirements for claiming the credit, which may be verified by a State agency that is capable of determining whether the proposed construction is in fact the type of activity the State wishes to incentivize.

Thank you for the opportunity to provide comments.

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David Y. Ige
Governor

Ronald Williams
Chief Executive Officer

Testimony of
Ronald Williams
President and Chief Executive Officer
Hawai'i Tourism Authority
on
H.B. No. 133, H.D.1
Relating to Taxation
Senate Committee on Tourism and International Affairs
Wednesday, March 18, 2015
2:45 p.m.
Conference Room 225

The Hawaii Tourism Authority (HTA) supports H.B. 133, H.D. 1, which proposes an income tax credit for new hotel facility construction or the renovation of hotel facilities.

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.

Mahalo for the opportunity to testify on this measure.

LAND USE RESEARCH
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March 18, 2015

Senator Gilbert Kahele, Chair
Senator J. Kalani English, Vice Chair
Senate Committee on Tourism and International Affairs

Comments, Suggested Amendments and Support of the Intent of HB 133, HD1 Relating to Taxation (Provides an income tax credit in an unspecified percentage for costs incurred in hotel construction or renovation.)

TSI Hearing: Wednesday, March 18, 2015, 2:45 p.m., Conference Room 225

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. LURF's mission 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 the intent of HB 133, HD1,** which provides an income tax credit of an unspecified percentage for costs incurred in new hotel construction for construction costs incurred after December 31, 2015, for plans, design, construction and equipment related to construction of a new hotel facility located in the State. However, LURF also recommends **an AMENDMENT of the current definition of "Hotel facility" to include "condominiums" and "time share units" which pay State transient accommodation taxes (TAT).**

Background. This bill is similar to one of the measures recommended by the 2009 Construction Industry Task Force (CITF), which was 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. It appears that portions of HB 133, HD1 were patterned after Act 10 (2001 Special Session).

LURF's Position. LURF strongly **supports the intent of HB 133, HD1,** as it provides a major incentive to implement the land use and tourism policies and plans of the State and counties, improve the quality of Hawaii's resort properties and tourism industry and strengthen Hawaii's construction and visitor industries. LURF recommends an **amendment of the current definition of "Hotel facility"** to include any building or structure that is used, or contains any room that is used, as a "condominium" as defined under section 514B-3 or "time share unit" as defined under section 514E-1, which pays the State TAT.

The implementation of this measure is necessary and warranted, and the following substantiate the benefits of this bill:

- **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 this measure), 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 somewhat similar to this measure 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 2009 proposal to re-enact Act 10 (2001). Act 10 (2001) differed from this bill in the amount of the tax credit (the CITF proposed a <u>10 percent "refundable"</u> tax credit in Act 10, while HB 133, HD1 proposes a tax credit in an <u>unspecified</u> percentage yet to be determined). Despite these technical issues, the two bills are very similar 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 in 2009 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.

<u>Conclusion</u>. LURF **<u>SUPPORTS</u> HB 133, HD1, with the <u>AMENDMENT</u> proposed herein**, and believes that the positive results of this measure, including the implementation of the land use and tourism policies and plans of the State and counties and improvement of the quality of Hawaii's resort properties and tourism industry, would be well satisfied and furthered by its enactment. In addition, as evidenced by the 2009 findings of the CITF and independent realty advisors, the investment incentive provided by this measure is anticipated to assist greatly with the strengthening of both the visitor and construction industries in Hawaii.

Based on the above, LURF respectfully requests that **HB 133, HD1 and LURF's proposed AMENDMENT to include "condominiums" and "timeshares" that pay TAT, be favorably considered and approved by your Committee.**

Thank you for the opportunity to provide our comments, requests for amendment and strong support for the intent of this bill.

Maui Hotel & Lodging
ASSOCIATION

Testimony of
Lisa H. Paulson
Executive Director
Maui Hotel & Lodging Association
on
HB133 HD1
Relating to Taxation

COMMITTEE ON TOURISM AND INTERNATIONAL AFFAIRS
Wednesday, March 18, 2015, 2:45pm
Conference Room 225

Dear Chair Kahele, Vice Chair English and Members of the Committee,

The Maui Hotel & Lodging Association (MHLA) is the legislative arm of the visitor industry. Our membership includes over 150 property and allied business members in Maui County – all of whom have an interest in the visitor industry. Collectively, MHLA's membership employs over 20,000 local residents and represents over 19,000 rooms. The visitor industry is the economic driver for Maui County. We are the largest employer of residents on the Island - directly employing approximately 40% of all residents (indirectly, the percentage increases to 75%).

MHLA **strongly supports** HB133 HD1 which provides an income tax credit for costs incurred in hotel construction or renovation.

This Bill would stimulate the revitalization many of the state's aging hotel properties. Investing in our infrastructure is critical to our ability to compete against other sun destinations, especially now when we are seeing an increased amount of competition with new resort locations and other destinations' deeply discounted air/hotel packages. New hotel construction would have the added benefit of generating construction and hospitability jobs throughout the state. Furthermore, new properties would generate additional tax revenues to support the State and Counties.

We urge you to **support** House Bill 133 HD1 as it would provide an important incentive for new investment in our visitor industry.

Thank you for the opportunity to testify.

MAUI CHAMBER OF COMMERCE

OUR BUSINESS IS MAUI BUSINESS

TESTIMONY IN SUPPORT HB133 HD1
RELATING TO TAXATION

TO THE SENATE COMMITTEE ON TOURISM AND INTERNATIONAL AFFAIRS

Hawaii State Capitol,
Conference Room 225
March 18, 2015
2:45 P.M.

Dear Chair Kahele, Vice Chair English, and Members of the Committee,

The Maui Chamber of Commerce **supports** HB133 HD1 which provides an income tax credit for costs incurred in new hotel construction.

This Bill would stimulate the revitalization many of the state's aging hotel properties. Investing in our infrastructure is critical to our ability to compete against other sun destinations, especially now when we are seeing an increased amount of competition with new resort locations and other destinations' deeply discounted air/hotel packages. New hotel construction would have the added benefit of generating construction and hospitability jobs throughout the state. Furthermore, new properties would generate additional tax revenues to support the State and Counties.

We urge you to support HB133 HD1 as it would provide an important incentive for new investment in our visitor industry.

Thank you for the opportunity to testify.

Sincerely,

Pamela Tumpap

Pamela Tumpap
President

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L E G I S L A T I V E   T A X   B I L L   S E R V I C E

TAX FOUNDATION OF HAWAII

126 Queen Street, Suite 304 Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: INCOME, Hotel construction and renovation tax credit

BILL NUMBER: HB 133, HD-1

INTRODUCED BY: House Committee on Tourism

EXECUTIVE SUMMARY: This bill establishes a hotel construction and renovation tax credit as a percentage of costs incurred on or between 1/1/16 and 12/31/21.

As a policy matter, an evaluation should be done to ascertain the effectiveness of this credit as it existed before, in order to make sure that lawmakers know that it is effective.

We also suggest technical amendments: (1) specify whether the credit is refundable or nonrefundable; and; (2) in order to prevent unintended leakage, we recommend that the credit be based on basis of the qualified hotel facility improvements as opposed to costs, so there is no double benefit (deduction plus credit) and so as to ensure that the costs are reliably linked to the improvements to real estate.

BRIEF SUMMARY: Adds a new section to HRS chapter 235 to allow taxpayers to claim a hotel construction and renovation tax credit for the construction or renovation costs incurred on or after 1/1/16 and ending before 12/31/21. The credit shall be ___% of the construction and renovation costs and shall not be applicable to costs of construction or improvements for which another income tax credit was claimed for the taxable year. Defines "construction or renovation costs" as those incurred for plans, design, construction, and equipment related to new construction, alterations, or modifications to a hotel facility located in the state.

In the case of a partnership, S corporation, estate or trust, the credit shall be determined at the entity level. 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 for state income taxes shall be reduced by the amount of credit allowable and claimed. In the alternative, the taxpayer shall treat the amount of the credit allowable and claimed as a taxable income item for the taxable year in which it is properly recognized under the method of accounting used to compute taxable income.

Also defines "net income tax liability," "qualified hotel facility" and "taxpayer" for purposes of the measure.

EFFECTIVE DATE: Upon approval; applicable to tax years beginning after December 31, 2015

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 hotel renovation costs incurred in a taxable year.

The original tax credit was promoted as 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.

This measure proposes to establish a new hotel or hotel renovation tax credit. However, no evaluation has been done to validate the effectiveness of the prior credit in spurring substantial renovations of hotel resort properties. Thus, it is difficult for taxpayers to know whether they are getting any bang for their bucks.

Some may argue that this credit is necessary to make hotel construction or renovations pencil out, but is it 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, how long must all other taxpayers suffer the heavy burden of taxation so that this subsidy can be extended to a few? 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.

More importantly, if the intent of this measure is to entice new hotel construction or hotel 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 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.

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 had amounted to more than $500,000 to that point and going forward, both the buyer and seller were 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 reluctant to make decisions in fear that they might make the wrong decision. The result is costly delays while construction work goes begging.

We also offer the following technical comments.

It is questionable whether the proposed credit is refundable or nonrefundable since it is not specified in the measure.

The measure defines “construction costs” loosely as “any costs incurred ...for plans, design, construction, and equipment related to new construction, alterations, or modifications to a hotel facility in the state.” One problem is the inclusion of “equipment,” like a bulldozer, that may be retained by the contractor after the construction is complete. Rather than focusing on costs, we suggest that the credit be awarded on *tax basis* of the new construction, alterations, or modifications to the facility, thereby limiting the credit to costs properly capitalized into the basis of the hotel facility and disallowing double benefits (taxpayer deducts the costs and claims a credit as well). A basis adjustment provision, ensuring that taxpayers are not allowed both the credit and depreciation on the same costs, already exists in the bill.

Digested 2/24/15

SAH - Subcontractors Association of Hawaii

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March 18, 2015

Testimony To: Senate Committee on Tourism and International Affairs
Senator Gilbert Kahele, Chair

Presented By: Tim Lyons
President

Subject: H.B. 133, HD 1 – RELATING TO TAXATION.

Chair Kahele and Members the Committee:

I am Tim Lyons, President of the Subcontractors Association of Hawaii. SAH is composed of nine separate and distinct subcontracting organizations including:

ELECTRICAL CONTRACTORS ASSOCIATION OF HAWAII
HAWAII FLOORING ASSOCIATION
ROOFING CONTRACTORS ASSOCIATION OF HAWAII
HAWAII WALL AND CEILING INDUSTRIES ASSOCIATION
TILE CONTRACTORS PROMOTIONAL PROGRAM
PLUMBING AND MECHANICAL CONTRACTORS ASSOCIATION OF HAWAII
SHEETMETAL CONTRACTORS ASSOCIATION OF HAWAII
PAINTING AND DECORATING CONTRACTORS ASSOCIATION
PACIFIC INSULATION CONTRACTORS ASSOCIATION

We support this bill.

Short and simple, our members are in need of work. Some say the economy is improving. Maybe. But, it certainly has not dwindled down to all sectors. Anything we can do to spur hotels to spend and build will help out hundreds of small contractors and their employees. This will benefit our members, as well as the economy.

Based on the above, we support this bill.