DAVID Y. IGE
GOVERNOR

SHAN TSUTSUI
LT. GOVERNOR

MARIA E. ZIELINSKI
DIRECTOR OF TAXATION

STATE OF HAWAII
DEPARTMENT OF TAXATION
P.O. BOX 259
HONOLULU, HAWAII 96809
PHONE NO: (808) 587-1540
FAX NO: (808) 587-1560

To: The Honorable Tom Brower, Chair
and Members of the House Committee on Tourism

Date: Wednesday, February 18, 2015
Time: 9:30 A.M.
Place: Conference Room 312, State Capitol

From: Maria E. Zielinski, Director
Department of Taxation

Re: H.B. 572, Relating to Tourism

The Department of Taxation (Department) appreciates the intent of H.B. 572 to support our State's tourism industry and provides the following comments for your consideration.

H.B. 572 creates a nonrefundable income tax credit equal to an unspecified percentage of construction or renovation costs incurred for qualified hotel facilities, provided the construction or renovation costs are incurred during taxable years beginning after December 31, 2015, but not during taxable years beginning after December 31, 2020, and further provides that the costs are pre-certified by the Department of Business, Economic Development and Tourism (DBEDT).

The Department appreciates that this measure contains several provisions the Department has requested in similar legislation introduced in previous years. In particular, the Department appreciates the inclusion of provisions requiring DBEDT to pre-certify the tax credits.

The Department does, however, have some concerns with the definition of "qualified hotel facility" in subsection (i). The definition states that "hotel" includes timeshare facilities subject to chapter 514E of the Hawaii Revised Statutes, but not units in condominium projects subject to chapter 514A or 514B. While the Department would defer to the Department of Commerce and Consumer Affairs for final analysis of what chapter a unit is governed by, it is the Department's understanding that units can be part of an association under chapter 514A or 514B and be part of a time share plan under chapter 514E simultaneously. Clarification may be needed.

Thank you for the opportunity to provide comments.

SUBJECT: INCOME, Hotel construction and renovation tax credit

BILL NUMBER: HB 572

INTRODUCED BY: Brower, Evans, Johanson, Nishimoto, Souki and 3 Democrats

EXECUTIVE SUMMARY: This bill establishes a nonrefundable hotel construction and renovation tax credit as a percentage of costs incurred on or between 1/1/16 and 12/31/20.

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. First, the requirement that a project be in compliance with all laws, rules, and regulations is not administrable at best, and should be deleted. Second, 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 nonrefundable hotel construction and renovation tax credit of the construction or renovation costs incurred on or after 1/1/16 and ending before 12/31/20. 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 qualified hotel facility.

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. Requires the taxpayer to receive certification from the department of business, economic development and tourism prior to claiming the credit.

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

EFFECTIVE DATE: July 1, 2015; 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 reestablish a 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 their upcoming 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 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 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.

Subsection (h) of the proposed new code section requires a taxpayer to be in compliance with all applicable federal, state, and county statutes, rules, and regulations. This requirement is not administrable and probably is not necessary because the other statutes, rules, and regulations probably will contain their own sanctions for violations.

Subsection (i) of the proposed new code section defines “construction or renovation costs” loosely as “any costs incurred ...for plans, design, construction, and equipment related to new construction, alternations [sic], or modifications to a qualified hotel facility.” 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 2/17/15

Maui Hotel & Lodging
ASSOCIATION

Testimony of
Lisa H. Paulson
Executive Director
Maui Hotel & Lodging Association
on
HB572
Relating to Tourism

<u>COMMITTEE ON TOURISM</u>
Wednesday, February 18, 2015, 9:30am
Room 312

Dear Chair Brower, Vice Chair Ohno 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 <u>**supports**</u> HB572 which provides an income tax credit for qualified hotel construction and renovation for taxable years beginning in the period after December 31, 2015, through December 31, 2020.

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 572 as it would provide an important incentive for additional investment in our visitor industry.

Thank you for the opportunity to testify.

1727-B Wili Pa Loop • Wailuku, HI 96793 • 808/244-8625 • 808/244-3094 fax • info@mauihla.org

SHERATON PRINCESS KAIULANI
120 Kaiulani Avenue
Honolulu, Hawaii 96815
t — 808 922 5811
f — 808 931 4577
sheraton.com

Sheraton

Testimony of
Frederick Orr
General Manager, Sheraton Princess Kaiulani Hotel
On
H.B. No. 572
Relating to Tourism
House Committee on Tourism
Wednesday, February 18, 2015
9:30 a.m.
Conference Room 312

Starwood Hotels & Resorts Hawai'i supports H.B. 572 which provides an income tax credit for qualified hotel construction and renovation for taxable years beginning in the period after December 31, 2015, through December 31, 2020.

Tourism is one of the leading economic drivers for Hawai'i and is responsible for bringing in more than $15 billion in revenue to our state. This creates nearly 200,000 jobs for Hawai'i residents, and generates significant tax revenue at the State and County levels for our community.

Tourism has led the economic recovery of our state and a healthy tourism industry will be critical to Hawai'i's continued economic rebound the coming decade.

However, Hawai'i is faced with increasing competition from numerous destinations around the world, including Mexico, the Caribbean and across Asia. These destinations have been investing billions in new hotels, attractions and visitor infrastructure in an attempt to attract more travelers.

Hawai'i has been enormously successful in positioning itself as one of the premier travel destinations in the world. However, our state has an aging visitor infrastructure that needs to be continuously renewed and refreshed if we hope to remain relevant and competitive.

The proposed tax credit will be a strong demonstration of Hawai'i's support of the tourism industry and will play a significant role in attracting outside investment into our state. There is intense competition for investment capital, and such a tax incentive could be the difference in convincing an investor to select Hawai'i instead of another destination.

In addition, from a long-term perspective, the timing is right to implement the tax credit. Although Hawai'i is currently enjoying a healthy tourism industry, attracting investment over the next five years will ensure that our tourism product is well positioned for the future and lay the foundation for decades of continued strength and success.

For these reasons we support H.B. 572.

Thank you for the opportunity to submit this testimony.

starwood
Hotels and Resorts
2155 kalakaua avenue, suite 300
honolulu, hi 96815

Testimony of
Harris Chan
Vice President, Operations - Hawaii & French Polynesia
Starwood Hotels and Resorts
On
H.B. No. 572
Relating to Tourism
House Committee on Tourism
Wednesday, February 18, 2015
9:30 a.m.
Conference Room 312

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The proposed tax credit will be a strong demonstration of Hawai'i's support of the tourism industry and will play a significant role in attracting outside investment into our state. There is intense competition for investment capital, and such a tax incentive could be the difference in convincing an investor to select Hawai'i instead of another destination. In addition, Starwood Hotels and Resorts owns two properties in Hawaii, the Westin Maui Resort & Spa and the Sheraton Kauai Resort. This tax credit will provide significant incentive and motivation to further enhance our properties therefore providing updated product to our State's tourism portfolio as well as enhancements to the destinations of Maui and Kauai. Our master plan of these properties depends on the proposed tax credit.

From a long-term perspective, the timing is right to implement the tax credit. Although Hawai'i is currently enjoying a healthy tourism industry, attracting investment over the next five years will ensure that our tourism product is well positioned for the future and lay the foundation for decades of continued strength and success.

For these reasons we support H.B. 572.

Thank you for the opportunity to submit this testimony.

starwood Hotels and Resorts Waikiki

Testimony of
Kelly Sanders
Area Managing Director Waikiki
Starwood Hotels and Resorts
On
H.B. No. 572
Relating to Tourism
House Committee on Tourism
Wednesday, February 18, 2015
9:30 a.m.
Conference Room 312

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The proposed tax credit will be a strong demonstration of Hawai'i's support of the tourism industry and will play a significant role in attracting outside investment into our state. There is intense competition for investment capital, and such a tax incentive could be the difference in convincing an investor to select Hawai'i instead of another destination.

In addition, from a long-term perspective, the timing is right to implement the tax credit. Although Hawai'i is currently enjoying a healthy tourism industry, attracting investment over the next five years will ensure that our tourism product is well positioned for the future and lay the foundation for decades of continued strength and success.

For these reasons we support H.B. 572. Thank you for the opportunity to submit this testimony.

From:	mailinglist@capitol.hawaii.gov
Sent:	Monday, February 16, 2015 12:28 PM
To:	TOUtestimony
Cc:	gm@napilikai.com
Subject:	Submitted testimony for HB572 on Feb 18, 2015 09:30AM

HB572
Submitted on: 2/16/2015
Testimony for TOU on Feb 18, 2015 09:30AM in Conference Room 312

Submitted By	Organization	Testifier Position	Present at Hearing
Gregg Nelson	Individual	Comments Only	No

Comments: Dear Committee, I urge you to consider approval of HB572 regarding a tax credit for new hotel construction and renovation of existing hotel properties. This would be a great boost to the construction industry and at the same time improve the appearance of many of our aging hotel properties. Your consideration is appreciated. Aloha Gregg Nelson

Please note that testimony submitted less than 24 hours prior to the hearing, improperly identified, or directed to the incorrect office, may not be posted online or distributed to the committee prior to the convening of the public hearing.

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HAWAI'I LODGING & TOURISM
ASSOCIATION

Testimony of George Szigeti
President & CEO
HAWAIʻI LODGING & TOURISM ASSOCIATION
House Committee on Tourism
Hearing on February 18, 2015, 9:30 A.M.
HB572 Relating to Tourism

Dear Chair Brower, Vice Chair Ohno, and Members of the Committee. My name is George Szigeti and I am the President and CEO of the Hawaiʻi Lodging & Tourism Association.

The Hawaiʻi Lodging & Tourism Association (HLTA) is a statewide association of hotels, condominiums, timeshare companies, management firms, suppliers, and other related firms that benefit from and strengthen Hawai`i's visitor industry. Our membership includes over 150 lodging properties, representing over 50,000 rooms, and over 400 other Allied members. The visitor industry was responsible for generating $14.9 billion in visitor spending in 2014 and supported 170,000 jobs statewide – we represent one of Hawai`i's largest industries and a critical sector of the economy.

On behalf of HLTA, permit me to offer this testimony regarding HB 572 Relating to Tourism, which provides an income tax credit for hotel construction and renovation for taxable years beginning in the period after December 31, 2015, through December 31, 2020.

The Hawaiʻi Lodging & Tourism Association **Strongly Supports** this measure because it provides incentives to encourage investment that would stimulate the revitalization of the state's inventory of aging hotel properties. Investing in our infrastructure is critical to our ability to compete against other destinations on a global scale (i.e. Mexico, Caribbean, etc.). Additionally, hotel construction and renovation would have the added benefit of generating construction and hospitability jobs throughout the state, as well as enhancing the economy's overall efficiency.

This measure can provide important incentives for new investment in our visitor industry and we urge its favorable consideration.

Thank you for this opportunity to testify.

Hawai`i Lodging & Tourism Association
2270 Kalakaua Avenue, Suite 1506, Honolulu, Hawaiʻi 96815 · Phone: (808) 923-0407 · Fax: (808) 924-3843
info@hawaiilodging.org · www.hawaiilodging.org

Testimony of
Gary M. Slovin / Mihoko E. Ito
on behalf of
Wyndham Vacation Ownership

DATE: February 17, 2015

TO: Representative
Chair, Committee on Tourism and International Affairs
Submitted Via TOUtestimony@capitol.hawaii.gov

RE: **H.B. 572 – Relating to Tourism**
Hearing: Wednesday, February 18, 2015 at 9:30 a.m.
Conference Room: 312

Dear Chair Brower and Members of the Committee,

We submit this testimony on behalf of Wyndham Vacation Ownership. Wyndham offers individual consumers and business-to-business customers a broad suite of hospitality products and services through its portfolio of world-renowned brands. Wyndham has a substantial presence in Hawaii through its Wyndham Vacation Resorts, WorldMark by Wyndham and Shell Vacations Club brands.

Wyndham **supports** H.B. 572, which provides an income tax credit for qualified hotel construction and renovations, including time share projects, for the five taxable years in the period beginning December 31, 2015 to December 31, 2020.

The visitor industry is a very significant part of Hawaii's economy, which creates and supports many jobs for our State. Rejuvenating Hawaii's resort inventory is critical to our State to continue to hold a place as a top tourist destination, and is essential for the industry to remain competitive in the global tourism market. Hawaii's hotel and resort infrastructure is aging, and traditional financing has not spurred necessary renovations and new construction. Providing this tax incentive will not only create new jobs, but will help create and maintain facilities that attract tourists and keep Hawaii's principal industry competitive in the global market. For the above reasons, we support this measure and respectfully request that the Committee pass it for further consideration.

Thank you for the opportunity to submit testimony in support of this measure.

Gary M. Slovin
Mihoko E. Ito
C. Mike Kido
Tiffany N. Yajima

999 Bishop Street, Floor 14
Honolulu, HI 96813
(808) 539-0840

LAND USE RESEARCH
FOUNDATION OF HAWAII

1100 Alakea Street, Suite 408
Honolulu, Hawaii 96813
(808) 521-4717
www.lurf.org

LATE

February 18, 2015

Representative Tom Brower, Chair
Representative Takashi Ohno, Vice Chair
House Committee on Tourism

Comments, Proposed Amendments and Strong Support for the intent of HB 572, Relating to Tourism; Income Tax Credit; Hotel Construction and Renovation - Provides an income tax credit for qualified hotel construction and renovation for taxable years beginning in the period after December 31, 2015, through December 31, 2020.

TOU Hearing: Wednesday, February 18, 2015, 9:30 a.m., Conference Room 312

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 provides the following **comments, proposed amendments and strong support for the intent of HB 572.** LURF strongly recommends that **the current definition of "Qualified hotel facility" should be amended to include "apartments or units in a condominium project."**

HB 572. The purpose of this bill is to provide an income tax credit for costs incurred for qualified hotel construction and renovation for taxable years beginning in the period after December 31, 2015, through December 31, 2020.

"Qualified hotel facility" is defined as a structure or structures used primarily for the business of providing transient lodging for periods of less than thirty days and which furnishes customary hotel services including but not limited to front desk, restaurant, daily maid and linen service, bell service, or telephone switchboard; including *"time share projects"* subject to chapter 514E. However, the above definition specifically excludes *"apartments or units in a condominium project"* subject to chapter 514A or 514B, that provide customary hotel services.

"Construction or renovation costs" means any costs incurred during the taxable year for plans, design, construction, and equipment related to new construction, alterations, or modifications to a qualified hotel facility.

<u>BACKGROUND</u>. HB 572 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. Portions of this measure were patterned after Act 10 (2001 Special Session).

<u>LURF'S POSITION</u>. LURF strongly **supports the intent of HB 572**, as the bill is intended to provide incentives to implement the land use and tourism plans of the state and counties and to improve the quality of Hawaii's tourism industry. However, **LURF strongly recommends that the current definition of "Qualified hotel facility" be amended to <u>include</u> *"apartments or units in a condominium project."***

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 somewhat similar to HB 133 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 HB 572 in the amount of the tax credit (the CITF proposed a 10 percent "refundable" tax credit in Act 10, while HB 572 proposes a tax credit in an unspecified percentage yet to be determined). Despite these technical issues, 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 2009 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>. As evidenced by the 2009 findings of the CITF and independent realty advisors, the tax credit incentive proposed by a similar 2009 bill was anticipated to encourage the implementation of the land use and tourism plans of the state and counties, to improve the quality of Hawaii's visitor industry and properties and to stimulate the visitor and construction industries. LURF therefore believes that the implementation of HB 572 is necessary and warranted, and that the positive results of this measure, would be well satisfied and furthered by its enactment.

Based on the above, LURF respectfully requests that HB 572 and LURF's proposed amendment to <u>include</u> *"apartments or units in a condominium project,"* be favorably considered and approved by your Committee.

Thank you for the opportunity to provide our **comments, request for amendment and strong support for the intent** of this measure.