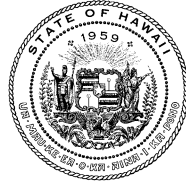


DAVID Y. IGE
GOVERNOR

JOSH GREEN M.D.
LT. GOVERNOR



RONA M. SUZUKI
DIRECTOR OF TAXATION

DAMIEN A. ELEFANTE
DEPUTY DIRECTOR

STATE OF HAWAII
DEPARTMENT OF TAXATION
P.O. BOX 259
HONOLULU, HAWAII 96809
Phone: (808) 587-1540 / Fax: (808) 587-1560
Email: Tax.Directors.Office@hawaii.gov

To: The Honorable Angus L.K. McKelvey, Chair;
The Honorable Lisa Kitagawa, Vice Chair;
and Members of the House Committee on Economic Development & Business

From: Rona M. Suzuki, Director
Department of Taxation

Re: H.B. 2605, Relating to Taxation of Real Estate Investment Trusts

Date: Wednesday, February 5, 2020

Time: 9:35 A.M.

Place: Conference Room 309, State Capitol

The Department of Taxation (Department) appreciates the intent of H.B. 2605 and provides the following comments. H.B. 2605 repeals the dividends paid deduction that real estate investment trusts (REITs) are allowed by current law. This will subject REITs' income to the Hawaii corporate income tax in the same manner as other corporations. The measure is effective upon approval and applies to taxable years beginning after December 31, 2020. The bill provides for its automatic repeal on December 31, 2023.

The Department of Business, Economic Development, and Tourism (DBEDT) is responsible for economic development, including the role of REITs. The Department is responsible for administering the tax laws in a fair, consistent, and efficient manner.

H.B. 2605 proposes to repeal the dividends paid deduction and is the most administratively efficient way in which to impose income tax on REITs.

The Department notes that it is able to administer the bill with its current effective date.

Thank you for the opportunity to provide comments.



**DEPARTMENT OF BUSINESS,
ECONOMIC DEVELOPMENT & TOURISM**

DAVID Y. IGE
GOVERNOR

MIKE MCCARTNEY
DIRECTOR

No. 1 Capitol District Building, 250 South Hotel Street, 5th Floor, Honolulu, Hawaii 96813
Mailing Address: P.O. Box 2359, Honolulu, Hawaii 96804
Web site: dbedt.hawaii.gov

Telephone: (808) 586-2355
Fax: (808) 586-2377

Statement of
MIKE MCCARTNEY
Director

Department of Business, Economic Development, and Tourism
before the

HOUSE COMMITTEE ON ECONOMIC DEVELOPMENT & BUSINESS

Wednesday, February 5, 2020
9:35 AM
State Capitol, Conference Room 309

In consideration of
HB 2605
RELATING TO TAXATION OF REAL ESTATE INVESTMENT TRUSTS.

Chair McKelvey, Vice Chair Kitagawa and Members of the Committee.

The Department of Business, Economic Development and Tourism (DBEDT) offers comments on HB2605, which would disallow dividends paid deduction for real estate investment trusts.

My comments are in the attached Policy Memorandum on the same subject dated April 26, 2019.

The policy position is from DBEDT which is from an economic development position and does not take into consideration the tax, fiscal and revenue policy, as it relates to the State of Hawaii, for that we defer to the Departments of Taxation and Budget and Finance.

Thank you for the opportunity to comment.



DEPARTMENT OF BUSINESS, ECONOMIC DEVELOPMENT & TOURISM

DAVID Y. IGE
GOVERNOR

MIKE MCCARTNEY
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April 26, 2019

The Honorable Donovan Dela Cruz
Chair, Senate Ways and Means
State Capitol, Room 208
Honolulu, Hawaii 96813

The Honorable Sylvia Luke
Chair, House Finance
State Capitol, Room 306
Honolulu, Hawaii 96813

Policy Memorandum

Relating to Taxation of Real Estate Investment Trusts

from Mike McCartney

Director, Department of Business, Economic Development & Tourism

Proposed legislation will impose state income tax on Real Estate Investment Trusts

Real Estate Investment Trusts (REIT) were established in 1960 by Congress to democratize real estate ownership so that individual investors could own income real estate or income-producing real estate assets as part of a widely held group.

From an economic development perspective, REITs appear to be more stable and a longer-term proposition for the State of Hawaii. Upgrades and improvements of older facilities and construction of new ones, like resort area hotels and timeshares, are the investment vehicles for job creation that will extend the economic supply chain into rental and commercial properties.

REITs continue to offer investment opportunities that provide long-term benefits to the State.

According to Blue Chip Economic Indicators, most of the world economies will have slower growth beginning in 2019. Hawaii's economy will experience decelerated growth in the next few years with a slower growth in nominal visitor industry spending and a drop in the real GDP growth in 2019. It is fiscally prudent to ensure that economic growth continues and that the State remains supportive for business investments.

Maintaining stable economic growth for the State is paramount to the future of Hawaii.

The Honorable Donovan Dela Cruz
The Honorable Sylvia Luke
Policy Memo
April 26, 2019
Page Two

The benefits of continuing with this federally established legislation are clear and quantifiable. REITs are an important investment vehicle for all types of investments in Hawaii. If the state income tax is imposed on a REIT there may be negative impacts to the state's economic health and the business climate, such as a reduction of general excise, property and state income taxes; decline of jobs; potential loss of future investments; and increased perception of Hawaii as a fiscally challenging state to do business.

Given the current economic conditions, the unintended consequences of imposing a corporate tax on REITs are not worth the potential benefits. Hawaii needs to be a place that is able to attract investment capital in order to create quality jobs and a sustainable economy.

DBEDT stands ready to work for you. Thank you for your consideration.

Note: The policy position is from the Department of Business, Economic Development & Tourism (DBEDT), which is from an economic development position and does not take into consideration the tax, fiscal and revenue policy, as it relates to the State of Hawaii.

c:

The Honorable David Y. Ige, Governor
Ford Fuchigami, Administrative Director
Clare Connors, Attorney General
Rod Becker, Director, Budget and Finance
Linda Takayama, Director, Department of Taxation



House Committee on Economic Development and Business
February 5, 2020 at 9:35 a.m.
State Capitol Conference Room 309

SUPPORTING HB 2605 WITH AN AMENDMENT

The Church of the Crossroads, founded in 1922, is Hawaii's first intentionally multicultural church and is committed to a mission of peace, justice, and environmental preservation.

Real Estate Investment Trusts (REITs) are the only type of for-profit corporations that do not pay Hawaii's corporate tax. This is unfair to the for-profit corporations that are required to pay the corporate tax, and it deprives the State of tax revenue.

The role of government is to create an infrastructure that supports business activity in general and to maintain a level playing field so that all businesses can compete fairly among each other.

The Hawaii State Legislature has passed legislation that conforms Hawaii tax law with the Internal Revenue Code to ease the administration of State taxes. In a number of cases, however, when the State would have been adversely affected, the Legislature made exceptions to the Internal Revenue Code.

The State adopted the federal REIT model in its entirety decades ago. By doing so, the State has, perhaps unintentionally, given a competitive advantage to REITs. They are for-profit corporations, but they do not pay a tax on their profits as other for-profit corporations do. For the sake of equity and fairness, REITs should be required to pay taxes on their profits, as do other for-profit corporations.

Applying Hawaii's corporate tax to REITs would result in an estimated \$60 million in tax revenue to the State. Those funds should be applied to reducing the enormous shortage of housing that is affordable to low- and middle-income individuals and families. Some efforts are being made to build affordable housing, but much greater efforts must be made because the shortage is so great and the cost to develop housing is so high.

The application of REIT tax revenue to affordable housing is consistent with a study entitled, "The Housing Action Plan Final Report to the State Legislature," which was funded by the Legislature and issued in 2017. Among the financing ideas is the dedication of new tax revenue for affordable/workforce housing or infrastructure, with the funds kept separate from the general fund.

This bill should be amended to separate the REIT tax revenue from the general fund and to dedicate it to the creation of affordable housing in Hawaii. We suggest the Rental Housing Revolving Fund. With that amendment, the Church of the Crossroads supports this bill.

HB-2605

Submitted on: 2/3/2020 4:12:07 PM

Testimony for EDB on 2/5/2020 9:35:00 AM

Submitted By	Organization	Testifier Position	Present at Hearing
Scott Foster	HAWAII ADVOCATES FOR CONSUMER RIGHTS	Support	No

Comments:

ALOHA,

PLEASE SUPPORT HB 2605. MAHALO.

HB-2605

Submitted on: 2/3/2020 4:37:36 PM

Testimony for EDB on 2/5/2020 9:35:00 AM

Submitted By	Organization	Testifier Position	Present at Hearing
Jon T Davidann	Faith Action	Support	No

Comments:

Sample Testimony:

Aloha, I am a member of Faith Action for Community Equity and I strongly support this bill. Please pass HB 2605 and close the loophole that exempts REITs from paying state corporate income tax. REITs already get a generous federal tax break and benefit from Hawaii's low property tax. They can operate and thrive in Hawai'i while paying state income tax, as every other Hawai'i corporation does. REITs operating in Hawaii need to do their part in supporting our community by paying their fair share of state taxes.

Mahalo for this opportunity to provide testimony in support of HB 2605.

HB-2605

Submitted on: 2/3/2020 4:49:14 PM

Testimony for EDB on 2/5/2020 9:35:00 AM

Submitted By	Organization	Testifier Position	Present at Hearing
Calvin Foo Pham	Faith Action for Community Equity	Support	No

Comments:

Aloha,

I am a member of Faith Action for Community Equity and I strongly support this bill. Please pass HB2605. The tax advantaged position of a real estate investment trust (REIT) enables businesses to have access to our resources and resident consumption without contributing back to our civic needs through taxes. If these businesses were organized by other means instead of as REITs, then they would be subject to taxes like any other business. This structure has subverted the spirit of taxation for using the services we all rely on.

Furthermore, a substantial majority of REIT shareholders do not live in Hawai'i. Therefore, the tax advantages are not even subsidizing residents of Hawai'i, but diverting revenue away from local taxpaying residents as a giveaway to investors who do not share in the civic responsibilities while using Hawai'i tourism and natural resources for profit. Even if the REITs were owned by 100% Hawai'i residents, the gains should still be realized by investors with respect to the civic resources consumed for generating their profits.

It would be more equitable to decouple from the federal system so that corporations and other business entities doing business in Hawaii pay a fair share of taxes for the resources they used in Hawai'i to generate their profits. They can continue receiving federal tax exemptions.

I pay my taxes for the income I earn and don't try to dodge my civic responsibility by turning myself into a special organization that only benefits my bottom line. REITs can and should pay their fair share too.

Mahalo.



HAWAII APPLESEED

CENTER FOR LAW & ECONOMIC JUSTICE

Testimony of the Hawai'i Appleseed Center for Law and Economic Justice
Supporting HB 2605 – Relating to Taxation of Real Estate Investment Trusts
House Committee on Economic Development & Business
Wednesday, February 5, 2020, 9:35 AM, in conference room 309

Dear Chair McKelvey, Vice Chair Kitagawa, and members of the Committee:

Thank you for the opportunity to provide testimony in **SUPPORT of HB 2605**, which would eliminate the corporate tax exemption for REITs. Right now, income produced on Hawai'i REIT property is escaping Hawai'i income tax. Typically, individuals and corporations in Hawai'i that generate income off Hawai'i real estate are paying state income tax. REITs should be no exception. Eliminating the exemption would generate an estimated \$60 million in tax revenue to fund the infrastructure, projects and programs our that community, and even REITs themselves, depend on.

A Real Estate Investment Trust or "REIT," is a corporation that owns income-producing real estate, like hotels and shopping malls. Like a mutual fund for real estate, people can purchase shares in a REIT to get a portion of the income it generates. REIT's have been granted a special tax status that exempts them from paying corporate income tax on the dividends paid to its shareholders.

REITs suggest that the exemption is appropriate because REIT shareholders pay income tax. However, while REITs own approximately \$17 billion worth of real estate in Hawai'i—more than any other state on a per capita basis—we have relatively few residents who are REIT shareholders, ranking 40th in the nation for the number of REIT shareholders as a percentage of the population. That means that a lot of REIT money is going out of our state, and only a little is remaining in. An estimated \$1 billion in profits is created in Hawai'i on Hawai'i REIT property, and a significant portion of it is escaping Hawai'i income tax.

REITs can still operate and thrive in Hawai'i, even if required to pay their share of taxes needed to build a strong Hawai'i for everyone. If the Hawai'i state corporate income tax exemption were eliminated, REITs would still receive generous federal tax exemptions, and they would continue to benefit from Hawai'i's extraordinarily low property tax rate. This bill would ensure that REITs start paying their fair share of Hawai'i income taxes to help support the communities in which they operate.

Mahalo for your consideration of this testimony.

The Hawai'i Appleseed Center for Law and Economic Justice is committed to a more socially just Hawai'i, where everyone has genuine opportunities to achieve economic security and fulfill their potential. We change systems that perpetuate inequality and injustice through policy development, advocacy, and coalition building.

February 3, 2020

Hearing Date: February 5, 2020

Time: 9:35 A.M.

Place: Conference Room 309

The Honorable Angus L.K. McKelvey, Chair

The Honorable Lisa Kitagawa, Vice Chair

House Committee on Economic Development & Business

Re: Testimony *Opposing* Repeal of the REIT Dividends Paid Deduction – HB 2605

Dear Chair McKelvey, Vice Chair Kitagawa, and Members of the Committee on Economic Development & Business:

My name is Tim Scott and I am Public Storage's Tax Counsel. Public Storage *strongly opposes* HB 2605, which would repeal the dividends paid deduction for real estate investment trusts (REITs) operating in Hawaii for 2021 and 2022.

Public Storage and Hawaii. Public Storage is a REIT that is the largest owner and operator of self-storage facilities in the United States, with over 171 million rentable square feet of real estate in 38 states. We have nearly 2,500 facilities and 1.4 million customers in the United States and we own 11 facilities in Hawaii. In 2019, those Hawaii properties generated more than \$31.8 million of gross revenue and we paid the state over \$1.4 million of general excise tax. For the 2019/2020 fiscal year, we will pay real estate taxes in Hawaii of more than \$2.25 million.

REITs and “Pass Through” Taxation. REITs were designed by Congress to distribute their taxable income to their shareholders, who then report and pay state and federal tax on those dividends. Our shareholders in Hawaii are taxable by the state on the full amount of our dividends, not just the very limited portion of those dividends attributable to the 11 properties we have in the state (compared to our almost 2,500 properties across the nation). This means that Hawaii benefits from the REIT regime because Hawaii shareholders are taxed on all REIT distributed income.¹

It is unfair to compare REITs to separately taxable regular corporations that are not required to distribute their income. The fact that REITs *must* distribute their income makes “pass-through” taxation (*i.e.*, no entity level tax) perfectly appropriate for REITs, and that treatment is even more suitable for REITs than it is with other pass-through entities such as LLCs, partnerships, or S corporations. Hawaii accords those other entities pass-through treatment, even though they are not required to distribute their income to their owners.

¹ We are confident that investors in Hawaii directly and indirectly hold significant PSA shares, but we cannot specifically identify our shareholders in Hawaii. Our common stock is traded publicly on the New York Stock Exchange under the symbol PSA. Publicly traded companies typically cannot identify their actual beneficial shareholders, as most publicly traded stock is held by depositaries in street name. Nareit analysis has suggested that about 44% of Hawaii households own REIT stock directly and/or through mutual funds or retirements accounts.

Simply a Tax Increase, Causing Double Taxation. The bill would impose new taxes on REITs operating in Hawaii (but not other pass-through entities). Those taxes would be an added cost of doing business in the state, and REITs would be expected to pass the cost along to Hawaii residents using the REITs' properties. The bill also will double tax REIT shareholders, but not owners of other pass-through entities.

Chasing REITs Away, Adverse Ripple Effects. While apparently motivated by an effort to raise added tax revenue, the bill can be expected to have the opposite effect. Although proponents of similar bills have offered unsupported estimates of very large increased annual tax collections, Hawaii's Department of Taxation reported that a similar prior bill only would produce collections of about \$2.2 million in its first year, with perhaps \$10 million per year afterwards. The Department also noted that REITs might offset their tax liabilities through tax planning or with allowable deductions. Others have projected that a repeal of the dividends paid deduction would jeopardize substantial general excise tax revenues, potentially resulting in a net loss of tax revenue for Hawaii.

Enacting such an anti-business tax would strongly incentivize REITs to reduce or avoid future investment in, and possibly redirect investments away from, the state. This could be expected to have adverse long term effects on the Hawaii economy and the state's tax collections. An economic study prepared for Nareit by Paul H. Brewbaker, PhD., CBE in December 2015 suggested that by repealing the dividends paid deduction, Hawaii could lose more revenue from foregone economic activity than might be gained in taxes payable by REITs. Another important consideration for maintaining REIT investment is that REITs are structured to hold investments for the long term and become lasting members of the community (REITs do not "flip" properties for quick profits).

Breaking the Mold; Inconsistent with Federal and Other State Treatment. Enactment of HB 2605 would make REITs separately taxable in Hawaii, imposing a double tax regime that is completely contrary to the accepted federal and state tax treatment of REITs. No state that imposes income tax upon REITs (other than New Hampshire) denies the dividends paid deduction as proposed by HB 2605. Indeed, over the past decade or so, a number of states (*e.g.*, Idaho, Louisiana, New Jersey, North Carolina, and Rhode Island) have examined, and then rejected, legislation that would have disallowed a widely-held REIT's dividends paid deduction in those states.

Strong Recommendation: Do NOT Move this Bill Forward. We believe Public Storage and other REITs have been, and can continue to be, positive forces in the Hawaii economy. For the reasons outlined above, Hawaii should decline to enact this bill, so that the dividends paid deduction for widely-held REITs will continue. We respectfully request that you do *not* move forward HB 2605.

Very truly yours,



A. Timothy Scott
Tax Counsel of Public Storage
tscott@publicstorage.com
818.244.8080, extension 1286

cc: Department of Taxation
Department of Business, Economic Development & Tourism



HB 2605, RELATING TO TAXATION OF REAL ESTATE INVESTMENT TRUSTS

FEBRUARY 5, 2020 · HOUSE ECONOMIC
DEVELOPMENT AND BUSINESS COMMITTEE ·
CHAIR REP. ANGUS L.K. MCKELVEY

POSITION: Support.

RATIONALE: IMUAlliance supports HB 2605, relating to taxation of real estate investment trusts, which disallows dividends paid deduction for real estate investment trusts and applies to taxable years beginning after 12/31/2020. Sunsets 12/31/2023.

Under state taxation law, REITs are currently afforded an exemption from paying corporate income taxes on dividends paid to shareholders. REIT shareholders, however, pay federal and state income taxes on their earnings from the REIT in which they have invested. Unfortunately, since most shareholders of Hawai'i REITs don't live in the Aloha State, they pay income taxes in other locations (if such income is subject to taxation in the states in which they reside, which it often is not). Thus, income generated from Hawai'i properties is being taxed elsewhere, if at all, sending sorely needed revenue for local schools, infrastructure, climate change mitigation, human and social services, and affordable housing outside of our shores.

Eliminating REIT dividend deductions will uplift Hawai'i's people. Over 30 REITs operate in Hawai'i, the most prominent of which is Alexander and Baldwin. Collectively, Hawai'i REITs own roughly \$17 billion worth of real estate and produce almost \$1 billion in dividend income exempt from the corporate income tax, amounting to over \$50 million in lost tax revenue—a number that will only increase over time, as real estate values continue to soar.

HB-2605

Submitted on: 2/3/2020 11:14:59 PM

Testimony for EDB on 2/5/2020 9:35:00 AM

Submitted By	Organization	Testifier Position	Present at Hearing
Robert H Stiver	Faith Action for Community Equity	Support	No

Comments:

Let's get "real": REITS REAL!

I'm from Pearl City and am a member of Faith Action for Community Equity. I strongly support this bill. It is "really get real" time to pass HB 2605 and close the loophole that exempts REITs from paying state corporate income tax. REITs already get a generous federal tax break, and they benefit from Hawaii's low property tax. Naturally they'll lobby against HB 2605; but they can manage to thrive in Hawai'i while paying state income tax, as does every other Hawai'i corporation and business. REITs operating in Hawaii must do their part to support our community in a real/right/REIT way by paying their fair share of state taxes! It's the "community equity" thing to do! Just do it!

Mahalo for allowing me to provide "Get Real!" testimony in support of HB 2605.

HB-2605

Submitted on: 2/4/2020 1:19:52 AM

Testimony for EDB on 2/5/2020 9:35:00 AM

Submitted By	Organization	Testifier Position	Present at Hearing
Evelyn Aczon Hao	Faith Action for Community Equity	Support	Yes

Comments:

Aloha, Chair McKelvey and members of the House Finance Committee

I am Evelyn Hao, President of Faith Action for Community Equity, an organization of multiple faith traditions and community action groups.

Faith Action supports HB2605 because it requires that Real Estate Investment Trusts pay their fair share of state taxes. Right now, Real Estate Investment Trusts (REITs) are exempt from state taxes because of a loophole in our state law. (Hawaii non-REIT companies, in contrast, pay their fair share of state taxes.)

That loophole allows REITs shareholders to pay income taxes in the state or country where they live. Unfortunately, 99% of shareholders of REITs in Hawaii are *not* from Hawaii, so those taxes do not stay in Hawaii. A 2016 DBEDT study estimated the revenue from a REITS tax to be in the neighborhood of \$60 million a year. It can be much higher now in 2020.

HB 2605 proposes to close that loophole to bring those Hawaii dollars back here where they belong, where they can be used for affordable housing, public education, long term kupuna care, infrastructure, prison reform, child care/early education, and other growing needs.

Some examples of local REITs are Ala Moana Shopping Center, Pearlridge Shopping Center, Hilton Hawaiian Village, Hilton Waikoloa, International Marketplace, and Alexander and Baldwin.

Last year, the REITS lobby, including NAREIT (the national REIT advocate), spent a huge budget spreading fear of the negative economic effects of the REITs legislation. However, our legislature passed the bill resoundingly. Unfortunately, the Governor vetoed it.

This year, we hope the outcome will be different.

There are over 55 REITs in Hawaii and the number is growing. Why? Because Hawaii is Hawaii. According to a NAREIT report from www.reitsacrossamerica.com, Hawaii is one

of the best states for REIT investment. Hawaii has the highest REIT asset value per capita; and it also happens to have the 14th highest value per REIT-owned property and the 12th highest rate of REIT asset value growth from 2014-2017, well ahead of larger states like Colorado, Illinois, and Texas. Hawaii's REIT asset value growth rate is over 10 percent higher than the national average.

REITs and other companies will continue to invest in Hawaii properties regardless of the taxes because Hawaii's properties are unique and uniquely valuable!

We, in Hawaii, are at a turning point. We can continue on the same path or we can realize that our residents are truly important. There really is no end to the needed projects to improve the quality of life for all.

Please pass this bill. We at Faith Action would, of course, prefer the funds to be earmarked for affordable housing, but really, we just want the bill passed and eventually made into law.

Thank you for your consideration.

WRITTEN TESTIMONY OF

**JEFFREY S. CLARK
SVP-TAX & RISK MANAGEMENT
HOST HOTELS & RESORTS, INC.**

IN OPPOSITION TO HB 2605

**BEFORE THE HAWAII HOUSE
COMMITTEE ON ECONOMIC DEVELOPMENT & BUSINESS**

**THE HONORABLE ANGUS L.K. MCKELVEY, CHAIR
THE HONORABLE LISA KITAGAWA, VICE CHAIR**

**HEARING ON HB 2605
FEBRUARY 5, 2020
9:35 A.M.**

Thank you for the opportunity to submit this testimony in opposition to HB 2605 on behalf of Host Hotels & Resorts, Inc. (Host). Host is the largest lodging real estate investment trust (REIT) and one of the largest owners of luxury and upper-upscale hotels. The Company is headquartered in Bethesda, Maryland and is traded on the New York Stock Exchange. Host owns 80 hotels throughout the U.S., Canada and Brazil, including four hotels in Hawaii. Host strongly opposes, and asks you to hold, HB 2605.

In addition, Host would like to emphasize that the federal tax law requirements of a hotel REIT like Host lead to the doubling or tripling of the liability for Hawaii general excise tax (GET) as compared with non-REIT hotel owners.

REITs are subject to federal income tax law requirements that do not apply to other forms of property owners. As relevant here, at least 75% of the annual gross income of a REIT must consist of “rents”. Hotel room charges are not considered to be “rents” for this purpose. As a result, federal income tax law requires hotel REITs to:

- Lease their hotels to a third party or to a taxable subsidiary of the REIT, and
- If leased to a taxable subsidiary of the REIT, the subsidiary must hire an independent third party operator to operate and manage the hotel.

Again, these requirements do not apply to non-REIT hotel owners.

Hawaii imposes GET not only on the room charges and other hotel operating income earned by the hotel from guests, but also on the rent received by the REIT from the taxable subsidiary and on the management fee paid to the operator by the taxable subsidiary. Again, this additional GET is not imposed on a non-REIT hotel owner. As a result, GET is imposed on at least three levels of income of a hotel owned in a REIT structure: the room charges and other operating income received from guests, the rent received by the REIT from the taxable subsidiary, and the management fee paid by the taxable subsidiary to the hotel operator.

For example, Host leases its four hotels in Hawaii, the Fairmont Kea Lani on Maui, the Hyatt Regency Maui Resort & Spa, the Andaz Maui, and the Hyatt Place Waikiki Beach to a taxable subsidiary, and the taxable subsidiary hires independent third party operators (Fairmont and Hyatt) to operate and manage its four hotels. The **additional annual GET liability of approximately \$6-\$8 million** paid to Hawaii for each of 2017, 2018, and 2019 attributable to the rents received by the REIT from the taxable subsidiary and the management fees paid by the taxable subsidiary to Fairmont and Hyatt would not have been paid if the same entity were both the owner and the operator of the hotels. Because the GET is a gross receipts, rather than a net income, tax, it is a much more reliable source of revenue for the State. It also is a much greater source of revenue to the State than the corporate income tax. The enactment of HB 2605 immediately would risk elimination of this extremely valuable source of GET revenue to the State.

Because of these unique requirements applicable to hotel REITs, the State received more than \$16 million of GET in 2018 alone from hotel REITs that own hotels in Hawaii that non-REIT hotel owners do not incur. Yet the proponents of HB 2605 claim that we operate tax-free in Hawaii!

Why own hotels in a REIT structure if it results in more aggregate tax than a non-REIT hotel owner-operator? The simple answer is that the ownership of hotels on the one hand and operating and managing the hotels on the other hand require different knowledge, experience, and expertise and separating the hotel ownership from the hotel operations and management creates more value both for the investors in the REIT and the investors in the hotel operator/manager. As an additional benefit, this separation of ownership and operations/management also creates millions of dollars of tax revenues to, and many jobs, in, this State. This creates a win-win situation, all of which immediately could be jeopardized by the

enactment of HB 2605. However, if HB 2605 is enacted, lodging REITs like Host would need to evaluate whether or not to retain their current ownership structure or to change it in order to offset the State corporate income taxes that the legislation would impose.

The estimate of \$16 million of incremental GET generated by hotel REITs which could be eliminated if the hotel ownership were changed to a REIT's taxable subsidiary or another non-REIT owner rather than the REIT itself should be compared to the Department of Taxation's 2019 determination that repealing a REIT's dividends paid deduction would raise no more than \$10 million per year. Then-Director of DoTax explained on a Hawaii Public Radio interview on April 4, 2019 (beginning at 10:10 in the recording), regarding similar legislation, that even this maximum amount does not contemplate basic planning opportunities that could be employed such as increased leverage or claiming tax credits to which a taxpayer already is entitled and that other non-REITs claim. It makes little sense to jeopardize jobs by scaring off needed investment in Hawaii, especially when the net result (even apart from the macroeconomic losses due to less investment in Hawaii) in terms of both corporate income taxes and GET is a LOSS to Hawaii.

As previously stated, Host Hotels & Resorts, Inc. currently owns four hotels in Hawaii, Hyatt Regency Maui on Kaanapali Beach, Andaz Maui at Wailea Resort, Fairmont Kea Lani, Maui and Hyatt Place Waikiki Beach. A key part of our disciplined approach to capital allocation is to make renewal and replacement capital expenditures that maintain the quality and competitiveness of our hotels. Enactment of HB 2605 would create a strong disincentive for us to employ this approach at our hotels in Hawaii. It would force us to revisit our plans to begin major renovation work at the Fairmont Kea Lani scheduled for 2021, discontinue our ground-up new construction of luxury villas at the Andaz Maui, as well as serve to discourage future investments in our hotels, potentially affecting hundreds of local jobs.

Accordingly, Host respectfully asks the Committee to hold HB 2605.



February 4, 2020

The Honorable Angus L.K. McKelvey, Chair
The Honorable. Lisa Kitagawa, Vice Chair
Committee on Economic Development and Business
State Capitol
415 South Beretania Street
Honolulu, HI 96813

RE: SB 2605/Hearing on February 5, 2020

Dear Chair McKelvey, Vice Chair Lisa Kitagawa and Members of the Committee:

On behalf of Simon Property Group (Simon), thank you for the opportunity to submit this testimony in strong opposition to SB 2605. Simon is a publicly traded real estate investment trust (REIT). We own, develop and manage premier shopping, dining, entertainment and mixed-use destinations, including Waikēle Premium Outlets in Waipahu. As of September 30, 2019, we owned or held an interest in 204 income producing properties in the United States, which consisted of 106 malls, 69 Premium Outlets, a number of other retail properties in 37 states and Puerto Rico. We also own a number of overseas properties.

SB 2605 would eliminate the REIT dividends paid deduction (DPD), contrary to federal law and the laws of virtually every state with a corporate income tax.

Modeled after mutual funds, Congress created REITs in 1960 to provide a way for ordinary Americans to combine their capital in order to invest in professionally-managed, income producing real estate with a single level of taxation. In the past, such investment was generally limited to wealthy investors through partnerships. Unlike other real estate owners, as a REIT, we must meet strict asset, income, and operational tests to ensure that we are a widely-held, real estate-focused company. Unlike other real estate owners, but like mutual funds, we can't retain our earnings. We must distribute at least 90% of our taxable income to shareholders. If we satisfy this distribution requirement as well as the other REIT rules, we are entitled to claim a DPD. We must pay corporate tax on an income we retain.

Like other REITs, we invest for the long-term. We have owned the Waikēle Premium Outlets since 2004. Since we've owned this property, we have invested over \$95 million to improve the



property. This investment has improved the property's value, allowing it to generate about \$1.4 million annually in property taxes and \$1.5 million annually in general excise taxes.

As a publicly traded REIT that invests in multiple states and throughout the world, we must consider the local business climate as a factor in terms of where to invest, and to continue to invest, capital. Enactment of this bill would lead to double taxation of our shareholders and would make Hawaii a less attractive place to invest, not just for Simon, but for other investors who may view its enactment as meant to discourage future investment, thereby jeopardizing jobs and future revenues in the State. Investments in virtually all other states would not be subject to this second level of tax, so SB 2605 would make it more likely that we would invest outside of Hawaii. Please consider the important contributions that REITs have made in Hawaii. We respectfully ask that you hold SB 2605.

Thank you again for the opportunity to submit this testimony.

Sincerely,

Desiree A. Mosiman
Manager
Waikēle Premium Outlets

February 4, 2020

Honorable Angus L.K. McKelvey, Chair
Honorable Lisa Kitagawa, Vice Chair
Committee on Economic Development & Business
State Capitol (conference room 309)
415 South Beretania Street
Honolulu, Hawaii 96813

Re: **Testimony in Opposition to House Bill 2605 relating to real estate investment trusts**

Dear Chair McKelvey, Vice-Chair Kitagawa and Committee Members:

On behalf of Taubman Centers, thank you for the opportunity to provide our testimony in **opposition** to House Bill No. 2605, which is being heard by the Committee on Economic Development & Business on February 5, 2020 at 9:35 am. HB No. 2605 would disallow the dividend paid deduction for real estate investment trusts (“REITs”).

REITs are responsible for a significant amount of economic activity in Hawaii and HB No. 2605 that increases state income taxation of REITs would be a policy change that could discourage future investment by REITs in Hawaii, stifling the availability of capital and putting Hawaii at a competitive disadvantage versus virtually every other state when trying to attract capital for investment. Because investments by REITs generate so much economic activity and create so many local jobs in the State, disallowing the deduction for dividends paid could not only hurt workers in Hawaii, over the long run, it ultimately may result in less tax revenue for the State as it makes Hawaii unattractive for investment by REITs resulting in less economic activity.

Taubman Centers alone invested over \$475 million for the redevelopment of International Market Place. Our shopping center pays annually over \$1.7 million in general excise tax and over \$3.7 million in property taxes. To date we have paid in total over \$1.5 million in local conveyance taxes. During the development of the center it resulted in employment of an estimated 1,000 construction jobs and after opening it created an estimated 1,600 permanent jobs (including employment by tenants). This generated both general excise tax revenues from construction work and individual income tax revenues from both the construction and permanent jobs. Please see page three for the economic benefits in Hawaii created by the REIT industry as a whole.

Taubman Centers in Hawaii

Taubman Centers is a publicly owned REIT engaged in the ownership, operation, management, development and leasing of 26 regional, super-regional and outlet shopping centers in the U.S. and Asia. We completed construction to redevelop International Market Place in Waikiki, Honolulu in August of 2016 for a total cost of over \$475 million. The construction began in 2014 with Queen Emma Land Company and our partner Coastwood Capital Group. The shopping center offers 86 retailers and 8 restaurants. It is designed to celebrate the rich history of the site and honor Queen Emma's legacy, while adding vitality and appeal to Waikiki for tourists and kama'āina alike. We are very excited about the center and are proud to be a part of the community.

REIT Tax Treatment

We are organized, owned and operated in a manner to qualify as a REIT under the Internal Revenue Code for federal income tax purposes. A REIT is a conduit vehicle designed to allow many small investors to participate in real estate development and ownership. REITs are also owned by institutions comprised of state and local pension funds and 401K individual retirement plans. Some of the requirements to qualify as a REIT include (1) ownership by at least 100 shareholders, (2) a prohibition on being closely held and controlled by limiting ownership by five or fewer persons to no more than a 50% interest in the REIT, (3) meeting certain asset and income tests to ensure we are primarily invested in real estate and operate it for rental purposes as a long term investor, and (4) paying out all of our taxable income as cash dividends to our shareholders which is not required by most other entity forms such as partnerships, LLCs and other corporations. Failure to meet these requirements results in losing our REIT tax status or in some circumstances harsh penalties like a prohibited transaction tax for not holding property as a long term investor in a rental real estate business. For meeting these stringent tests, Taubman Centers, like all REITs, is entitled to a deduction for dividends paid to our shareholders to reduce our taxable income. It is this deduction afforded in the federal tax law and permitted by virtually all other states that HB No. 2605 would eliminate and disallow for Hawaii corporate income taxation.

Because of the forced dividend requirement to distribute all of its taxable income, a REIT's taxable income is effectively taxed at the shareholder level by the state taxing the shareholder's dividend income in their state of residence. This allows for a single level of taxation at the shareholder level and no double taxation (i.e., it prevents taxation at both the entity level and again at the shareholder level) and is consistent with the treatment of investors in mutual funds that are treated as regulated investment companies for tax purposes. For REITs, state income taxation

based on the shareholder's residence is the uniform tax treatment in virtually all states that impose an income based tax system. This results in state income taxation by Hawaii on dividends received by Hawaii residents who are shareholders in REITs that may own property and operations outside of the State.¹

REIT Economic Benefits in Hawaii

Approximately 80 REITs have invested in commercial real estate in Hawaii and are responsible for significant economic activity in the construction industry, resort industry, restaurant and retail industry, office and industrial leasing and others.² Taubman alone invested over \$475 million for the redevelopment of International Market Place. In addition, it will continue to require investment to fund significant capital expenditures on a recurring annual basis to maintain the property to our standards and provide the highest quality shopping destination for our shoppers and tenants.

Such business activity generates substantial economic benefit for Hawaii, including providing jobs, as well as significant tax revenues for the State government. The tax revenues include substantial general excise taxes on rents from tenants, on the sale of goods and services at retail by the tenants, and on construction activities. For local governments the business activity generates property and conveyance taxes.

In year 2015 REITs were associated with more than 11,700 jobs representing labor earnings of nearly \$500 million and \$95 million in tax revenue in Hawaii. And in the past five years REIT funded construction activity is estimated to have generated \$3 billion in Hawaii GDP.
3

¹ More than 9,300 individual investors in Hawaii receive \$30 million in dividend each year
Brewbaker, P.H., Ph.D., CBE. (2015, December). *Economic Impacts of Real Estate Investment Trusts in Hawaii*
(Prepared for the National Association of Real Estate Investment Trusts® (NAREIT))

² Brewbaker, P.H., Ph.D., CBE. (2015, December). *Economic Impacts of Real Estate Investment Trusts in Hawaii*
(Prepared for the National Association of Real Estate Investment Trusts® (NAREIT))

³ *ibid*

Hawaii residents own an estimated \$2.5 billion in real estate equity through REITs, mutual funds and exchange traded funds that distribute more than \$105 million in REIT dividends annually. Approximately 9,300 individual investors in Hawaii receive \$30 million each year in REIT distributions.⁴ HB No. 2605 resulting in double taxation to REIT profits (once at the REIT level and again at the shareholder level) will affect after tax return on investment of Hawaii residents.

For more information about REITs in Hawaii please visit www.thereitwayhawaii.com.

As previously mentioned, such a policy change in state taxation of REITs could discourage future investment by REITs in Hawaii, stifling the availability of capital and putting Hawaii at a competitive disadvantage versus virtually every other state when trying to attract capital for investment. Because investments by REITs generate so much economic activity and create so many local jobs in the State, disallowing the deduction for dividends paid could not only hurt workers in Hawaii, over the long run, it ultimately may result in less tax revenue for the State as its makes Hawaii unattractive for investment by REITs resulting in less economic activity.

For the foregoing reasons, we respectfully ask the Committee on Economic Development & Business to hold HB 2605.

Thank you for your consideration of our testimony.

Very truly yours,



Simon J. Leopold
Executive Vice President, Chief Financial
Officer and Treasurer
Taubman Centers, Inc

⁴ ibid



COMMERCIAL REAL ESTATE
DEVELOPMENT ASSOCIATION
HAWAII CHAPTER

February 4, 2020

The Honorable Angus L.K. McKelvey, Chair
The Honorable Lisa Kitagawa, Vice Chair
Members of the House Committee on
Economic Development & Business
Thirtieth Legislature
Regular Session of 2020

RE: **HB 2605 – RELATING TO TAXATION OF REAL ESTATE INVESTMENT TRUSTS**

Hearing Date – February 5, 2020 at 9:35 a.m.

Aloha Chair McKelvey and members of the committee,

Thank you for allowing NAIOP Hawaii to submit testimony in **OPPOSITION** to HB 2605 – Relating to Taxation of Real Estate Investment Trusts. NAIOP Hawaii is the Hawaii chapter of the nation's leading organization for office, industrial, retail, residential and mixed-use real estate. NAIOP Hawaii has over 200 members in the State including local developers, owners, investors, asset managers, lenders and other professionals.

Over the past few years, REIT investment has resulted in several billion dollars of construction activity, creating thousands of local jobs, both construction and permanent, and helping our community maintain a strong economy.

REITs have continued to contribute to our community by investing in affordable housing, retail, healthcare, office buildings and other commercial projects that will serve our community and local families for decades to come.

HB 2605 would disallow the dividends paid deduction for REITs. Hawaii is already among the most heavily taxed states in the entire country which stifles economic growth, and HB 2605 would make Hawaii one of only two states to disallow the dividends paid deduction. This change would create additional barriers to do business in our state and would negatively impact the level of interest in future investment in Hawaii and put jobs and revenues at risk.

Representative Angus L.K. McKelvey, Chair
Members of the House Committee on Economic
Development & Business
February 4, 2020
Page 2

Simply put, the bill will not provide the tax benefit assumed, but would increase even further the cost of doing business in this state. Accordingly, we respectfully urge you to defer HB 2605.

Mahalo for your consideration,

Catherine Camp, President
NAIOP Hawaii



SUNSTONE

HOTEL INVESTORS

February 3, 2020

Hearing Date: February 5, 2020

Time: 9:35 AM

Place: State Capitol Conference Room 309

Committee on Economic Development & Business

Rep. Angus L.K. McKelvey, Chair

Rep. Lisa Kitagawa, Vice Chair

State Capitol

415 South Beretania Street

Honorable Chair McKelvey & Committee Members,

Thank you for the opportunity to provide written testimony in opposition of HB 2605, relating to the taxation of Real Estate Investment Trusts in Hawaii. My name is Olivier Kolpin and I am and have been the Vice President of Tax at Sunstone Hotel Investors, Inc. ("Sunstone") since 2003. Sunstone is a publicly traded lodging real estate investment trust ("REIT") with 20 upper upscale, luxury and resort properties comprised of 10,610 rooms in 9 states (including Hawaii) and Washington DC.

Our presence in Hawaii began in 2014 with the purchase of the Marriott Wailea on the beautiful island of Maui. Soon after we made a significant capital investment of just over \$130 million dollars to renovate and reposition the resort. Of that \$130 million dollars in capital investment 76%, or just over \$100 million dollars went directly to local contractors, consultants, vendors and small businesses. As the hotel industry is capital intensive, we also will continue to make capital improvements to the property in the millions of dollars, most all of which will stay with Hawaiian businesses. In addition, through our manager we employ over 500 people in well-paying jobs that ensure our guests have a wonderful time when visiting the Hawaiian Islands. To support and service these endeavors we typically maintain over \$10 million in various accounts at local banks.

HB 2605 would subject hotel REIT's doing business in Hawaii to far more taxation than a regular hotel corporation doing business in the state. I bring your attention to Hawaii's General Excise Tax ("GET"). GET reaches most all transactions and has very few and

limited exceptions. For example, our past and future capital investments mentioned above are all subject to GET. GET also reaches a transaction unique only to REITs that own lodging facilities. Per the federal Internal Revenue Code, REITs are required to generate a majority of their income through rents and other passive income. For hotel REITs this is accomplished by the REIT leasing the hotel property to a fully taxable subsidiary corporate entity, who in turn must hire an independent 3rd party to manage the hotel on its behalf. This arrangement is also subject to GET. In Sunstone's case, our annual GET payments have ranged between \$1.5 and \$2.1 million dollars. The GET applicable to the rent from the taxable subsidiary are dollars that a non-REIT hotel business does not have to pay.

Key to Sunstone's business philosophy is the ability to listen. We listen to our investors and take what they say seriously. We listen to our employees and take what they say seriously. We listen to our guests and take what they say seriously. Over the years the Legislature has made several attempts to decouple from the federal treatment of dividend paid deductions, the reasons for which to influence social policy in regard to homelessness and basic housing needs. The purpose of HB 2605, it seems, is to argue that decoupling is based on equity. To level the playing field between "regular" corporations and REIT's. We strongly and respectfully disagree with this notion. HB 2605 states that REIT's "would continue to receive their generous federal tax exemptions...", however, we would still be required to distribute 90% of our earnings; something a regular corporation is never required to do. It is our opinion that the intended and unintended consequences of decoupling Hawaii's tax regime from the Internal Revenue Code would lead to less investment, less tax revenues and fewer jobs in Hawaii. For Sunstone in particular HB 2605 would make it more difficult to justify future investment in Hawaii.

In conclusion, I would like to strongly reiterate our opposition to HB2605.

Sincerely,



Olivier Kolpin
VP Tax
Sunstone Hotel Investors, Inc.

TAX FOUNDATION OF HAWAII

126 Queen Street, Suite 304

Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: INCOME, Disallow dividends paid deductions for REITs

BILL NUMBER: HB 2605; SB 2697

INTRODUCED BY: HB by BROWER, CREAGAN, HOLT, D. KOBAYASHI, C. LEE, LOWEN, MCKELVEY, NAKASHIMA, NISHIMOTO, ONISHI, QUINLAN, SAN BUENAVENTURA, TAKAYAMA, TAKUMI, TODD, Eli, Matayoshi, Morikawa; SB by KEITH-AGARAN, J.KEOHOKALO, MORIWAKI, S. Chang, Kanuha, Kidani, Kim, Riviere, Shimabukuro

EXECUTIVE SUMMARY: Disallows dividends paid deduction for real estate investment trusts. Applies to taxable years beginning after 12/31/2020. Sunsets 12/31/2023.

SYNOPSIS: Amends HRS section 235-2.3(b) to provide that section 857(b)(2)(B) (with respect to the dividends paid deduction for real estate investment trusts) shall not be operative for Hawaii income tax purposes.

Amends HRS section 235-71(d) to provide that for tax years beginning after December 31, 2020, no deduction for dividends paid shall be allowed for REITs for Hawaii income tax purposes.

EFFECTIVE DATE: This Act shall take effect upon its approval and shall apply to taxable years beginning after December 31, 2020; provided that this Act shall be repealed on December 31, 2023; provided further that sections 235-2.3(b) and 235-71(d), Hawaii Revised Statutes, shall be reenacted in the form in which they read prior to the effective date of this Act.

STAFF COMMENTS: Currently under federal and state income tax law, a real estate investment trust (REIT) is allowed a dividend paid deduction, unlike most other corporations, resulting in that dividend being taxed once, to the recipient, rather than to the paying corporation. The proposed measure would make that section of the IRC inoperative for Hawaii income tax purposes for tax years beginning after 12/31/19, meaning that REITs would be subject to double taxation like other corporations.

All state income tax systems in the United States, including ours, have a set of rules that are used to figure out which state has the primary right to tax income. For example, most tax systems say that rent from real property is sourced at the location of the property, so if a couple in Florida rents out a property they own on Maui they can expect to pay our GET and our net income tax on that rent. These sourcing rules, which do vary by state but are relatively consistent across state lines, are there to assure consistent and fair treatment between states.

Real estate investment trusts (REITs) are source shifters. For income tax purposes, they take in rent income, which is sourced to the location of the property being rented. They don't pay income tax on that income as long as they distribute the money to their shareholders as dividends. The dividend income of their shareholders, on the other hand, is generally sourced to

the residence of the shareholders. So, the income that the property states expected to tax is instead taxed in the states in which the shareholders live. And, to the extent that REIT shares are held by tax-exempt entities such as labor unions and retirement funds, passive income such as dividends may not be taxed at all. Source shifting is an issue specific to state taxation.

Apparently, the evil sought to be addressed by the bill is that (1) REITs are very visible in Hawaii, but do not get taxed because of the deduction allowed for dividends paid, while (2) many REIT owners who receive the dividend income are either (a) outside of Hawaii and don't get taxed either because they are outside of Hawaii, or (b) are exempt organizations that normally are not taxed on their dividend income. Normally we like to have our income tax law conform to the Internal Revenue Code to make it easier for people and companies to comply with it, but our legislature has departed from conformity when there's a good reason to do so (such as if it is costing us too much money). The issue is whether such a good reason exists here.

REITs do pay general excise and property taxes on rents received and property owned – as do the rest of us who are fortunate enough to have rental income or property to our name.

There is an issue that has developed around REITs that own hotels or other operating assets. Under federal rules, REITs cannot receive operating income, but can receive passive income from real estate (such as rent). To operate the hotels, they normally form a taxable REIT subsidiary (TRS), which is taxed as an ordinary corporation, to do that; the TRS then pays rent to the REIT. That rent is of course taxable under Hawaii's GET law, and the hotel REITs have suggested that if this bill passes the hotel REITs will unwind their ownership structure and eliminate the extra level of GET on those rents. In our mind this threat is not credible. The hotel REITs established their holdings before 2018 and presumably found that it was financially beneficial to do so despite the extra level of GET. Since then, the Tax Cuts and Jobs Act drastically reduced the federal corporate income tax rate, from 35% to 21%, and thereby lessened the burden that had been placed on the TRS's. If it was beneficial to adopt a REIT/TRS structure to run a hotel before the Tax Cuts and Jobs Act and the Act slashed the federal corporate rate, it is hard to imagine that unwinding the structure would be financially beneficial.

This bill is similar to SB 301 (2019), which was passed by the Legislature but was vetoed by the Governor amid concerns that enactment of the measure would chill investments in Hawaii and dry up the availability of already-scarce capital to Hawaii projects.

The bill's proponents have an answer to this concern, which is stated in the bill's preamble:

The legislature further finds that real estate investment trusts in Hawaii own real estate assets of about \$17 billion, generating an annual income of \$1 billion, which, if taxed, at the current corporate rate assessed to all other corporations, would generate Hawaii taxes of \$65 million per year. A 2016 analysis conducted by the department of business, economic development, and tourism concluded that the State had foregone about \$36 million in income tax in year 2014, and that the amount of real estate investment trust investments has risen substantially since 2014.

Some real estate investment trust shareholders live in Hawaii, but a substantial majority do not. Further, while real estate investment trusts own more real estate in Hawaii per capita than in any other state, it ranks fortieth in the nation for the number of real estate investment trust shareholders as a percentage of the population. As a result, many real estate investment trusts and their shareholders pay a mere fraction of the Hawaii state income tax compared to what other corporations pay.

The legislature therefore finds that it would be more equitable to decouple from the federal system in this regard so that corporations and other business entities doing business in Hawaii pay a fair tax burden commensurate with the substantial privileges and resources in Hawaii that were used to generate their profits. Real estate investment trusts would continue to receive their generous federal tax exemptions and continue to benefit from Hawaii's low property tax rates.

The Foundation is attempting to present both sides of the argument and is not taking a position for or against this bill's passage.

Digested 2/3/2020



Park Hotels & Resorts Inc.
Scott Winer, SVP Tax
1775 Tysons Boulevard
7th Floor
Tysons, VA 22102
+1 571 302 5757 Main

WRITTEN TESTIMONY OF

Scott D. Winer
Senior Vice President, Tax
Park Hotels & Resorts Inc.

IN OPPOSITION TO HB 2605

BEFORE THE COMMITTEE ON ECONOMIC DEVELOPMENT & BUSINESS

HEARING ON HB 2605

FEBRUARY 5, 2020

On behalf of Park Hotels & Resorts Inc. ("PARK"), thank you for this opportunity to provide our testimony on HB 2605. PARK submits this testimony in **opposition** to HB 2605.

As described in more detail below, PARK opposes HB 2605 for the following reasons:

- It would not add significant revenue to the State. The Hawaii Department of Taxation ("DoTax") has stated elimination of the DPD would raise only modest amounts of income taxes while likely resulting in less General Excise Tax ("GET").
- It would threaten the GET revenue associated with the statutorily required lodging REIT structure.

PARK is a publicly traded lodging real estate investment trust ("REIT") (NYSE:PK) that owns 62 premium branded hotels and resorts primarily located in the United States. Included within PARK's portfolio of hotels are (i) the iconic Hilton Hawaiian Village Waikiki Beach Resort located along Oahu's prestigious Waikiki Beach, and (ii) the Hilton Waikoloa Village located on the Kohala Coast of the Big Island of Hawai'i. PARK strives to be the preeminent lodging REIT, focused on consistently delivering superior, risk adjusted returns for shareholders that invest in the hotel sector. PARK, like most REITs, has a long-term investment focus and is committed to creating sustainable value at its properties.

As you know, Congress enacted the REIT legislation in 1960 to allow individual investors the ability to own and benefit from professionally managed, institutional quality, income-producing real estate. As with all REITs, PARK must meet multiple stringent, complex and costly requirements in order to maintain its status as a REIT, including: organizational requirements, asset holding requirements, passive income generation requirements, and importantly REITs must distribute at least 90% of their taxable income annually. These stringent, complex and costly requirements do Not apply to non-REIT real estate owners and require REITs to continuously access the debt and equity capital markets to obtain capital for maintenance, improvements and growth projects. By meeting these stringent, costly and complex requirements REITs are allowed to claim a dividend paid deduction ("DPD") essentially passing through their taxable income to shareholders.

As state above, one of the REIT requirements is the passive income generation requirement, which separates the federal tax rules for REITs and the rules applicable to non-REIT real estate owners. Federal tax law dictates that a REIT must earn most of its income from "rents", and income from operating a hotel is not "rents". Thus, federal law requires that a lodging REIT lease its hotels to a third party or one or more fully taxable subsidiaries. If leased to a taxable subsidiary (which is the structure used by public REITs), the taxable subsidiary is required to hire an independent operator, like Hilton, to manage the hotel. The rents paid by the taxable subsidiary to the REIT hotel owner and the management fees paid to the independent operator are both subject to Hawaii GET.

Thus, hotels operating within the REIT structure are subject to **triple GET taxation**. The over-whelming majority (approx..85%) of the additional GET is a direct result of federal law requirements governing hotel REIT operations and is not paid by a typical non-REIT hotel owner.

As described below, Park's acquisition and ownership of the two Hawai'i hotels results in approximately **\$11 million in additional GET being paid to the State of Hawaii annually**.

Further, as REITs are passive real estate companies, they cannot actively trade in real estate properties without being subject to a 100% tax on the gain. Thus, unlike non-REIT owners, as a passive real estate company, REITs are long term investors in their real estate. Park, as is widely known, acquired land adjacent to the Hilton Hawaiian Village Waikiki Beach Resort complex with the express intent of investing in an additional hotel tower. The construction of such a new hotel tower will likely cost hundreds of millions of dollars and create significant jobs and additional revenues for the State.

HB 2605 would, for three years, beginning in taxable years after Dec. 31, 2020 and ending on Dec. 31, 2023, disallow REITs from claiming the DPD and thus require REITs to pay corporate income tax to the State of Hawai'i during this three-year period.

We believe **the DPD should not be disallowed for any period of time or eliminated**. Not only is HB 2605 bad public policy, it would not add significant revenue to the State. DoTax has stated elimination of the DPD would raise only modest amounts of income taxes while likely resulting in less GET, both because of less investment by REITs and the likely planning that would reduce lodging REIT duplicate GET payments. The disallowance of the DPD would be inconsistent with federal tax rules and the existing rules of virtually all other states with an income-based tax system.

We believe that our investment and the investments by other REITs in Hawai'i are beneficial to the state and that disallowing the DPD would have the undesirable consequence of discouraging investment by REITs in Hawai'i. In fact, Park is currently in the planning phase related to the possible construction of a hotel tower adjacent to, and to be an addition to, the Hilton Hawaiian Village Waikiki Beach Resort complex. If HB 2605 were to become law, it will force us to reconsider whether we will proceed with this and future capital investment projects in the State of Hawai'i.

We believe the proposed legislation will not increase tax revenue for the state as the cost of doing business in Hawai'i will diminish investment returns and result in less investment. Further, disallowance or elimination of the DPD could result in foundations or pension funds replacing REIT ownership of real property. Foundations and pension funds generally are passive owners that pay no federal or state income taxes and do not make the same capital investments as REITs. Further, if hotels in Hawai'i are converted to non-REIT ownership, including ownership by taxable subsidiaries of REITs, the additional GET revenue generated solely as a result of the REIT structure will disappear.

We believe the GET, which is a tax on gross receipts rather than a tax on net income, is a more reliable and steadier source of state revenues than Corporate income tax and HB 2605's enactment would threaten this extremely valuable source of revenues to the State.

PARK's two landmark, oceanfront resorts cater to residents from Hawai'i and the mainland, and international travelers. PARK's Hawai'ian resorts provide significant economic benefit to the State of Hawai'i. We have made extensive renovations in excess of ~\$228 million at Hilton Hawaiian Village and Hilton Waikoloa Village, over the last 5 years.

PARK's economic footprint benefits the State of Hawai'i in many ways, including:

JOB: PARK's hotels directly employ more than 2,857 employees. The payroll and associated benefits for these direct employees is in excess of \$203,001,326 million annually.

CAPITAL MAINTENANCE: Over the next five years, PARK will likely spend \$200 million at Hilton Hawaiian Village and Waikoloa Village on capital maintenance projects, exclusive of any expansion capital.

CAPITAL DEVELOPMENT / IMPROVEMENTS. Given the long-term nature of our investment, PARK is currently analyzing significant development opportunities that will require meaningful capital investment at both resorts. These capital investments which are at various stages of feasibility / underwriting would be **hundreds of millions** of dollars.

HAWAII TAXES GENERATED / PAID BY PARK:

- General Excise and Use Tax - Operations. The tax revenues generated from our operations totaled \$27,981,455 in 2019.
- General Excise Tax – Rent / Management Agreement. As described above as a REIT, unlike non-REIT real estate owners, PARK must use a lease structure. As a result, we are required to pay General Excise Tax on the rent paid between our related companies. Effectively a double taxation of the same revenue. This additional GET paid by PARK was \$9,349,896 in 2019 and the additional GET paid by PARK on the management fees paid to our independent operator was \$1,564,830 in 2019.
- Property taxes. Property taxes at PARK's two resorts totaled \$22,403,103 in 2019.

CHARITABLE ENDEAVORS BY PARK and ITS ASSOCIATES in HAWAII:

- PARK associates spend thousands of hours annually volunteering for local events and charities.
- PARK and its associates provide cash and in-kind charitable contributions more than \$600,000 annually.

We believe that Park has been a solid corporate citizen and partner to the state of Hawai'i – paying significant tax, supporting numerous jobs and benefitting the community at-large. PARK's REIT structure and hotel ownership benefits the State of Hawai'i and Kama'aina tremendously in a variety of economic and charitable ways.

If adopted, this controversial legislation would (i) put Hawai'i at a competitive disadvantage for REIT investment, (ii) penalize Hawai'ian citizens, including the Hawaii Employer-Union Health Benefits Trust Fund beneficiaries, that invest in REITs by reducing their investment returns, (iii) discourage REITs from investing in Hawai'i, (iv) require PARK to reassess the level of future capital invested in Hawai'i and our Hawai'ian assets including the potential construction of an additional hotel tower as part of the Hilton Hawaiian Village Waikiki Beach Resort complex, and (v) require Park, as a publicly-traded company, to address our form of ownership and operation in Hawai'i, which could lead to implementing one or more appropriate tax planning techniques or strategies to maintain shareholder value. Further, this legislation would have a chilling effect on the positive economic and charitable impact PARK provides through its REIT ownership and capital investment in Hawai'i.

We thank you again for this opportunity to provide testimony against HB 2605 and sincerely hope you consider our **strong opposition** to this proposed legislation.

Respectfully submitted,

A handwritten signature in purple ink, appearing to read "S Winer", with a horizontal line extending to the right.

Scott Winer
Senior Vice President, Tax



OPSEU Pension Trust

Fiducie du régime de
retraite du SEFPO

February 5, 2020

The Honorable Angus McKelvey, Chair
And Committee Members
Committee on Economic Development and Business
Hawaii State House of Representatives
415 S. Beretania St., #309
Honolulu, HI 96813

Dear Chair McKelvey and Committee Members:

RE: HB 2605 Relating to Taxation of Real Estate Investment Trusts

My name is Andrew Alcock, Director, Real Estate Investments, OPTrust, testifying in strong opposition to HB 2605 Relating to Taxation of Real Estate Investment Trusts. OPTrust is one of Canada's largest pension funds with net assets of over \$20 billion CAD. The trust administers a defined benefit plan with almost 95,000 members and retirees.

OPTrust partnered with DeBartolo Development ("DeBartolo") to develop the Ka Makana Ali'i center in Kapolei. DeBartolo's vision and partnership with the Department of Hawaiian Home Lands ("DHHL") were important factors in OPTrust's decision to invest in Hawaii. One of the deciding factors in OPTrust making its investment in Ka Makana Ali'i, was the sound investment policies of both the State of Hawaii and its partnership with private developers like DeBartolo. OPTrust invests across the globe. Many of those investments are made through REIT structures, which provide a dividend exemption by law. By way of example, there is only one State in the United State of America (New Hampshire) which does not permit the REIT dividend deduction. The ability to invest in Ka Makana Ali'i through a REIT structure was paramount to OPTrust's decision to invest in Hawaii.

REIT's provide a way to finance projects that local investors or the State of Hawaii would not be able to provide. Disallowing the dividends paid deduction for REIT's will result in the double taxation on REIT income and will place Hawaii at a disadvantage compared to other states when it comes to attracting investor capital. Disallowing the deduction would prevent numerous investors from investing in the State of Hawaii, resulting in far fewer development projects and less low-income housing.

Should this bill pass, OPTrust would be forced to direct its investment capital elsewhere. Unfortunately, we also understand and recognize that any changes in the law will have a very undesirable effect on DHHL and impact any income that they receive to further their efforts to build housing and provide programs for their beneficiaries.

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We urge you to strongly oppose HB 2605, so that projects such as Ka Makana Ali'i can continue to be built and enhance not only Hawaii's economic growth but continue to provide DHHL with the means to provide more for the native Hawaiian community.

Yours truly,

A handwritten signature in black ink, appearing to read 'Andrew Alcock', with a long horizontal flourish extending to the right.

Andrew Alcock

**WRITTEN TESTIMONY OF
DARA F. BERNSTEIN
SENIOR VICE PRESIDENT & TAX COUNSEL
IN OPPOSITION TO HB 2605
BEFORE THE HAWAII HOUSE
COMMITTEE ON ECONOMIC DEVELOPMENT & BUSINESS**

**THE HONORABLE ANGUS L.K. McKELVEY, CHAIR
THE HONORABLE LISA KITAGAWA, VICE CHAIR
HEARING ON HB 2605
FEB. 5, 2020
9:35 A.M.**

Dear Chair McKelvey, Vice Chair Kitagawa, and Members of the House Committee on Economic Development & Business:

Thank you for the opportunity to submit this testimony on behalf of Nareit and its REIT members active in Hawaii. These REITs have substantial long-term investments in Hawaii. Nareit is the worldwide representative voice for real estate investment trusts—REITs—and publicly traded real estate companies with an interest in U.S. real estate and capital markets.

Earlier this week, Nareit was pleased to welcome Gladys Marrone as the Executive Director of our new Nareit Hawaii office. Ms. Marrone’s responsibilities include representing REITs locally, coordinating outreach to investors and the investment community in Hawaii, and working with government agencies as well as community and charitable organizations to address social issues of importance.

For the reasons discussed in more detail below, we strongly oppose, and ask you to hold, HB 2605, legislation that would eliminate the REIT “dividends paid deduction” (DPD) temporarily.

- **HB 2605’s enactment would likely produce less overall revenue than current law.**
- **Department of Taxation’s (DoTax) public testimony regarding similar legislation estimates at best an incremental increase in revenue from enactment of similar legislation:** Enactment would raise, at best, approximately \$2.5 million the first year and \$10 million annually thereafter according to DoTax’s public testimony.¹
- **DoTax says actual revenue could be lower—even zero:** A DoTax representative cautioned in public testimony and a radio interview that actual revenue raised could be lower.²
- **Loss of general excise tax (GET) would likely more than offset any increase:** Federal law applicable to hotel REITs requires them to use a lease structure that results in an additional level of GET **not applicable to non-REITs**. As described below, jeopardizing this additional GET could more than offset any revenue gains.

¹ Note comments around 3:40:23 to 3:40:38 / 4:01:24 of the Feb. 12, 2019 video of the House Consumer Protection & Commerce hearing on a 2019 bill that also would have eliminated the REIT DPD, [HB 475, HD 1](#), available at [this link](#).

² Note comments around 3:41:02 to 3:41:41 / 4:01:24 of the Feb. 12, 2019 video of the House Consumer Protection & Commerce hearing on HB 475 HD 1 available at [this link](#) and comments of Former Director of the Hawaii Department of Taxation, Linda Chu Takayama in this Feb. 4, 2019 [interview](#) with Hawaii Public Radio (“Raising Taxes on REITs”), beginning at 10:10.

- **What about the larger amounts asserted by proponents?** DoTax testimony suggests proponents are relying on “incorrect” numbers in an earlier DBEDT study.³
- **HB 2605’s enactment would risk job loss at a time when the construction industry is reportedly weakening.** It would not be prudent to risk this job loss given the unlikelihood of any overall revenue gain.

The remainder of this testimony provides additional detail and information.

REITs in Hawaii

REITs are companies that provide a way for anyone, including Hawaii residents, to own professionally managed, income-producing real estate for the long term—just like the way mutual funds let small investors buy stock in a corporation. Many local people own REITs, either as individual investors or through mutual funds and employer or union pension plans.

Many Hawaii residents may not even realize that they benefit from REITs either through mutual funds or their pension or retirement accounts. [Nareit analysis of data](#) from 2016 Federal Reserve Board Survey of Consumer Finances (SCF), the Employment Benefit Research Institute data on 401(k) equity allocations (EBRI), Census population and household counts, and Morningstar Direct data, indicates that about 47% of Hawaii households own REIT stock directly and/or through mutual funds or certain retirement accounts. There are more than 200 publicly traded REITs, and only about 30 REITs with Hawaii properties. As a result, a significant portion of REIT ownership most likely relates to REITs with properties outside of Hawaii.

REITs are long-term property holders that own, renovate, and manage affordable housing projects, commercial buildings, medical facilities, shopping centers, cell phone towers, and hotels throughout Hawaii. Examples of REIT-owned properties in Hawaii include:

- the state-of-the-art Hale Pawa'a Medical Building in Downtown Honolulu (Healthcare Realty Trust);
- nearly 500 soon-to-be available [affordable housing rentals](#) at Bishop Place in Honolulu for tenants earning between 80% and 120% of area median income and workforce rentals at Moanalua Hillside apartments (Douglas Emmett Inc.)
- Pearlridge Center in Aiea, which just last year completed a \$33 million renovation (Washington Prime Group);

³ Note comments around 3:40:40 to 3:40:56 /4:01:24 of the Feb. 12, 2019 video of the House Consumer Protection & Commerce Committee hearing on HB 475 HD 1, available at [this link](#).

- Ka Makana Ali'i in Kapolei, whose revenues assist DHHL in building homes for Native Hawaiians;
- A number of hotels, including Hilton Hawaiian Village (Park Hotels & Resorts, Inc.); Fairmont Kea Lani on Maui (Host Hotels & Resorts, Inc.); and Wailea Beach Marriott Resort & Spa (Sunstone Hotel Investors, Inc.), all of which, as described below, are required to use a lease structure that generates at least \$16 million in general excise taxes to the state over what non-REITs would owe.

In addition, Brookfield Property REIT recently announced that starting in 2021, it plans to build a 550-unit residential tower with a mix of unit sizes with 110 apartments being rented to tenants earning 80% or less of the area median income.

REITs also have increased student housing opportunities at the University of Hawaii. EdR developed the Hale Mahana apartments at the University of Hawaii at Manoa. American Campus Communities also redeveloped Frear Hall for the University of Hawaii a number of years ago.

HB 2605's Enactment Would Produce Less State Tax Revenue than Current Law

According to the Department of Taxation, enactment would only raise an incremental amount of revenue; however, enactment could result in a potential \$6 million loss when factoring in potential lost general excise tax (GET) revenue

In an April 4, 2019 Hawaii Public Radio [interview](#) regarding similar legislation, former Department of Taxation Director Linda Chu Takayama stated the following when speaking merely of the corporate income tax impact of enactment of similar legislation (beginning at 10:10 in "Raising Taxes on REITs"): "[Our economist's analysis] is that it might bring in \$2 million the first year, something less than \$10 million in the out years, and even that's a little bit fuzzy because that doesn't represent all of the deductions that these companies could be taking; once you factor that in, the number goes way down." See also footnotes 1-3 above and accompanying text for more detail.

Because of unique requirements applicable to lodging REITs, essentially resulting in an additional level of GET, the state received more than \$16 million in annual GET in 2018 alone just from hotel REITs in Hawaii that non-REIT hotel owners wouldn't owe.

- Federal law requires that lodging REITs—**unlike non-REIT hotel owners**—to lease their hotels either to an unrelated company or to a fully taxable REIT subsidiary at market rent that must hire an unrelated hotel operator (like Marriott or Hilton).
- Park Hotels & Resorts, Inc.'s [testimony](#) (on page 28 of the posted testimony) with respect to a similar bill, [SB 2409](#), said this extra GET was over \$9 million more than a non-REIT would pay in

GET—and that is just one hotel REIT. When aggregated with other REIT hotel owners in Hawaii, this additional GET is estimated to have **exceeded \$16 million in 2018**.

- And as a tax on gross receipts rather than a tax on net income, the GET is a very stable source of almost half of state revenues and compared with the corporate income tax (around 1-3%) (For example, see data from Council on State Revenues for [FY 2019 To FY 2025](#)). **HB 2605's enactment would seriously endanger this extremely valuable source of GET revenues to the state.** Not only that, enactment also would put at risk the revenues and jobs created by non-hotel REITs that invest in the state.
- Given the risk of losing up to \$16 million in GET annually, and the risk of lost jobs, it would not be prudent to enact HB 2605.

HB 2605 Enactment Would Risk Job Losses for Hawaii Residents

HB 2605 risks significant job loss, at a time when the construction industry is reportedly weakening. Enactment of HB 2605 would potentially result in a reduction of millions of dollars of new REIT investment, a shift in property ownership to tax-exempt owners like pensions and endowments (who invest significantly in real estate), and loss of revenue and the stability of hundreds of the jobs generated by REITs to the state. These existing and potential jobs belong to real people. Is it fair to risk significant job loss by enacting this proposal, particularly in light of [DBEDT's report](#) to the Hawaii Senate Ways & Means Committee and House Finance Committee on Jan. 7, 2020 that the construction industry is weakening?

Enacting this proposal would signal Hawaii's discouragement of long-term capital investment in the state. REITs provide sorely needed investment capital to Hawaii. If this measure is passed it is very likely that potential REIT and non-REIT investors, fearing unexpected law changes post-investment, would choose to deploy their capital elsewhere, and Hawaii would be on the outside looking in.

Hawaii's significant economic growth over the past several years is, and we hope into the future, will be, in large part a direct result of REIT investment. The popular new addition to Ala Moana Center was made possible by REIT funding. That project alone was estimated to have brought in more than \$146 million in state revenue in 2016. Since completion, the additional retail sales produced some estimated \$33 million in GET revenue for the state, along with 3,000 new jobs.

Hawaii residents have benefitted from REIT investment, which made possible dining at the Cheesecake Factory at Ka Makana Ali'i or taking their family to Wet'n'Wild, or going shopping at Pearlridge, more eating choices and better Waikiki parking opportunities with the redevelopment of the International Market Place, not to mention the financial benefits to the Queens Health System, which is the landowner.

These jobs and tax revenue would not be here without REIT funding. REIT investment continued during the recession we recently experienced. While regular investors shied away from redevelopment, REITs continued to build and improve their properties, providing a boost to the state's local economy through needed construction jobs and later retail jobs for the completed projects.

Contrary to its goals of fairness, HB 2605's enactment would impose obligations and liabilities on REITs that are not imposed on non-REIT corporations or partnerships

Contrary to the goals of "fairness," enactment of HB 2605 would be anything but fair by imposing additional obligations and liabilities on REITs not imposed on non-REIT corporations or partnerships.

Specifically, REITs are just corporations or business trusts that file a tax return with the IRS electing REIT status. If they comply with the many requirements imposed on REITs, among them, being widely-held (no family-owned, closely-held businesses); investing mostly in real estate; not "flipping" properties (or paying a 100% tax on gains if they do) and distributing all of their income, they can deduct their distributions from their taxable income. As a result, their income is taxed at the investor level—like that of partnerships. If they don't meet these requirements, they are taxed at the entity level like non-REIT corporations, and then again at the shareholder level when their income is distributed. Non-REIT corporations and partnerships aren't subject to the burdens and obligations imposed on REITs; most importantly, unlike REITs, they can retain their profits.

If enacted, HB 2605 wouldn't eliminate the requirements applicable to REITs—they would still need to be widely held, invest mostly in real estate; distribute all of their income, and not flip properties, but these requirements would not apply to non-REIT corporations or partnerships. Despite being subject to these requirements, REITs would be unable to claim the DPD in Hawaii with respect to distributed income. Thus, although non-REIT corporations and partnerships in Hawaii could retain 100% of their income; REITs in Hawaii would be required to distribute at least 90% of their income, and both would be unable to claim a DPD.

HB 2605 would not change the tax exemption of other entities that earn rental income from real property such as tax-exempt pension funds and endowments, who invest in rental real estate through partnerships, sometimes along with REITs, and pay no income tax on their earnings from those properties.

Finally, because REITs generally have no income tax liability, they generally do not claim tax credits, and they cannot pass through credits or losses to investors. Non-REIT corporations and partnerships can and do claim tax credits, and partnerships can pass through credits and losses to investors.

HB 2605 Would Violate Core State Comity Principles

HB 2605 would be contrary to federal income tax rules and the existing laws of virtually every other state with an income-based corporate tax system. Virtually every state with an income-based tax system, including Hawaii currently, allows REITs a deduction for dividends paid. (New Hampshire is the only state with income-based corporate tax that does not permit a DPD. New Hampshire has much less REIT investment than Hawaii despite having a similarly sized economy). Additionally, Hawaii currently taxes all REIT dividend income received by Hawaii resident shareholders, regardless of where the REIT's real estate is located or the REIT does business.

Please Hold HB 2605

For the reasons described above, Nareit requests the Committee to hold HB 2605.

February 4, 2020

Representative Angus L.K. McKelvey, Chair
Representative Lisa Kitagawa, Vice Chair
Members of the House Committee on
Economic Development & Business
Thirtieth Legislature
Regular Session of 2020

RE: HB 2605 – RELATING TO TAXATION OF REAL ESTATE INVESTMENT TRUSTS

Hearing Date – February 5, 2020 at 9:35 a.m.

Dear Chair McKelvey and members of the Committee,

My name is Jan Yokota and I am the Regional Vice President of the Pacific Region for The RMR Group LLC. The RMR Group LLC is an alternative asset management company that was founded in 1986 to invest in real estate and manage real estate related businesses. In Hawai'i, The RMR Group manages more than 17,000,000 square feet of property for three real estate investment trusts (REITs): Industrial Logistics Properties Trust; Diversified Healthcare Trust; and Service Properties Trust.

REITs were established by Congress in 1960 to give everyone, regardless of income level, an opportunity to invest in real estate. By law, a REIT must distribute at least 90% of its taxable income to shareholders as dividends. Many of these shareholders are Hawai'i residents and institutions, such as pension plans of Hawai'i companies and the State of Hawai'i Employees Retirement System, who rely on these dividends for secure income. HB 2605 would effectively double tax the REITs and their shareholders.

REITs have access to global capital markets, which provide them with funding to invest in Hawai'i. Over the past few years, investment by REITs in Hawai'i has resulted in several billion dollars of construction activity, creating thousands of local jobs, both construction and permanent, and helping our community to maintain a strong economy. Passage of HB 2605 would put future capital investment by REITs in properties in Hawai'i at risk, resulting in a corresponding reduction of general excise taxes and jobs.

REITs have contributed significantly to Hawai'i by adding jobs, increasing revenues for the State and supporting the community through charitable contributions. Any tax revenues that may be generated by HB 2605 will be greatly outweighed by the negative consequences to the State's economy, tax revenue and jobs. Accordingly, we respectfully urge you to defer HB 2605.

Mahalo for your consideration.



February 4, 2020

Hearing Date: February 5, 2020

Time: 9:35 am

Place: State Capitol, Conference Room 309

Rep. Angus L.K. McKelvey, Chair

Rep. Lisa Kitagawa, Vice Chair

State Capitol

Committee on Economic Development and Business

415 South Beretania Street

Honolulu, Hawaii 96813

Re: Testimony in Opposition to House Bill No. 2605

Dear Chairman McKelvey, Vice-Chairman Kitagawa and Committee Members:

Thank you for the opportunity to provide written testimony on House Bill No. 2605. My name is Francis Cofran, the Senior General Manager of Ala Moana Center, the largest retail center in the state of Hawaii, and I am Jared Chupaila, Chief Executive Officer of Brookfield Properties' retail group, operator of Ala Moana Center. Simply put, we do not support this Bill that would disallow the dividends paid deduction, subject REIT investment in Hawaii to double taxation, and contradict the taxation of REITs nationwide. As we have previously testified, this legislative path is clearly inappropriate and will ultimately harm Hawaii.

We last testified on behalf of Ala Moana and GGP; GGP is now known as Brookfield Property REIT and is an affiliate of Brookfield Asset Management. Brookfield Properties' retail group, which encompasses the former GGP portfolio, as well as other retail properties within Brookfield Properties, has an extensive portfolio of mall properties encompassing over 170 locations across 43 U.S. states. Brookfield Properties assures premier quality and optimal outcomes for our tenants, business partners and the communities in which we do business. Brookfield Properties continues GGP's legacy of being a part of the economic fabric of Hawaii for more than 30 years (since 1987) -- managing, owning and reinvesting in its Hawaii real estate assets as part of a long-term commitment that provides economic stability, growth, and jobs through all economic cycles.

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Indeed, across its portfolio and in Hawaii, Brookfield Properties' REIT capital and investment are focused on producing stable, long term cash flows over a variety of economic conditions. Brookfield Properties operates three major retail shopping centers in Hawaii – the Prince Kuhio Plaza ("PKP") in Hilo, Whalers Village in Lahaina, and the Ala Moana Center in Honolulu. As the largest indoor shopping center on the island of Hawaii, PKP provides great event space for local Kupuna groups passing on their knowledge of music and dance, artisan craft fairs and the celebration of other local traditions. The latter two are iconic visitor attractions that help sustain Hawaii's important tourism industry. Home to more than 350 stores and restaurants, Ala Moana Center is the primary shopping, dining and leisure destination for Kama`aina and visitors. Our two office buildings, which include the Ala Moana Building (Bank of Hawaii) and Ala Moana Pacific Center (Shokudo Building), primarily are occupied by local tenants who cater to residents. In addition to their important role in tourism, all three centers directly benefit the state and local economy through the Hawaii general excise tax.

Efficient REIT capital allows us to constantly reinvest in and enhance the customer experience as well as evolve to meet the needs of Hawaii. For example, at Ala Moana during 2012-2016, we invested almost \$1 billion to construct additional retail square footage and residential condominiums. We announced in October 2019, that starting in 2021, we plan to build a 550-unit residential tower with a mix of unit sizes with 110 apartments being rented to tenants making no more than 80% of the area median income. This new investment will continue to enhance Ala Moana's standing as a live, work, play destination for all.

In prior year legislative sessions, we have testified in opposition to attempts to eliminate the deduction for dividends paid by REITs. That testimony has focused on the following points:

- If Hawaii enacts this legislation, it will be out of step with all other states with respect to the dividends paid deduction for REITs (except for New Hampshire, where we believe REIT investment has been inhibited).
- The deduction for dividends paid by REITs results in a single level of taxation at the shareholder level which is consistent with how limited liability companies, Subchapter S corporations and partnerships that own real estate are taxed. Changing the taxing structure here would put REITs at a disadvantage in relation to these other forms of doing business.
- REITs produce substantial economic benefits to the State of Hawaii in the form of jobs, general excise tax, income tax from persons working or engaging in business at REIT properties, and real property taxes. The three properties annually pay more than \$40

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million in real property and general excise taxes – metrics that clearly demonstrate that REITs are investing in the economic well-being of the state and its residents.

As we look forward over the next 30 years, future expansion plans could be reconsidered if the attractiveness of investing in Hawaii relative to the rest of the United States is diminished. Proponents of the legislation say that REIT investment would not leave Hawaii but both the Department of Business, Economic Development & Tourism (“DBEDT”) and the Department of Taxation have noted that there is no surety that investment will not be reduced and that estimates of revenues will be realized. Deviation from a long held national legislative norm is not good policy.

Please do not allow the perception of a revenue increase override the long-term economic benefits that REIT investment, under the existing tax regime, brings to the state of Hawaii and its residents. For the foregoing reasons, we respectfully oppose House Bill No. 2605 and urge you to oppose it as well. Thank you for your consideration.

Sincerely,



Francis Cofran
Senior General Manager



Jared Chupaila
Chief Executive Officer

Written Testimony of

Joseph Greenbaum

Senior Tax Director

RLJ Lodging Trust

In opposition to HB 2605

Relating to the taxation of Real Estate Investment Trusts

Before the Hawaii House of Representatives

Hearing on February 5, 2020

On behalf of RLJ Lodging Trust (“RLJ”), I am providing concerns about HB 2605, relating to the taxation of real estate investment trusts (“REIT”).

RLJ is a publicly traded lodging REIT (NYSE:RLJ) that owns 104 hotels in 23 States and the District of Columbia. One of our hotels is the Courtyard Waikiki Beach located in Honolulu, Hawaii. RLJ has a long-term investment focus for this hotel and is committed to creating sustainable value at this property that benefits the community. Our hotel provides jobs to the local residents, and over the next 4 years we expect to spend approximately \$10 million on capital development projects that will benefit local contractors and vendors. Additionally, we pay approximately \$1.5 million per year in real estate taxes.

Congress created REITs in 1960 to provide individual investors a way to invest in professionally managed, income producing real estate. Investors are aware that REITs do not pay federal income taxes, thus avoiding the double taxation of corporate and personal income taxes that impacts most other corporations. In order to avoid double taxation, a REIT must satisfy multiple stringent and complex requirements. One such requirement is that the REIT must distribute at least 90% of their taxable income annually, and most REITs, including RLJ, distribute 100% of their taxable income. The distribution requirements, as well as the other REIT rules, entitle REITs to claim a dividends paid deduction (“DPD”) on its federal and state income tax returns.

Should the DPD be disallowed, non-resident shareholders will be made subject to double taxation on income derived from REIT property in Hawaii, which would be in direct contravention to the intent underlying the federal government’s establishment of REITs. We believe investors would favor REIT investments that avoid such double taxation, causing a reduction in the number of REITs investing in Hawaii.

One of the requirements of a lodging REIT, unlike non-REIT property owners, is that the REIT form a taxable REIT subsidiary (“TRS”) to operate its hotels and pay rents to the REIT for the use of the properties. This results in general excise tax (“GET”) on the rent payments between the TRS and the REIT. The GET is a gross receipts tax, rather than a tax on net income, which makes the GET a stable and reliable source of revenue for the State. We believe the elimination of the DPD could cause REITs to re-evaluate the structure and eliminate the intercompany leases, thus threatening this valuable source of GET revenues to the State.

We believe that RLJ contributes to the growth and well-being of Hawaii and its residents. Our REIT structure enables us to raise capital in order to reinvest in our hotel. The elimination of the DPD would force us to revisit our structure and future plans in the State. For the reasons described above, RLJ strongly opposes, and asks you to hold, HB 2605.



ALEXANDER & BALDWIN
PARTNERS FOR HAWAII

**HB 2605
RELATING TO TAXATION OF REAL ESTATE INVESTMENT TRUSTS**

**PAUL T. OSHIRO
DIRECTOR – GOVERNMENT AFFAIRS
ALEXANDER & BALDWIN, INC.**

FEBRUARY 5, 2020

Chair McKelvey and Members of the House Committee on Economic Development
& Business:

I am Paul Oshiro, testifying on behalf of Alexander & Baldwin (A&B) on HB 2605, “A
BILL FOR AN ACT RELATING TO TAXATION OF REAL ESTATE INVESTMENT
TRUSTS.” We respectfully oppose this bill.

While A&B has always been a Hawaii-based company, in 2012, A&B made a strategic decision to be 100% Hawaii-based and to migrate its mainland investments back to Hawaii. Since then, A&B has sold all of its mainland properties and has reinvested the proceeds in Hawaii—acquiring properties including the Kailua Town commercial center, Manoa Marketplace, Waianae Mall, Laulani Village (Ewa Beach), Puunene Shopping Center (Maui), and Hokulei Village (Kauai). In 2017, to better support our Hawaii-focused strategy and increase our ability to invest in Hawaii in an increasingly competitive environment, A&B made the decision to convert to a real estate investment trust (REIT). A REIT structure enables A&B to attract new investors to its stock, giving us capital to invest in our Hawaii-focused strategy, and puts us in a better position to compete with large, out-of-state investors, with greater sources of capital, for the acquisition of Hawaii properties,

thus keeping them in locally-owned hands, with a management team that lives here and is committed to Hawaii. Furthermore, REITs are structured to be long-term holders of real estate, thus complementary to A&B's goal of being Partners for Hawaii, with a long-term commitment to our communities.

Real estate investment trusts were established by Congress in 1960 to enable all types of investors to invest in real estate. REITs generally own, operate, and finance income-producing commercial real estate such as shopping malls, hotels, self-storage facilities, theme parks, and apartment, office, and industrial buildings. Other REITs provide financing for income-producing real estate by purchasing or originating mortgages and mortgage-backed securities, which provides liquidity for the real estate market.

In Hawaii, REIT investments help communities grow through the development of workforce rental housing, medical facilities, shopping centers, and commercial buildings that enhance our quality of life. REITs own high-quality office, retail, and industrial space, which provide a favorable environment for numerous locally owned businesses to operate and grow. These REIT owned facilities also provide numerous employment opportunities and jobs for Hawaii's residents.

BILL WILL RESULT IN DOUBLE TAXATION OF SHAREHOLDER DIVIDENDS

The purpose of this bill is to disallow the dividend paid deduction for real estate investment trusts. At present, all states except for one (New Hampshire) allow REITs to pass through its federally mandated shareholder dividend distribution without the imposition of a corporate tax, as individual shareholders are responsible to pay the tax on these dividends. The disallowance of the dividend paid deduction will result in the double taxation of Hawaii REIT shareholder dividends. This will essentially result in Hawaii REITs

continuing to distribute, as mandated by Federal Law, at least 90% of their taxable income to shareholders. However, unlike the other states, the REIT will also pay Hawaii corporate income tax prior to making the dividend distribution to its shareholders, thus reducing the amount of dividends shareholders will receive. In addition, shareholders of Hawaii REIT properties will also continue to be responsible to pay income tax on the distributed dividends—a second tax on the same profits.

If REITs and their investors are double taxed in Hawaii, it is likely that investors may shift their investments to other states where a better return on their investments can be realized. This will result in REITs spending and investing less money in Hawaii to operate, maintain, and enhance their properties. Hawaii's economy will inevitably be negatively impacted should the dividend paid deduction be repealed.

NEGATIVE IMPACT ON HAWAII'S ECONOMY

REITs provide a much-needed source of outside capital for Hawaii. Very few individual investors and a fairly small number of corporate players in Hawaii have capital market access equivalent to what is enabled by REITs. REITs bring this externally raised capital to invest in, develop, and enhance properties here in Hawaii. In addition, REITs continually invest during both good and bad economic times, thus softening the impact of recessions and local economic downturns.

Today, only New Hampshire disallows the REIT dividend paid deduction. If this bill is enacted into law, REITs and their investors may prefer to invest in states other than Hawaii. Hawaii, along with REITs with properties in Hawaii, will be at a competitive disadvantage in attracting additional investors and capital to support continued investment, economic development, and growth in our state. When combined with the direct reduction

in general excise and income taxes from diminished REIT related construction, fewer jobs, and the reduction in business and individual income taxes because of the direct and indirect impacts of lower REIT related activity, this bill poses a significant risk to the health of the state's overall economy.

Based on the aforementioned, we respectfully request that this bill be held in Committee. Thank you for the opportunity to testify.

HB-2605

Submitted on: 2/3/2020 9:57:01 AM

Testimony for EDB on 2/5/2020 9:35:00 AM

Submitted By	Organization	Testifier Position	Present at Hearing
lynne matusow	Individual	Oppose	No

Comments:

This is unfair to the many taxpayers who use this dividend income for everyday expenses. REITs are one of the safest investments, with a dividend component as well as a growth component. You are doing a disservice to many seniors and others who need this income to live on, and not have to divert away some for taxes. To add insult to injury, you are sunseting the provision after three years, which means you really do not support it.

Please kill this bill.

lynne matusow

HB-2605

Submitted on: 2/3/2020 4:02:06 PM

Testimony for EDB on 2/5/2020 9:35:00 AM

Submitted By	Organization	Testifier Position	Present at Hearing
Robin Hart	Individual	Support	No

Comments:

I'm writing in support of HB2605.

How can it be, that we are allowing for-profit corporations to make their money here, and not pay Hawaii's corporate tax???

This is very unfair. REITS have a competitive edge. The playing field is not level. Correcting this would generate \$60 million in tax money and Hawaii needs that money.

REITS should be required to pay taxes on thier profits, just like everybody else.

Come on. Our schools are falling apart. Teachers and first responders are underpaid.

I realize this passed last year and the Governor, Ige, vetoed it. Do the right thing and let's get this passed again.

TO: HOUSE COMMITTEE ON ECONOMIC DEVELOPMENT & BUSINESS
Rep. Angus L.K McKelvey, Chair
Rep. Lisa Kitagawa, Vice-Chair

FROM: Eldon L. Wegner, Ph.D.
Professor Emeritus in Sociology, UH-Manoa

SUBJECT: HB 2605 Relating to Taxation of Real Estate Investment Trusts

HEARING: Wednesday February 5, 2020, 9:35 am
Conference Room 300, Hawaii State Capitol

POSITION: Support with suggested amendments. Currently, REITS allow individuals to avoid paying Hawaii state taxes on the profits from business transactions in the state of Hawaii. This bill would end this unfair practice by closing that loophole. However, we suggest an amendment that the additional revenue be channeled into affordable housing and programs to end homelessness.

RATIONALE:

I am offering my testimony as an individual. I am a Professor Emeritus in Sociology, UH-Manoa. I belong to Faith Action and Church of the Crossroads. This bill is a priority for both of these organizations in the current legislative session..

Real Estate Investment Trusts (REITs) are corporations that use a loophole to avoid the Hawaii corporate tax. **We should not give away potential state revenue to wealthy individuals and then make the claim that the state can't afford to solve our pressing housing problems.**

We need solutions to our affordable housing crisis now!

REITs own income-producing property in Hawaii such as Ala Moana Center, the Hilton Hawaiian Village Resort, as well as office buildings and many other shopping centers and hotels. Together, they own property with an estimated total value of \$18 billion that earns an estimated \$1 billion in profits annually. If Hawaii's corporate tax were applied to REITs, an estimated \$60 million in tax revenue would be generated.

Meanwhile, Hawaii faces an enormous shortage of housing that is affordable to low- and middle-income individuals and families. New housing is being built, but most of it is priced for the high-income strata. Some efforts are being made to build affordable housing for low- and middle-income levels, but much greater efforts must be made because the need is so great and the cost of housing is so high.

Various ideas to fund affordable housing are contained in an action plan for workforce/affordable housing that was funded by the Legislature and issued in 2017. Those ideas include dedicating new tax revenue for affordable/workforce housing or infrastructure, with the funds kept separate from the general fund. (Housing Action Plan Final Report to the State Legislature, 2017, p. xii)

The revenue generated by this bill could easily be dedicated to funding affordable housing and programs for the houseless. The bill should be amended to separate the new tax revenue from the general fund and direct it to the creation of affordable housing in Hawaii.

Thanks you for the opportunity for me to submit testimony.

Sincerely,
Eldon L. Wegner, Ph.D.

HB-2605

Submitted on: 2/3/2020 6:12:14 PM

Testimony for EDB on 2/5/2020 9:35:00 AM

Submitted By	Organization	Testifier Position	Present at Hearing
Claire Gearen	Individual	Support	No

Comments:

Dear Chair Angus L.K. McKelvey, Vice-chair Lisa Kitagawa, and Members of the Committee on Economic Development and Business,

My name is Claire Gearen, and I write in strong support of House Bill 2605. I am a member of Faith Action for Community Equity and speak also as a concerned private citizen.

As a career public teacher, I have a clear stake in legislators' work to maintain an adequate revenue stream while operating within the state biennial budget. Not only is my salary tied to the legislators' appropriations, my students educational experience is affected by the amount available in the weighted student formula. I still teach students who experienced Furlough Fridays and am just recovering financially from those pay cuts. My conditions in the classroom have improved in recent years as I acquire the resources I need to teach.

Yet, putting my own interests and those of my students aside, the public more widely has an interest in closing the Real Estate Investment Trust (REIT) tax loophole. As House Bill 2605 states, with approximately \$17 billion in REIT entities in the islands, this bill could generate between \$60 and \$70 million per year in additional revenue. That amounts to about \$50 per resident. A lost \$50 a year in revenue per person is a sizable loss in government services that we shouldn't allow. Put in a positive way, an additional \$50 government services per person could measurably improve citizens' lives.

We could find good uses for an additional \$120 million in the biennium budget. For example, millions could go to the rental revolving fund to support affordable housing. Legislators will know how best to appropriate the additional monies; the imperative is to close this tax loophole.

Sincerely,
Claire Gearen

Chair Angus McKelvey
Vice Chair Lisa Kitagawa
House Committee on Economic Development & Business

Wednesday, February 5, 2020
9:35 AM

TESTIMONY IN SUPPORT OF HB2605 RELATING TO TAXATION OF REAL ESTATE INVESTMENT TRUSTS

Aloha Chair McKelvey, Vice Chair Kitagawa, Members of the House Committee on Economic Development & Business,

My name is Jun Shin. I am 20 years old, a member of Generation Z. I am a Sophomore at the University of Hawai'i at Mānoa, and a member of the Faith Action for Community Equity (FACE). I am testifying in **support** of **HB2605** relating to taxation of real estate investment trusts.

This has become an issue that is very close to my heart. I live in the Ala Moana area currently, so I'm personally neighbors with the Ala Moana Center, one of the well known REIT-owned properties in Hawai'i that is constantly busy. However, I am also neighbors with houseless individuals, and have also seen their struggles up close while coming home from school. I want to be able to do something to help our fellow human beings who have just as much worth as everyone else and who are struggling. To me, this is a tale of two cities, two very stark contrasts in my community that needs fixing and it cannot be ignored.

Closing the REITs tax loophole and making them pay their fair share of taxes is a much needed reform and a great step in the right direction to begin to address this divide. REITs are a well-off part of our communities. They should be helping to support the communities that they are currently operating in, and be a good neighbor. With REITs having federal tax exemptions and benefiting from our low property tax, they are in a great position to pay their fair share in taxes while still being well off. It is a common understanding among residents that it is very hard to live here. With low wages, our workers are taking on several jobs and living paycheck to paycheck, close to seeking the streets for refuge while our young people are moving out. We need to continue to work together on creating a society that works for all of us.

By doing their part, REITs can still operate and thrive in Hawai'i while being a responsible community member. By paying their share of the taxes, they are helping to build a strong Hawai'i for everyone, revenue that would be able to go to critical needs. Please continue to help in making a Hawai'i that is livable for my generation and generations to come so that we can all have an opportunity to succeed, afford our basic needs, and have families of our own, staying here and giving back to the islands. For future generations, I ask you to please **support** and **pass HB2605** out of your committee and eliminate the corporate income tax exemption on dividends paid out by REITs.

Thank you for the opportunity to testify,

Jun Shin

1561 Kanunu St.

Honolulu, HI 96814

Cell: 808-255-6663

Email: junshinbusiness729@gmail.com

HB-2605

Submitted on: 2/3/2020 7:54:03 PM

Testimony for EDB on 2/5/2020 9:35:00 AM

Submitted By	Organization	Testifier Position	Present at Hearing
Ashleigh Loa	Individual	Support	No

Comments:

Aloha, I am a member of Faith Action for Community Equity and I strongly support this bill. Please pass HB 2605 and close the loophole that exempts REITs from paying state corporate income tax. REITs already get a generous federal tax break and benefit from Hawaii's low property tax. They can operate and thrive in Hawai'i while paying state income tax, as every other Hawai'i corporation does. REITs operating in Hawaii need to do their part in supporting our community by paying their fair share of state taxes.

HB-2605

Submitted on: 2/3/2020 8:11:11 PM

Testimony for EDB on 2/5/2020 9:35:00 AM

Submitted By	Organization	Testifier Position	Present at Hearing
noel kent	Individual	Support	No

Comments:

The fact that REITs remain untaxed is a great inequity and a burden on our state finances and taxpayers. We failed last year to remedy this, but this session presents a golden opportunity to step up and make the REITs into genuine contributors to our society.

HB-2605

Submitted on: 2/3/2020 8:59:19 PM

Testimony for EDB on 2/5/2020 9:35:00 AM

Submitted By	Organization	Testifier Position	Present at Hearing
Catherine Susan Graham	Individual	Support	Yes

Comments:

Feb 4, 2020

Testifying in favor of HB 2605

Aloha Chair McKelvey and Committee Members,

I am Sheila O’Keefe, a member of Faith Action for Community Equity. Our name says it all, we are a group of 18 Faith Institutions and several other community groups who work for Community Equity. Fairness. The social good of all the residents of Hawaii, especially those who do not have a voice.

We whole-heartedly support HB 2605, a bill that would require REITs to pay income tax to the state of Hawaii. Given that a huge portion of our state real estate is owned by REITs and 99.5% of their shareholders live out of state (or even out of the country), Hawaii is not receiving any income tax based on the current law. DBEDT estimated that the State could be losing up to \$60 million a year in revenue due to this tax loophole.

I have seen Hawaii be developed with beautiful shopping centers, hotels and condos. It was just recently that I learned that we, as a state, are getting ripped off because the owners of these properties do not pay income tax to our state.

Loopholes do not benefit the hard-working residents of our state. With housing shortages and far too many homeless people living on the streets, I can foresee a very good use of the potential income that this bill would help provide.

I understand that REIT owners, (mostly large developers and resort owners) are against this bill. Of course, they are. They are naturally not in favor of any measures that will negatively affect their bottom line. But it is time for the legislators of our state, who are elected by the residents of our state, to stand up for our state and people. Stand up to big money and fully consider the welfare of our island home. These investors and REIT owners don’t live here, they just make their profits here. We are being robbed.

It is long-passed time to protect our island assets and residents.

Please pass this bill.

Mahalo,

Sheila O'Keefe

Faith Action for Community Equity

808-489-4620

HB-2605

Submitted on: 2/3/2020 9:42:06 PM

Testimony for EDB on 2/5/2020 9:35:00 AM

Submitted By	Organization	Testifier Position	Present at Hearing
Carla Allison	Individual	Support	No

Comments:

Aloha, I am a member of Faith Action for Community Equity and I strongly support this bill. Please pass HB 2605 and close the loophole that exempts REITs from paying state corporate income tax. REITs already get a generous federal tax break and benefit from Hawaii's low property tax. They can operate and thrive in Hawai'i while paying state income tax, as every other Hawai'i corporation does. REITs operating in Hawaii need to do their part in supporting our community by paying their fair share of state taxes. Mahalo for this opportunity to provide testimony in support of HB 2605.

HB-2605

Submitted on: 2/4/2020 3:07:23 AM

Testimony for EDB on 2/5/2020 9:35:00 AM

Submitted By	Organization	Testifier Position	Present at Hearing
Nanea Lo	Individual	Support	No

Comments:

Hello,

I am a member of Faith Action for Community Equity and I strongly support this bill. Please pass HB 2605 and close the loophole that exempts REITs from paying state corporate income tax. REITs already get a generous federal tax break and benefit from Hawaii's low property tax. They can operate and thrive in Hawai'i while paying state income tax, as every other Hawai'i corporation does. REITs operating in Hawaii need to do their part in supporting our community by paying their fair share of state taxes.

Thank you for this opportunity to provide testimony in support of HB 2605.

me ke aloha 'Ä• ina,

Nanea Lo

HB-2605

Submitted on: 2/4/2020 6:57:02 AM

Testimony for EDB on 2/5/2020 9:35:00 AM

Submitted By	Organization	Testifier Position	Present at Hearing
Ellen Godbey Carson	Individual	Support	No

Comments:

I am writing in SUPPORT of HB2605, with a request for an amendment. Real Estate Investment Trusts (REITs) should pay taxes in Hawaii for their profits earned off Hawaii properties. The loophole in our laws that has failed to tax REITS in the past has led to a large erosion in our tax base, since REITs own major commercial properties in Hawaii that are essentially going untaxed here. That loophole should be closed. **This bill should be amended to dedicate a major portion, up to 100% of its tax revenues, to the creation of affordable housing in Hawaii.** With that amendment, I would be in full support of this bill.

REITs own many large income-producing properties in Hawaii such as Ala Moana Center, the Hilton Hawaiian Village Resort, as well as office buildings and many other shopping centers and hotels. Together, they own property with an estimated total value of \$18 billion that earns an estimated \$1 billion in profits annually. If Hawaii's corporate tax were applied to REITs, millions of additional dollars in tax revenue would be generated. Those revenues are lost for every year we fail to tax REITs.

Meanwhile, profitable activities of REITs and other large landholders increase the price of property for everyone in Hawaii. Hawaii now faces an enormous shortage of housing that is affordable to low- and middle-income individuals and families. New housing is being built, but most of it is priced for the high-income strata. Some efforts are being made to build affordable housing for low- and middle-income levels, but much greater efforts must be made because the need is so great and the cost of housing is so high. Devoting 100% of the tax revenues from REITs would provide a sustainable source of major funding for Hawaii's critical needs for affordable housing



February 4, 2020

LATE

Rep. Angus L.K. McKelvey, Chari
Rep. Lisa Kitagawa, Vice Chair
Committee on Economic Development & Business

Re: Testimony **Opposing** HB 2605, Relating to Taxation of Real Estate Investment Trusts

Dear Chair McKelvey, Vice Chair Kitagawa, and Committee Members:

On behalf of Extra Space Storage Inc. (“Extra Space”), thank you for this opportunity to provide our testimony on HB 2605. Extra Space submits this testimony in **opposition** to this bill.

Extra Space is a publicly traded real estate investment trust (“REIT”) that is the second largest owner and operator of self-storage facilities in the United States. Extra Space owns and/or operates 1,647 self-storage properties in 40 states, which comprise approximately 1.2 million units and approximately 125.7 million square feet of rental storage space. Extra Space owns or operates seventeen self-storage facilities in Hawaii.

REITs produce substantial economic benefits to the State of Hawaii in the form of jobs, general excise tax, and real property taxes. In 2019, Extra Space paid the state more than \$1.3 million of general excise tax and almost \$1.5 million of real estate taxes.

The bill seeks to eliminate the dividends paid deduction (“DPD”) for all REITs operating in Hawaii. One of the many requirements a REIT must satisfy in order to maintain its REIT status is to distribute annually all of its taxable income to their shareholders. The shareholders then report and pay state and federal tax on those dividends. This allows for a single level of taxation at the shareholder level. In this respect, REITs are most comparable to other “pass-through” entities such as S corporations, LLCs, or partnerships, which are not separately subject to entity level income tax in Hawaii.

Enactment of this bill will result in negative consequences to the real estate industry in Hawaii. The bill will impose double taxation on REIT shareholders. This is inconsistent to the accepted federal and state tax treatment of REITs. No other state (other than New Hampshire) disallows the dividends paid deduction. This tax will put REITs at a disadvantage in relation to other “pass-through” entities that hold real estate.

This tax will essentially be passed on to Hawaii residents and businesses in the form of higher rental rates as REITs must now look for ways to offset this increased tax liability.



This tax will also discourage future investment by REITs in Hawaii as it will now be more costly to operate in Hawaii as compared to other states.

For the foregoing reasons, Extra Space **opposes** HB 2605 and asks the committee to not move forward on this or any similar bill.

Thank you for your consideration of our testimony.

Sincerely,

A handwritten signature in black ink, appearing to read 'Gwyn McNeal'.

Gwyn McNeal
Executive Vice President, Chief Legal Officer

LATE

HB-2605

Submitted on: 2/4/2020 10:08:55 AM

Testimony for EDB on 2/5/2020 9:35:00 AM

Submitted By	Organization	Testifier Position	Present at Hearing
Galen Fox	Faith Action	Support	No

Comments:

It's long past time for Hawaii to collect taxes from REITS, as we do from all other corporations. Alaska, New Mexico, Oklahoma hammer with high taxes corporations who exploit their natural resources. Our resources are the assets of paradise, in danger of being over-exploited by tourists. Time to make the corporations that make money off our precious beauty to pay their fair share. These businesses won't go away! There is only one Hawaii, no ka oi!



Chamber of Commerce HA

The Voice of Business

LATE

**Testimony to the House Committee on Economic Development and Business
Wednesday, February 5, 2020 at 9:35 A.M.
Conference Room 309, State Capitol**

RE: HB 2605, RELATING TO TAXATION OF REAL ESTATE INVESTMENT TRUSTS

Chair McKelvey, Vice Chair Kitagawa, and Members of the Committee:

The Chamber of Commerce Hawaii ("The Chamber") **does not support** HB 2605, which disallows dividends paid deduction for real estate investment trusts and applies to taxable years beginning after December 31, 2020. This bill would also sunset after December 31, 2023.

The Chamber is Hawaii's leading statewide business advocacy organization, representing about 2,000+ businesses. Approximately 80% of our members are small businesses with less than 20 employees. As the "Voice of Business" in Hawaii, the organization works on behalf of members and the entire business community to improve the state's economic climate and to foster positive action on issues of common concern.

Hawaii businesses already pay many taxes, and this bill represents yet another tax increase on our business community. REITs invest in many important local projects that would not be able to secure funding otherwise. For example, before American Assets Trust became a partner in the Waikiki Beach Walk, the property owner was not able to secure funding locally.

Additionally, REITs are also long-term property owners. They do not flip properties, which keeps our commercial real estate prices down and adds stability to the market. An increase in taxes on these companies, who owns the commercial space, would likely be passed down to the hundreds of businesses that hold leases in their buildings. As a result, these businesses would have to pass the increased cost of operating onto their customers. In other words, this measure could have a ripple effect that affects not just REITs, but also their tenants and consumers.

Finally, like any business, REITs are going to be making their decisions based on where it will be able to generate the best return on investment. By increasing the costs to doing business in Hawaii, and diminishing the return on investment, REITs are going to look to other states to fund future projects.

In consideration of these concerns, we respectfully urge you to defer HB 2605. Thank you for the opportunity to testify.

LATE

HB-2605

Submitted on: 2/4/2020 10:29:46 AM

Testimony for EDB on 2/5/2020 9:35:00 AM

Submitted By	Organization	Testifier Position	Present at Hearing
Jake Fergus	Individual	Support	No

Comments:

I am writing testimony in support of HB2605. According to a recent study by NAREIT, there is currently \$18.21B of REIT owned real estate in Hawaii consisting of approximately 748 properties, many of which are high quality real estate assets (for example, see Ala Moana Center). All except one REIT is based on the mainland or abroad.

There is a loophole in our state income tax law that allows REIT to shift their taxable profits to other states or abroad, which means our state loses out on tax revenue generated by these highly profitable entities.

I strongly urge our legislators to pass this bill which will require REITs to pay their fair share to our state. REITs still enjoy significant federal tax advantages over traditional corporations and other taxable entities, and would not suffer any material disadvantages from the passing of this bill.

LATE

HB-2605

Submitted on: 2/4/2020 10:30:15 AM

Testimony for EDB on 2/5/2020 9:35:00 AM

Submitted By	Organization	Testifier Position	Present at Hearing
Wally Inglis	Individual	Support	Yes

Comments:

To: Chair McKelvey and Members of EDB Committee:

I write in strong support of HB 2605, relating to REITS. Both as an individual and a supporter of the efforts of Faith Action for Community Equity, I urge you to pass out this bill.

During the past session, the Legislature sent a clear message that it is time for REITS to pay their fair share of corporate taxes. Please continue your efforts during the 2020 session to see that this bill is finally enacted into law.

Aloha,

Wally Inglis

Palolo Valley

February 3, 2020

Representative Angus L.K. McKelvey, Chair
Representative Lisa Kitagawa, Vice Chair
House Committee on Economic Development & Business

RE: HB 2605 Relating to Taxation of Real Estate Investment Trusts – In Opposition
Wednesday, February 5, 2020; 9:35 AM; Conference room 309

Aloha Chair McKelvey, Vice Chair Kitagawa and Members of the Committee:

On behalf of Douglas Emmett, Inc. (“Douglas Emmett”), we appreciate this opportunity to present testimony expressing concerns on HB 2605, which disallows a dividends-paid deduction (“DPD”) for real estate investment trusts (“REITs”).

Douglas Emmett has been investing in Oahu for over fifteen years. We currently own over 2,000 workforce rental apartment units and recently invested over \$120 million to build approximately 500 rental apartments in Moanalua. The development employed hundreds of local construction workers and created desperately needed workforce housing.

Douglas Emmett is currently working to add approximately 500 more rental apartments in downtown Honolulu by converting one of our office properties into workforce housing. We anticipate investing between \$80 million and \$100 million in the Bishop Place project, which will employ a large number of kama’aina union construction workers. The first units should come online in 2020 with rents targeted to serve local families in the 80% to 120% Average Median Income range. Douglas Emmett also owns two other office properties in downtown Honolulu, and we employ over 275 local residents.

We are concerned that this bill’s targeted double taxation on REIT shareholders will negatively impact REIT investment into Hawaii. The bill incentivizes REITs to invest in states that recognize the intent of Congress for REITs to be a single tax entity. If HB 2605 is enacted, Hawaii will likely lose one of the best sources of capital to build workforce housing and improve our communities. The bill will also have a negative economic impact on the construction trades, building suppliers, architects, and engineers.

As a stakeholder in Hawaii, Douglas Emmett believes HB 2605 will eliminate an important source of capital that generates substantial local economic activity. Inasmuch as this bill appears to be outside of the best interest of the residents of Hawaii and the objectives of the State to encourage the investment into, and growth of, Hawaii’s economy, we respectfully ask that you defer HB 2605.

Respectfully,



Kevin Crummy
Chief Investment Officer



Michele Aronson
Senior Vice President

LATE

HB-2605

Submitted on: 2/4/2020 1:19:13 PM

Testimony for EDB on 2/5/2020 9:35:00 AM

Submitted By	Organization	Testifier Position	Present at Hearing
Bruce Anderson	Individual	Support	No

Comments:

I support this bill to ensure fair taxation in our state.



LATE

February 4, 2020

Representative Angus L.K. McKelvey, Chair
Representative Lisa Kitagawa, Vice Chair
House Committee on Economic Development & Business

Comments and Concerns in Strong Opposition to HB 2605, Relating to Real Estate Investment Trusts (REITs) (Disallows Dividends Paid Deduction for REITs; Applies to taxable years beginning after 12.31.2020; sunsets 12.31.23.)

Wednesday, February 5, 2020, 9:35 a.m., in Conference Room 309

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 utility companies. 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.

HB 2605. The purpose of this bill is to amend subsection (b) of Section 235-2.3, Hawaii Revised Statutes, to deem Internal Revenue Code Section 857(b)(2) (with respect to the dividends paid deduction for real estate investment trusts) inoperative, thereby disallowing the dividend paid deduction for REITs. Should HB 2605 be adopted, REITs will be taxed on their net income in Hawaii, while REIT shareholders will continue to be taxed on dividend income received, resulting in a double tax.

LURF's Position. LURF acknowledges the intent of this and prior, similar iterations of this measure given what may be perceived to be the potential for tax avoidance and abuse by foreign/mainland corporations and wealthy individuals through real estate ownership arrangements structured through REITs, however, stated justifications for this bill have not, to date, been proved or supported by any credible facts or evidence.

The State’s Final Report on the Impact of REITs in Hawaii Has Failed to Validate the Alleged Purpose of and Need for this Proposed Legislation.

Given that an unwarranted change of a universal tax rule in place since 1960 could undoubtedly affect investments made by REITs in Hawaii, significantly reduce the availability of capital in this State, as well as result in other economic repercussions, the Legislature determined in 2015 that it was necessary and prudent to require support for this type of measure prior to considering its passage. Thus, Act 239, Session Laws of Hawaii 2015, was passed which required the State Department of Business, Economic Development & Tourism (DBEDT) and the State Department of Taxation (DOTAX) to study the impact of REITs in Hawaii, and to present material facts and evidence which could show that such proposed legislation is in fact needed, and whether the State’s economy will not be negatively affected because of taking the action proposed.

An interim report was released in December 2015 (the “Interim Report”),¹ followed by a final report issued in September 2016 (the “Final Report”),² however, even the Final Report is based on assumptions and estimates; relies on inconclusive results of surveys admittedly taken with a small sample size and low response rate; and is fraught with uncertainties, inconsistencies and weighting errors, making it unfeasible and ill-advised to rely upon for presenting any conclusive calculations or impacts.

Inquiries which critically must be, yet have not been proficiently or accurately addressed in the Final Report, include the amount of income the State would in fact receive as a result of the proposed legislation,³ especially given the likelihood that REIT investment in Hawaii will in turn decline (i.e., whether the proposed measure is fiscally reasonable and sound); and whether it would be possible to replace the billions of dollars in investments currently being made by REITs should they elect to do business elsewhere if this proposed legislation is passed.

Given the inadequacy, inaccuracy and unreliability of the tenuous findings contained in the Interim and Final Reports, as well as the complete failure of said Reports to come to any meaningful and valid conclusions required to be made pursuant to Act 239, it should be brought to this Committee’s attention that another study on the economic impacts of REITs in Hawaii dated December 2015, was prepared by economic expert Paul H. Brewbaker, Ph.D., CBE for the National Association of Real Estate Investment Trusts (the “Brewbaker Study”).⁴ The Brewbaker Study concludes that the repeal of the

¹ Department of Business, Economic Development & Tourism Research and Economic Analysis Division. *Real Estate Investment Trusts in Hawaii: Preliminary Data and Analysis - Interim Report*. December 2015.

² Department of Business, Economic Development & Tourism Research and Economic Analysis Division. *Real Estate Investment Trusts in Hawaii: Analysis and Survey Results*. September 2016.

³ LURF understands that even the State DOTAX does not know how much tax income the government might receive as a result of the proposed legislation.

⁴ Paul H. Brewbaker, Ph.D., CBE. *Economic Impacts of Real Estate Investment Trusts in Hawaii*. December 2015.

dividend paid deduction (DPD) for REITs in Hawaii would likely result in a net revenue loss to the State due to a number and combination of negative consequences which would be experienced by the local economy.

In view of the inconsistency between findings contained in the Final Report and the Brewbaker Study, LURF believes it would be irresponsible for this Committee to consider, let alone support HB 2605 which may potentially stifle, if not reverse the current growth of the State's economy, in reliance solely upon the untenable findings of the Final Report and must respectfully urge this Committee to at the very least, conduct an independent investigation and analysis of all the available facts and information relating to the disallowance of the DPD, and the potential financial and economic consequences thereof, prior to making any decision on this bill.

In view of the inability of the Final Report to conclusively support the validity of this measure, LURF must oppose HB 2605 based on the following reasons and considerations:

1. The “Double-Tax” Resulting from this Proposed Measure is Contrary to the Underlying Intent of REITs.

REITs are corporations or business trusts which were created by Congress in 1960 to allow small investors, including average, everyday citizens, to invest in income-producing real estate. Pursuant to current federal and state income tax laws, REITs are allowed a DPD resulting in the dividend being taxed a single time, at the recipient level, and not to the paying entity. Most other corporations are subject to a double layer of taxation – on the income earned by the corporation and on the dividend income received by the recipient.

Proponents of this measure attempting to eliminate the DPD, however, appear to ignore that the deduction at issue comes at a price. REITs are granted the DPD for good reason - they are required under federal tax law to be widely held and to distribute at least 90% of their taxable income to shareholders,⁵ and must also comply with other requirements imposed to ensure their focus on real estate. In short, REITs earn the DPD as they must comply with asset, income, compliance and distribution requirements not imposed on other real estate companies.

According to the Brewbaker Study, repealing the DPD for REITs would subject Hawaii shareholders to double taxation and may reduce future construction and investment by REITs locally, thereby resulting in revenue loss to the State.⁶ Moreover, replacement investor groups may likely be tax-exempt institutions such as pension plans and foundations which would generate even less in taxes from their real estate investments.⁷

⁵ The State of Hawaii thus benefits from taxes it collects on dividend distributions made to Hawaii residents.

⁶ *Brewbaker Study* at pp. 1, 32, 38.

⁷ *Id.*

2. HB 2605 is Contrary to the Tax Treatment of REITs Pursuant to Current Federal Income Tax Rules and Laws of Other States with an Income-Based Tax System.

HB 2605 would enact serious policy change that would create disparity between current Hawaii, federal, and most other states' laws with respect to the taxation of REIT income.

The laws of practically every state with an income-based tax system now allow REITs a deduction for dividends paid to shareholders. Hawaii, as well as other states which impose income taxes currently tax REIT income just once on the shareholder level (not on the entity level), based on the residence of the shareholder that receives the REIT dividends and not on the location of the REIT or its projects.

By now proposing to double tax the REITs that do business in Hawaii as well as their shareholders, HB 2605 would upset the uniformity of state taxation principles as applied between states. Other states which have similarly explored the possibility of such a double tax over the past years have rejected the disallowance of the DPD for widely held REITs.

3. Hawaii REITs Significantly Contribute to and Benefit the Local Economy.

Elimination of the DPD would result in a double taxation of income for Hawaii REITs which would certainly mitigate, if not extinguish interest and incentive in investing in Hawaii-based REITs, which currently contribute significantly to Hawaii's economy.

Results from the Final Report indicate that even as of September 2016, approximately 42 REITs operating in Hawaii reportedly held assets in the amount of an estimated \$7.8 billion at cost basis⁸, which has resulted in substantial economic activity in local industries including construction, retail, resort, healthcare and personal services, as well as employment for many Hawaii residents, and considerable tax revenues for the state and city governments. Such tax revenues include State General Excise Tax (GET) on rents and retail sale of goods, business income tax on profits made by tenants, income tax from employment of Hawaii residents, and millions of dollars in property taxes.

Proponents of this bill should be mindful that significant economic growth experienced in this State over the past years, and which is expected to continue in the future, is undoubtedly attributable in part to REIT investment in Hawaii. Outrigger Enterprises partnered with REIT American Assets Trust to successfully develop the Waikiki Beach Walk. General Growth' Properties' expansion and renovation of the Ala Moana Shopping Center, as well as its partnering with Honolulu-based, local companies (The MacNaughton Group, The Kobayashi Group and BlackSand Capital) to develop the Park Lane residential condominium project is another example. The capital invested in that project to construct additional retail space and luxury residences reportedly exceed \$1 billion, and the development will have created an estimated 11,600 full- and part-time jobs and over \$146 million of state revenue. Taubman Centers, Inc., another REIT, also

⁸ *Final Report* at pages 3, 15-16.

partnered with CoastWood Capital Group, LLC to revitalize Waikiki through the redevelopment of the International Market Place at a cost of approximately \$400 million.

REIT projects have helped to support Hawaii's construction industry immensely⁹ by providing thousands of jobs, and continue to significantly contribute to the local economy through development of more affordable housing (more than 2,000 rental housing units for Hawaii's families, such as the Moanalua Hillside expansion of more affordable housing rentals), student housing near the University of Hawaii, health care facilities, offices, shopping centers (Ala Moana Center addition; Pearlridge Center renovations; Ka Makana Ali'i), and hotels.

Despite claims made by detractors, the multibillion-dollar investments and contributions to Hawaii's economy made by REITs may not be so easily generated through other means or resources. Attracting and obtaining in-state capital for large projects is very difficult. The State should also be concerned with the types of entities willing and able to invest in Hawaii and should be wary of private investors looking only to make quick gains when the market is booming. Because federal regulations preclude REITs from "flipping" properties, REITs are by law, long-term investors which help to stabilize commercial real estate prices, and which are also likely to become a part of the local community.

4. The Disallowance of the DPD Proposed by this Bill will Unfairly Affect REITs and the Small Investors Which Have Already Made Substantial Investments in Hawaii.

Disallowance of the DPD and resulting increased taxation of REITs is expected to reduce investment returns as well as dividend payments to shareholders, which will no doubt have a significant negative effect on future investment by REITs in Hawaii.

Proponents of this bill attempt to minimize the negative consequences of disallowing the DPD by claiming that very few Hawaii taxpayers invest in REITs with property in Hawaii, however, LURF understands that in 2014 over 9,000 Hawaii investors had investments in over 70 public, non-listed REITs and received almost \$30 million in distributions, and that tens of thousands more directly or indirectly own shares in stock exchange-listed REITs.

Supporters of this measure also ignore the fact that tax law changes proposed by HB 2605 will unfairly impact those publicly traded REITs which have already made substantial investments in Hawaii and have contributed greatly to the State's economy in reliance on the DPD, which, as discussed above, is considered a fundamental principle of taxation applicable to REITs.

⁹ In the past five years, REIT-related construction activity alone is estimated to have generated \$3 billion in Hawaii GDP.

If passed, this measure would strongly discourage future investment by REITs in Hawaii, which would ultimately impact jobs, reduce tax revenue and result in significant consequences for the State's future economy.

Conclusion. LURF's position is that the findings of the Final Report which have not been updated or amended since issuance, have failed to credibly present any material facts or circumstances to prove that this proposed legislation is in fact necessary, or that the State's economy will significantly improve because of taking the action proposed. The intent and application of HB 2605 thus arguably remain unreasonable, unwarranted, and exceedingly anti-business.

Act 239, SLH 2015 was specifically enacted by the State Legislature to validate the alleged purpose of disallowing the DPD. The results of the Final Report are thus considered vital to confirm the need for this type of measure. Therefore, based on the inability of said Report to convincingly and conclusively determine that the State's economy will be negatively impacted as a result of the action proposed, or that this proposed legislation is otherwise warranted, and given that an unjustifiable change of a universal tax rule in place since 1960 could significantly reduce the availability of capital in this State, as well as result in other negative economic repercussions, LURF must **strongly oppose HB 2605**, and respectfully requests that this bill be **held in this Committee**.

LATE

Testimony of
Pacific Resource Partnership

House Committee on Economic Development & Business
The Honorable Angus L.K. McKelvey, Chair
The Honorable Lisa Kitagawa, Vice Chair

HB 2605 Relating to Taxation of Real Estate Investment Trusts

Wednesday, February 5, 2020
9:35 A.M.
Conference Room 309

Aloha Chair McKelvey, Vice Chair Kitagawa, and Members of the Committee:

Pacific Resource Partnership (PRP) **opposes** HB 2605, which disallows dividends paid deduction for real estate investment trusts (REITs).

REITs were established by Congress in 1960 to enable all sizes of investors to invest in real estate. Like other corporations, REITs are subject to corporate income tax rules. However, unlike other corporations, REITs must meet several restrictive regulatory requirements which include a requirement under federal tax law to distribute at least 90% of their taxable income to shareholders as dividends. Currently, with the exception of New Hampshire, REITs can claim a dividend paid deduction in all states which allows them to distribute dividends to shareholders without paying a corporate tax—individual shareholders will pay the tax on these dividends in their state of residence. REITs can retain up to 10% of taxable income but must pay a corporate tax on what they retain.

REITs invest in long-term projects that help communities grow including, but not limited to, rental housing, medical facilities, shopping centers and commercial buildings, all of which provide important services and functions to the public. REIT-funded projects, like the expansion of Ala Moana Center and redevelopment of the International Market Place, generate GET revenue for the state, along with jobs for Hawaii's residents.

REITs also play an important role in solving Hawaii's housing crisis by developing more workforce rental housing for Hawaii's residents. For example, Douglas Emmett is a REIT, with headquarters in California and investments in Hawaii, that completed the revitalization of the Moanalua Hillside Apartments by adding 491 workforce rental units. Currently, Douglas Emmett is converting 1132 Bishop, a 25-story downtown Honolulu office building, into approximately 500 new workforce rental apartments for families in the 80 percent to 120 percent Average Median Income (80% - 120% AMI) range.

During the February 12, 2019 House Committee on Consumer Protection and Commerce hearing, a Department of Taxation (DoTax) representative testified before the committee on a similar bill that disallowing the dividends paid deduction for REITs would raise approximately \$2.5 million the first year and \$10 million annually thereafter. However, the DoTax representative cautioned that the actual revenue raised could be lower if the REITs take advantage of all the deductions to which they are entitled.



(Continued From Page 1)

More importantly, we share industry concerns that if HB 2605 were to become law, REITs that do business in Hawaii may cease or decrease investing on future projects and REITs that currently partner with nonprofits to acquire and/or develop affordable and sustainable rental housing outside Hawaii may choose not to invest in Hawaii. Given the affordable housing crisis in Hawaii, we need more investors who are willing to create or preserve homes to residents in low-and moderate-income communities and, nationally, REITs have helped to boost the supply of workforce housing. REITs can and should play a similar role in Hawaii, but will be less inclined should HB2605 become law.

Given the above, PRP respectfully requests that this Committee defer HB 2605. Thank you for the opportunity to submit written testimony.



THE HOUSE

Committee on Economic Development and Business

Representative Angus L.K. McKelvey, Chair

Representative Lisa Kitagawa, Vice Chair

State Capitol, Conference Room 309

Wednesday, February 5, 2020; 9:35 a.m.

**STATEMENT OF THE ILWU LOCAL 142 ON H.B. 2605
RELATING TO TAXATION OF REAL ESTATE INVESTMENT TRUSTS**

The ILWU Local 142 **supports** H.B. 2605, which disallows dividends paid deduction for real estate investment trusts and applies to taxable years beginning after 12/31/2020.

The State is losing out on millions of dollars in taxes because the tax deduction for dividends paid by Real Estate Investment Trusts. REITs are able to avoid paying state taxes as long as they distribute 90% of their taxable income to shareholders, who then pay taxes only in their home states. Most of the REITs with real estate holdings in Hawaii have shareholders/investors who do not live in Hawaii. Since REITs themselves currently enjoy a deduction for dividends paid, and most shareholders are not Hawaii taxpayers, the State receives virtually NO taxes from real estate activity of REITs in Hawaii.

The State can certainly use another revenue source. Requiring REITs to pay income taxes would be one means of generating revenues to support the services and programs needed to address a myriad of issues facing our residents—including public education, early childhood education, homelessness and affordable rental housing, access to quality health care, and support for the elderly and disabled as well as their caregivers.

Those who oppose repealing the deduction argue that REIT investment will dry up. We think this is most unlikely. Real estate in Hawaii is highly profitable. Investors would be foolish to pull out of Hawaii simply because of taxes they must pay. Paying taxes should be considered a cost of doing business. Everyone should pay their fair share of taxes to benefit the entire community. In fact, if this bill is not passed, more corporations with real estate holdings may seek to convert into Real Estate Investment Trusts in order to avoid paying taxes. If that happens, the State could potentially lose even more tax revenue.

The ILWU urges passage of H.B. 2605. Thank you for the opportunity to offer testimony on this measure.

LATE

HB-2605

Submitted on: 2/4/2020 10:07:30 PM

Testimony for EDB on 2/5/2020 9:35:00 AM

Submitted By	Organization	Testifier Position	Present at Hearing
Kim Watts	Individual	Support	No

Comments:

Aloha Senators, Chair, and Councilmembers. I urge you to please support HB2605 so that these taxed funds can be used towards affordable housing. Mahalo in advance.

Kim Watts

**HAWAII OPERATING ENGINEERS
INDUSTRY STABILIZATION FUND**



*Uniting our strengths and working together
for a better tomorrow.*

Affiliated AFL-CIO
OPEIU - 3 - AFL-CIO (3)

LATE

House of Representative Committee on Economic Development & Business

Honorable Angus L.K. McKelvey, Chair

Honorable Lisa Kitagawa, Vice Chair

Honorable Members of the House Committee on Economic Development & Business

February 3, 2020

RE: OPPOSITION OF H.B. 2605 RELATING TO TAXATION OF REAL ESTATE INVESTMENT TRUSTS

The Operating Engineers Industry Stabilization Fund is deeply concerned about what will happen if Hawaii breaks from the federal tax code and repeals the deduction real estate investment trusts receive on the dividends paid to their shareholders. These REIT shareholders include thousands of Hawaii residents who would see their pensions and future incomes diminished by this legislation.

The union organization we represent, Operating Engineers Local 3 (OE3) is also highly invested in REITs and a REIT related project on the Big Island. This type of legislation will have an adverse effect on our project and future investments in Hawai'i.

Officials from the Hawaii State Department of Taxation (DoTax) have stated publicly that these types of REIT taxation bill would produce an estimated \$2.2 million in additional income tax revenue the first year and less than \$10 million per year after that. However, DoTax noted this estimate does not represent all the deductions REIT-owned companies could take if this bill becomes law, the result of which would be a substantial decline in the tax revenue generated and therefore underfund the proposed "Returning Resident Down Payment Program."

Hawai'i will puts at risk \$16 million or more of hotel REIT General Excise Tax (GET) revenue this type of bill becomes law.

- Federal law requires all REITs, including hotel REITs, to have 75% of their annual revenues come from rent and/or other real estate-related sources.
- In order for a REIT that owns a hotel to qualify as a REIT, the REIT has to earn rent. It can do so by creating a taxable subsidiary (which is subject to federal and Hawaii corporate income tax), which pays lease rent (at market rates) for the property to the REIT.
- Those taxable subsidiaries, in turn, are prohibited from operating hotels and must hire hotel operators to manage day to day operations.

- GET revenue is captured from each of these layers of ownership/management. Available data show this additional GET revenue is about \$16 million for Hawai'i each year that non-REIT hotels do not pay.
- If this bill passed, hotel REITs will reassess their form of operation in Hawai'i, potentially putting at risk this \$16 million in GET, the potential loss of which could equate to an estimated net loss of \$6 million for Hawai'i when taking into account DoTax's \$10 million revenue estimate.

REITs create affordable workforce rental housing in Hawai'i.

- Douglas Emmett is the largest developer of affordable workforce rental apartments in Hawai'i.
- Douglas Emmett recently built 491 new units at its Moanalua Hillside Apartment Community in Aiea.
- Douglas Emmett just announced it will be converting office space at 1132 Bishop Street into 500 affordable workforce rental units for those making 80-120% of the median area income.

44% of Hawai'i households own REIT stock through their retirement savings and other investment funds.

- Many Hawai'i residents rely on REIT stock, both in Hawai'i and other markets, for their pensions.
- Bank of Hawaii and First Hawaiian Bank hold millions of dollars worth of shares of REITs on behalf of their clients.
- Hawai'i pension plans, like those of Queen's Health System and Hawaiian Airlines, Inc. have allocated millions of dollars of their portfolios to REITs.

For all these reasons, we are deeply concerned about this bill and its impact on our industry, even as we see slower growth of our economy. Scaring people away from funding projects in Hawai'i is the last thing we need now as an industry and a state. I urge you to hold this bill for the sake of Hawaii's working families.

Sincerely,

A handwritten signature in black ink that reads "Pane Meatoga III". The signature is written in a cursive style with a horizontal line extending from the end.

Pane Meatoga III
Community Liaison
Hawaii Operating Engineers Industry Stabilization Fund

LATE

HB-2605

Submitted on: 2/5/2020 1:09:45 AM

Testimony for EDB on 2/5/2020 9:35:00 AM

Submitted By	Organization	Testifier Position	Present at Hearing
Cheryl Guzikowski	Individual	Support	No

Comments:

Aloha, I strongly support this bill. Please pass HB 2605 and close the loophole that exempts REITs from paying state corporate income tax. REITs already get a generous federal tax break and benefit from Hawaii's low property tax. They can operate and thrive in Hawai'i while paying state income tax, as every other Hawai'i corporation does. REITs operating in Hawaii need to do their part in supporting our community by paying their fair share of state taxes.

When thinking about who we tax and why, I think it is EXTREMELY important to remember that everyday families are struggling. Our state is broke and we are constantly looking for ways to fund the projects needed. So, the people who can afford least to be hit with bills should not be the ones being asked to fund our state the most.

From Civil Beat: "Some of the largest landowners in our state — including the Ala Moana and Pearl Ridge Shopping Centers and the Hilton Hawaiian Village — do not pay Hawaii corporate income tax. REITs own about \$18 billion worth of properties in Hawaii, and DBEDT estimates that the corporate tax on income earned from these REITs properties would total in the tens of millions of dollars annually.

The anti-taxation of REITs' argument: that they shouldn't have to pay Hawaii corporate income tax because they also pay general excise tax and property tax is absurd and disingenuous at best. That's as if the REIT executives stated they should not be paying Hawaii personal income tax because they already pay property tax on their houses and GET on every purchase from Longs.

And as a practical matter, close to 100% of REIT earnings are distributed annually as dividends to their shareholders. States with income taxes receive a tax on the dividends paid to their resident shareholders on REIT income.

Hawaii's problem is that we have the largest amount of REIT investment in the country per capita, but a minuscule portion of REIT shareholders — only about 3% of Hawaii REIT shareholders reside in this state. Thus, the income tax from Hawaii real estate that clearly deserves to be paid to Hawaii is in fact being paid to other states."

When I heard about how the Ko'olina area pays \$0 in property taxes and has minuscule parking available for residents to have access to the ocean due to a sweetheart deal

with Hanabusa. (20 spots each pool compared to the ample amount of parking available at Turtle Bay for example) AND how they have the nerve to ask the state to move Waimanalo Gulch Landfill because of their 'investment' I am frustrated that we do not require more of these corporations to invest in the community they 'care' about. When I find out they are giving \$0 towards the rail project and HART (a project they will benefit from exponentially). This shows just how much money and power can corrupt. I am ashamed that our state would allow big corporations to take advantage of our Aina in this way over and over and over again. We must find ways to use taxation to keep our mainland landowners invested in our precious land and people.

Taxing the Real Estate Investment Trust is not the same as taxing the individual business owners within the malls and hotels. It's taxing 97% of the wealthy investors who make money on those businesses. If these REIT's being tax free was a good idea for Hawaii, than why is it that so many business locations within these centers stay shuttered? How are they making money without having businesses in them? Tax incentives must guide this clearly counter intuitive situation.

The sheer amount of waste and waste water generated in these areas merits their taxation. Rather than tax every local and individual property owner for waste water treatment, why not tax the malls and the hotels who cater to the tourists (i.e. non tax payers) and whose waste puts a burden on our whole island. When over 9 million people come here every year versus the 1 to 1.7 million residents, consider which of those numbers is larger and thus which group should pay more to compensate for their fare share.

If making sure local families can stay in Hawaii is truly the mission and the goal, then finding ways to decrease their cost of living while finding moneys for the state to operate MUST be the way that we look at every taxation opportunity and also how we govern.

Mahalo for this opportunity to provide testimony in support of HB 2605.

LATE

HB-2605

Submitted on: 2/5/2020 6:15:12 AM

Testimony for EDB on 2/5/2020 9:35:00 AM

Submitted By	Organization	Testifier Position	Present at Hearing
Randy Ching	Individual	Support	No

Comments:

Aloha Chair McKelvey, Vice Chair Kitagawa, and members of the committee,

I am a member of Faith Action for Community Equity and I strongly support this bill. Please pass HB 2605 and close the loophole that exempts REITs from paying state corporate income tax.

REITs already get a generous federal tax break and benefit from Hawaii's low property tax. They can operate and thrive in Hawai'i while paying state income tax, as every other Hawai'i corporation does. REITs operating in Hawaii need to do their part in supporting our community by paying their fair share of state taxes.

Mahalo for this opportunity to provide testimony in support of HB 2605.

Randy Ching

Honolulu



MAUI
CHAMBER OF COMMERCE
VOICE OF BUSINESS

LATE

**HEARING BEFORE THE HOUSE COMMITTEE ON
ECONOMIC DEVELOPMENT & BUSINESS
HAWAII STATE CAPITOL, HOUSE CONFERENCE ROOM 309
WEDNESDAY, FEBRUARY 5, 2020 AT 9:35 A.M.**

To The Honorable Angus L.K. McKelvey, Chair;
The Honorable Lisa Kitagawa, Vice Chair; and
Members of the Committee on Economic Development & Business,

**TESTIMONY IN OPPOSITION TO HB2605 RELATING TO
TAXATION OF REAL ESTATE INVESTMENT TRUSTS**

Aloha, my name is Pamela Tumpap and I am the President of the Maui Chamber of Commerce, with approximately 650 members. I am writing share our opposition to HB2605.

The Maui Chamber of Commerce opposes HB2605 to disallow dividends paid deduction for real estate investment trusts (REITs). REITs are important to our state's economy as they provide outside capital. They are also important for our economic development as they frequently develop shopping centers and commercial buildings that benefit businesses and workforce rental housing that is desperately needed by residents. Passing this bill will hurt Hawaii's REITs and make investors less likely to invest in our state.

Therefore, we oppose this bill and ask that it be deferred. We appreciate the opportunity to testify on this matter.

Sincerely,

Pamela Tumpap

Pamela Tumpap
President

To advance and promote a healthy economic environment for business, advocating for a responsive government and quality education, while preserving Maui's unique community characteristics.

LATE

HB-2605

Submitted on: 2/5/2020 9:38:53 AM

Testimony for EDB on 2/5/2020 9:35:00 AM

Submitted By	Organization	Testifier Position	Present at Hearing
Michael deYcaza	Individual	Support	No

Comments:

Please end corporate welfare.