DEPARTMENT OF BUDGET AND FISCAL SERVICES
**CITY AND COUNTY OF HONOLULU**
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MAYOR

MARY PATRICIA WATERHOUSE
DIRECTOR

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January 30, 2008

The Honorable Maile S.L. Shimabukuro and
Members of the Committee on Human Services & Housing
House of Representatives
State Capitol, Room 329
Honolulu, Hawaii 96813

Dear Chair Maile S. L. Shimabukuro and Committee Members:

Subject: H.B. 2394 Relating to Taxation

Thank you for the opportunity to testify in opposition to H.B. 2394. This bill proposes to allow certain counties, and more specifically the City and County of Honolulu, to levy an additional county surcharge on the State general excise tax of up to one percent, provided the City repeals all ad valorem property tax ordinances with respect to improved residential and apartment tax categories, but excluding vacant land and other property tax categories. This bill also provides for a reduction in rental rates in participating counties to offset the reduction in the real property taxes paid by landlords.

Replacement of portions of the real property tax program with a "riskier" excise tax would likely cause the City's debt costs for bonds to increase substantially. The City also could be forced to re-issue, at higher costs, existing bonds which secured favorable rates due to the City's total control of property tax revenues and our ability to adjust tax rates when necessary. The City requires flexibility in its budget process and reliability in its revenue funding. The excise tax is not as reliable a vehicle for the City's revenue base. And, bond raters steadfastly cite their concerns when proposals are introduced to limit the reliability of the City's source of funding.

Furthermore, the one percent surcharge would not cover the revenue loss realized by the elimination of the tax on residential and apartment properties. Since recent studies indicate each one-half percent increase in the general excise tax generates $150 million in taxes, a minimum increase in the general excise tax of 1.5 percent would be required to replace the residential property tax revenue.

Additionally, any future shortfall in the excise tax due to an economic downturn could cause enormous disruptions in City services and would require the remaining property classifications to shoulder the burden of this risk of revenue shortfall with even higher tax rates.

The exclusion of residential type properties from the City's real property taxation program may invite challenges and expose the City to potential lawsuits by non-residential property owners that may allege they are carrying an unfair burden of the City's property tax.

We appreciate your considering our concerns regarding H.B. 2394 and ask that it be held. We will be glad to answer any questions you may have.

Sincerely,

Mary Patricia Waterhouse, Director
Budget and Fiscal Services

Working Together for Hawaii

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Hawaii Government Employees Association
AFSCME Local 152, AFL-CIO

The Twenty-Fourth Legislature, State of Hawaii
Hawaii State House of Representatives
Committee on Human Services & Housing

Testimony by
Hawaii Government Employees Association
January 31, 2008

## H.B. 2394 – RELATING TO TAXATION

The Hawaii Government Employees Association opposes the purpose and intent of H.B. 2394. This bill would permit the City and County of Honolulu to replace the property tax with a surcharge on the state tax up to 1%. If the county decides to implement the surcharge, it must repeal all ad valorem property tax ordinances on improved residential and apartment tax categories.

We have several concerns about this bill. First, the 1% surcharge may not provide the same amount of revenue as property taxes currently collected on improved residential and apartment tax classifications. Reducing such a major tax revenue source will require other significant tax policy changes, including the possibility of higher property tax rates on other property tax classifications (e.g. hotel and resort, commercial, industrial).

Second, any change from the current property tax system to one financed by increased general excise taxes would increase the level of uncertainty in annual budgeting. As a result, unanticipated shortfalls could easily occur. The property tax is a relatively stable revenue source compared to the sales or excise tax. Greater reliance on historically volatile revenue sources will result in more volatile annual budgeting. A related concern is that the excise tax, which is based on consumption, tends to be regressive in that it takes a larger percentage of income from a low or moderate-income family than a higher-income family. Thank you for the opportunity to testify in opposition to H.B. 2394.

Respectfully submitted,

Kevin Mulligan

for Nora A. Nomura
Deputy Executive Director

**From:** Chuck Prentiss [mailto:prentissc001@hawaii.rr.com]
**Sent:** Monday, January 28, 2008 11:11 PM
**To:** HSHtestimony
**Subject:** Testimony on HB2394

# TESTIMONY IN SUPPORT

HB2394 Relating to Taxation
Hearing January 31, 2008
HSH 8:40 AM, Room 329

Charles A. Prentiss, Ph.D
519 Wanaao Road, Kailua HI 96734
prentissc001@hawaii.rr.com

The property tax on homes and apartments is considered to be the most regressive tax, and in Honolulu it has doubled since 2003. It is also one of the most unfair taxes. How fair is it that large tax increases occur because a few out-of-State people pay inflated prices for a second home in Hawaii, or a fractional part of one? How fair is it that resident homeowners get an exemption, but renters do not? The Honolulu City Council reduced the residential and apartment property tax rate this year, but because of higher assessments most tax bills still went up.

The use of an ad valorem tax base has been the norm for many decades on the mainland and in Hawaii. It has been the main source of revenue for counties and local municipalities. However, nationwide, there have always been problems with the residential and apartment categories such as easily changed rates, unfair assessments, and actual political scandals. The tax was first used in the mid-west where the value of agricultural property was a good indication of how much a farmer could afford to pay. But now people in other states have actually had to give up their family homes because they could not afford the tax. A recent letter to the editor in a local newspaper indicated that this is beginning to happen here.

Locally we have seen attempts to salvage what is a broken system with all sorts of exemptions and credits which never do get at the real problem that **the market value of a house or apartment is not a fair measure of the ability to pay for the financing of city government.** People with widely differing incomes may pay the same tax. Neighbors living on social security may pay the same tax as someone next door making $100,000 per year. In addition, witness the problem the Honolulu City Council had last year when they wanted to do something to help renters, but could not find a way to do it.

## THE CALIFORNIA SOLUTION

But things are finally beginning to change, spurred by the voters of California who, in 1978, approved a system where property values are addressed in a much different way known as Proposition 13. A Proposition 13-type reform could significantly benefit the homeowners and renters of Honolulu. However, the problem with these systems is that they have not provided sufficient revenue for government to operate the necessary services it must provide, and has led to many increases in user fees which are even more undesirable and regressive. In Hawaii, because the State funds our public schools, altering the property tax assessment method would not affect the schools as it can in other states, but it could have an effect on a county's ability to adequately fund public employee salaries, and on the provision of services such as reconstructing sewerage systems, etc. This is why our local government and others such as public employee unions can be expected to resist the California-type procedures.

**HOPE FOR HOMEOWNERS AND RENTERS**

Fortunately, there is a better way. Available data shows that it may be a relatively simple task to completely do away with the residential and apartment property tax in Honolulu while still providing funds needed for government services. This would be a revenue neutral system that would also provide a **huge tax cut** for everyone with a roof over their heads.

Consider these facts: This fiscal year, the City and County of Honolulu expects to raise about $430 million from residential and apartment properties (based upon the new $3.29 per $1000 tax rate and the $200 one-time rebate). In the fiscal year ending June 30, 2006, the State collected $1.68 billion from the then 4% GET on Oahu1[1]. That includes the 4% GET on rental housing. Since we would not want to increase the GET on rental housing, if we subtract collections the State received from these rentals on Oahu, the amount collected would have been $1.62 billion2[2]. Divide that by four, and we see that each 1% of GET on Oahu would have raised over $406 million, if we don't include what was received from rentals. So, if the City and County of Honolulu could collect the desired $430 million via the GET instead of the property tax, it would require an increase in the GET rate on Oahu of 1.06 points (430 million divided by 406 million). Based upon the current GET rate of 4.5%, the new rate would amount to (4.5+1.06) 5.56%.

Imagine completely doing away with the property tax on homes and apartments by using a GET rate on Oahu of 5.56%. No more arguments over property assessments, no more tax increases because of rich people buying second homes, no more passing the tax on to the renters, no more seniors facing losing their homes, etc., etc. This is not smoke and mirrors - it is a real opportunity. It can work because the GET is a much broader-based tax; for example, visitors pay over 38% of it3[3].

What would this mean for us in terms of dollars? The following example provides some idea of how much we would be saving in taxes. If members of a household spend

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1[1] Hawaii Department of Taxation, Annual report 2005-2006.

2[2] Statewide, 3.34% of GET collections are from rental housing according to Dr. William Fox in IBID APPENDIX C. This was applied to Oahu collections with the assumption that the 3.34% is accurate for Oahu.

3[3] Tax Research and Planning Office, Hawaii State Department of Taxation, "Study on the Progressive or Regressive Nature of Hawaii's Taxes," report prepared for the 2005-2007 Tax Review Commission, November 2006, p.1.

$40,000 a year on things subject to the GET, they would pay an additional $424 **instead** of the property tax. Many now pay over $3,000 a year, essentially a tax cut of $2,576 for this example.

**GOOD FOR BUSINESS AND GOVERNMENT**

Businesses and the economy would also benefit because residents would have more money to spend in local stores every year. Also, the City will still get its $430 million. A total win, win, win. Substituting the GET for the property tax on homes and apartments would be a benefit for everyone on Oahu whether they own or rent.

An additional benefit is that population and economic growth increase GET revenue. GET revenue has increased on average nearly 8% per year since year 2000 without a rate increase4[4]. This is one of the reasons why the State has a huge surplus, while the City is struggling. The City could look forward to an average annual increase of 8% with no rate increase.

HB2394 provides a serious, workable proposal for genuine tax reform that deserves serious consideration. It is time to start considering this alternative before people are forced to give up their homes or food or medications to pay the property tax. Please move this bill forward.

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*Charles Prentiss is a retired former Executive Secretary of the Honolulu Planning Commission. He has a Masters Degree in Public Administration from the Fels Institute of Government, Wharton School of Finance, University of Pennsylvania.*

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4[4] Calculated from State of Hawaii Data Book 2005, Table 9.17.

**From:** Dave Rolf [mailto:drolf@hawaiidealer.com]
**Sent:** Wednesday, January 30, 2008 6:05 PM
**To:** HSHtestimony
**Subject:** HADA testimony with grave concerns on HB2394

January 30, 2008

Testimony with GRAVE CONCERNS about HB2394
Relating to Taxation
For the House Committee on Human Services & Housing
At the public hearing 9:45 a.m. Thursday, January 31, 2008
In House Conference Room 329, Hawaii State Capitol

Submitted by David H. Rolf, for the Hawaii Automobile Dealers Association
Hawaii's franchised new car dealers

Chair Shimabukuro and members of the committee:

The 1% surcharge tax proposed in HB2394 appears to apply to gross proceeds from income on a sale and such a tax thus would, in effect, create an amount on a new vehicle sale equal to that of a 13th car payment in a year.

With the fragile state of Hawaii's economy, the elasticity of demand application of requiring from consumers an amount equal roughly to a 13th car payment, would drive new car sales down further.

Further, there is no accompanying support schedule showing the effect of eliminating property taxes on rental properties and adding a surcharge on gross receipts.

HADA asks that this measure be deferred until a full explanation of its implications are presented.

Respectfully submitted,

David H. Rolf

**The Chamber of Commerce of Hawaii**
*The Voice of Business in Hawaii*

## Testimony to the House Committee on Human Services & Housing
## Thursday, January 31, 2008 at 9:45 a.m.
## Conference Room 329, State Capitol

## RE: HOUSE BILL NO. 2394 RELATING TO TAXATION

Chair Shimabukuro, Vice Chair Rhoads, and Members of the Committee:

The Chamber of Commerce of Hawaii opposes HB 2394.

The Chamber is the largest business organization in Hawaii, representing 1100 businesses. Approximately 80% of our members are small businesses with less than 20 employees. 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.

H.B. No. 2394 proposes to provide an additional county surcharge on the State General Excise tax of up to 1% for the City and County of Honolulu. The purpose of the tax increase is to replace the real property tax collected by the County on rental projects. The Bill also proposes to reduce rental rates to offset reduction in the real property taxes paid by landlords.

In the City and County of Honolulu, the real property tax rate for residential and apartments is $3.29 per $1,000.00 in assessed value. It is unclear from the information contained in the bill how the proposed 1% GET increase, which we understand based on numbers from the .5% GET for transit, could approach $300 million, will be used to reimburse the City and County of Honolulu for the loss in real property taxes from rentals who will be required to reduce rents by the amount necessary to offset any reduction in the amount of real property taxes assessed on such rental properties.

Currently, the total projected real property tax revenues for the City and County of Honolulu for FY 2007-2008 are $790 million. Of that, approximately $332 million comes from improved residential properties and $126 million from apartments. The bill should provide more detailed information on the financial impact to the tax payers who effectively will be subsidizing rentals in Honolulu.

We believe an overall housing policy should be looked at that first identifies what the problems are in each segment of the housing market and secondly provides solutions that will increase the overall supply of housing in the various segments of the market. This approach will allow the public to see how proposed solutions, such as this 1% GET increase, will result in increasing the supply of housing in the market. Without some quantitative measurement, it is difficult to support such a large tax increase.

For the above reasons, The Chamber opposes HB 2394 at this time. Thank you for the opportunity to submit written comments.