Rec'd after the Hearing.

KAUA'I Chamber of Commerce

January 31, 2011

Testimony to House of Representatives - Committee on Tourism
January 31, 2011, 9:15 a.m., Hearing: 9:15 a.m., Capitol Conference Room 312
Hawaii State Capitol

Honorable Representatives Chair Tom Brower, Vice-Chair James Kunanae Tokioka and members:

Dear Representatives:
RE: House Bill 371
My name is Randall Francisco and I am President/CEO of the Kauai Chamber of Commerce which comprises of approximately 450 members, 650+ representatives and 6000+ employees from across 119 industry sectors. 89% of the members are small businesses. The Chamber appreciates the efforts being made by members of the Legislature in addressing the budget shortfall during this tough economy.

On behalf of the Chamber, I am writing to express support of HB371.
The Chamber continues to support legislation such as HB371 which helps to provide the necessary leverage for economic growth and to stimulate the construction industry as a key economic driver of our economy. In continuing our partnership with the Chambers of Commerce of Hawaii and Business Alliance and trade and industry partners, initiatives such as those outlined in Section 2 related to Hotel and resort property construction and renovation tax credit provided a much-needed boost that will contribute to businesses reinvesting in the state's leading industry. This legislation will provide the short-term investment for long-term benefits and help to also keep our tourism infrastructure competitive with the rest of the global tourism economy. We all know the multiplier effects. More importantly, the socio- as well as economic benefits will provide the trickle-down effect to families who continue to live paycheck- to-paycheck. Your support and boldness in approval of this bill will contribute to the economic recovery that the people of Hawaii need to return to a place of economic well-being, peace of mind and contributors to our tax base.. Furthermore, the legislation demonstrates that Hawaii is a pro-business climate.

Thank you for the opportunity to submit testimony. If you have any questions, please contact me at Kauai Chamber of Commerce, 245-7363. Mahalo Nui Loa and Aloha.

Randall Francisco

Randall Francisco
Kauai Chamber of Commerce

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L E G I S L A T I V E

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LATE

SUBJECT: INCOME, Hotel construction and remodeling tax credit

BILL NUMBER: ~~SB 769~~; HB 371 (Identical); HB 1653 (Similar)

INTRODUCED BY: SB by Fukunaga, Baker, Chun Oakland, Ige, 1 Democrat and 1 Republican; HB 371 by McKelvey; HB 1653 by Manahan, Brower, Ito, Tokioka, Yamane and 1 Democrat

BRIEF SUMMARY: Adds a new section to HRS chapter 235 to allow taxpayers subject to HRS chapter 235 and HRS chapter 237D to claim a refundable hotel construction and remodeling tax credit of the construction or renovation costs incurred before 12/31/16. The credit shall be 7% of the construction and renovations costs between $1 million and $10 million in the aggregate; or 10% of the construction or renovation costs over $10 million to a maximum of $100 million in the aggregate. The credit shall not be applicable to costs of construction or improvements for which another income tax credit was claimed for the taxable year. Establishes a total annual cap of tax credits of $50 million.

SB 769/HB371 provides that the tax credit shall be available for tax years beginning after December 31, 2010 and shall not be available for tax years beginning after December 31, 2016. HB 1653 provides that the tax credit shall be available for tax years beginning after December 31, 2010 and shall not be available for tax years beginning after December 31, 2015.

In the case of a partnership, S corporation, estate or trust, association of apartment owners of a qualified hotel facility, time share owners' association, or any developer of a time share project, the credit shall be based on qualified costs incurred by the entity with costs on which the credit is computed determined at the entity level. To qualify for the credit, the taxpayer shall be in compliance with all applicable federal, state, and county statutes, rules, and regulations. If a deduction is taken under IRC section 179 (with respect to election to expense depreciable business assets), no tax credit shall be allowed for such qualified costs for which the deduction was taken. The basis of eligible property for depreciation or accelerated cost recovery system purposes shall be reduced by the amount of credit allowable and claimed.

Credits in excess of a taxpayer's income tax liability shall be applied to subsequent tax liability. Claims for the credit, including any amended claims, must be filed on or before the end of the twelfth month following the close of the taxable year.

Defines "construction or renovation cost," "net income tax liability," "qualified hotel facility," "qualified resort area," and "taxpayer" for purposes of the measure.

EFFECTIVE DATE: July 1, 2011; applicable to tax years beginning after December 31, 2010

STAFF COMMENTS: The legislature by Act 195, SLH 2000, enacted a hotel construction and renovation tax credit of 4% for hotel renovations effective for tax years beginning after 12/31/98 but before

12/31/02. Act 10 of the Third Special Session of 2001 increased the hotel renovation tax credit to 10% for construction costs incurred before 7/1/03. Act 10 also provided that the credit shall revert back to 4% on 7/1/03 and sunset on 12/31/05. These measures propose a similar credit for hotel renovation costs incurred in a taxable year.

The original tax credit was promoted on the argument that the tax credit would be an incentive for hotels to refurbish their properties in order to remain competitive with other destinations around the world. The credit amount was set at 4% to seemingly offset the 4% general excise tax. When 9/11 hit, the momentum of the crisis fostered support for an increase in the credit to 10% to supposedly keep projects which were already in progress going. However, the governor objected and threatened to veto the sweetened credit. The legislature compromised and provided that the 10% credit would be nonrefundable.

While these measures propose to reestablish a hotel renovation tax credit, it should be noted that no evaluation has been done to validate the effectiveness of this credit in spurring substantial renovations of hotel resort properties. While some may argue that this credit is necessary to make their upcoming renovations pencil out, one must ask whether or not it is the role of government to subsidize private investments. While the credit might be viewed as critical to a taxpayer's project or to the continued renovation of the resort plant, one must ask how long must all other taxpayers suffer the heavy burden of taxation so that this subsidy can be extended to a few?

It would be a very different picture if those who are asking for the subsidy would be willing to forgo other public services or make recommendations on how government can rein in spending, but that is not the case. Now, more than ever, lawmakers need to recognize that they need to set priorities for what precious few dollars taxpayers can part with to run state and local government. One must ask how lawmakers can provide subsidies like these proposals while they raised the general excise tax on all other taxpayers to pay for a transit system in Honolulu? Taking care of a few taxpayers at the expense of all other taxpayers is certainly a cavalier attitude.

More importantly, if the intent of these measures is to entice hotel owners to undertake major renovations, then the sponsors do not understand what is happening to the nation's economy. In order to undertake large scale construction or renovations, either the hotel owner has to be cash rich or else have access to the credit markets. As the nation now knows, the credit markets froze beginning in late 2007 and hit a crisis at the end of 2008. The phenomenon was a major reason for the demise of Aloha Airlines and ATA which were highly dependent on credit lines to meet on-going expenditures. When the credit markets froze, there was no way to secure cash advances to meet current liabilities and the two airlines, along with thousands of other businesses, had to shut their doors.

Despite herculean efforts to thaw those credit markets and to cajole corporations that are still sitting on over a trillion dollars worth of cash to loosen up and spend that money, have all been for naught as there are still jitters about how firm a recovery is being had. Given that fact, it is doubtful that any hotel owner will undertake new renovation projects, in fact, some who had such projects underway have pulled back or completely shut down those projects for the time being. Thus, the sponsors of these proposals may find this incentive useless in this environment.

Instead of subsidizing construction in order to get construction workers off the bench, government can assist in a number of other ways. For private projects, the permitting and planning process can be accelerated. One developer recently reported that it had taken two years to subdivide two parcels into seven house lots in rural Oahu at which time the planning and permitting department deferred approval citing eight issues to be addressed regarding subdivision approval. The interest on the seller has amounted to more than $500,000 to this point and going forward, both the buyer and seller are shelling out more than $27,000 a month for interest alone, not to mention the other planning and engineering costs. These are costs that could be mitigated if permitting officials would just work with developers and owners in streamlining these requirements. Apparently officials are reticent to make decisions in fear that they might make the wrong decision. The result is costly delays while construction work goes begging.

In the public arena, both the state and counties need to take advantage of this window of opportunity of readily available labor and exceptionally low interest rates to undertake a massive capital improvement program. As economists on the Council on Revenues noted recently, when adjusted for inflation, the amount of public construction projects in the state is at its lowest level since statehood.

Thus, rather than tinkering with the economy, lawmakers should rein back the role of government, or in other words, get out of the way and let the market lead the way to recovery. If nothing else, these measures demonstrate that lawmakers do not understand what makes the economy run and how businesses make their decisions. It is certainly sad that groups of people who have little, if any, business experience are attempting to tell business how it should be run.

Digested 1/31/11