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To: The Honorable Sylvia Luke, Chair
and Members of the House Committee on Finance

Date: Tuesday, February 25, 2014
Time: 11:15 A.M.
Place: Conference Room 308, State Capitol

From: Frederick D. Pablo, Director
Department of Taxation

Re: H.B. 2170, H.D. 1 Relating to Taxation

The Department of Taxation (Department) appreciates the intent of H.B. 2170, H.D. 1 to support our State's tourism industry.

H.B. 2170, H.D. 1 creates a nonrefundable income tax credit equal to an unspecified percentage of construction or renovation costs incurred for new hotel facilities, provided the construction or renovation costs are incurred during taxable years beginning after December 31, 2014 but not during taxable years beginning after December 31, 2019, and further provided that the costs are pre-certified by the Department of Business, Economic Development and Tourism (DBEDT).

The House Committee on Tourism made all of the Department's suggested amendments to the previous version of this bill. The Department appreciates consideration of its suggested amendments and defers to DBEDT regarding the pre-certification requirements of subsection (g).

Thank you for the opportunity to provide comments.

L E G I S L A T I V E

TAXBILLSERVICE

126 Queen Street, Suite 304 TAX FOUNDATION OF HAWAII Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: INCOME, Hotel construction tax credit

BILL NUMBER: HB 2170, HD-1

INTRODUCED BY: House Committee on Tourism

BRIEF SUMMARY: Adds a new section to HRS chapter 235 to allow taxpayers subject to HRS chapter 235 to claim a hotel construction tax credit for the construction costs incurred after 12/31/14 and before 1/1/20. The credit shall be ___% of the construction costs incurred during the taxable year and shall not be applicable to costs of construction for which another income tax credit was claimed for the taxable year. Defines "construction costs" as those incurred for plans, design, construction, and equipment related to construction of a new hotel facility located in the state.

In the case of a partnership, S corporation, estate or trust, 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. 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.

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

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

EFFECTIVE DATE: Tax years beginning after December 31, 2014

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 revert back to 4% on 7/1/03 and sunset on 12/31/05. This measure proposes a similar credit of 10% for new hotel construction costs incurred in a taxable year.

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

This measure proposes to establish a hotel construction tax credit. No evaluation has been done to validate the effectiveness of these types of credits in spurring new hotel construction or substantial renovations of hotel resort properties. Some may argue that this credit is necessary for the hotel industry, but is it the role of government to subsidize private investments? While the credit might be viewed as critical to a taxpayer's project, how long must all other taxpayers suffer the heavy burden of taxation so that this subsidy can be extended to a few? Now, more than ever, lawmakers need to recognize that they need to set priorities for what precious few dollars taxpayers can part with to run state and local government.

More importantly, if the intent of this measure is to entice new hotel construction, then the sponsors do not understand what is happening to the nation's economy. In order to undertake large scale construction, either the developer or 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.

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

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.

This measure is similar to others proposing a hotel construction tax credit. However, it is a nonrefundable credit but does not contain language allowing unused credits to be carried forward. Thus, if the measure is passed as is, any credit earned by a taxpayer that is unable to use it is permanently lost.

Digested 2/24/13

OUTRIGGER ENTERPRISES GROUP

Hospitality • Retail • Development

HOUSE OF REPRESENTATIVES
THE TWENTY-SEVENTH LEGISLATURE
REGULAR SESSION OF 2014

COMMITTEE ON FINANCE
Representative Sylvia Luke, Chair

2/25/2014
Rm. 308, 11:15 AM

HB 2170, HD 1
Relating to Taxation

Chair Luke and Members of this Committee, my name is Max Sword, here on behalf of Outrigger Hotels Hawaii, in support of the intent of HB 2170, HD 1.

The promotion of construction activity alone is very important to any economy—it is a significant component of overall economic activity especially in a small island state such as Hawaii. Investment in physical assets in the visitor industry, however, reaps even more benefits than straight construction alone—it provides the means by which future economic activity will take place. The visitor industry cannot be competitive without an attractive, up-to-date physical plan in the form of hotels and recreational facilities.

Construction of hotels brings more revenues back into the economy, and taxes, because the hotel/tourist industry continues to bring in revenues beyond construction. Such projects result in higher hotel occupancies, visitor-days, and room rates. It is estimated that 30% of room rates goes back to employee salaries. Both the GET and TAT is paid by the industry thru the 11+ percent assessed each hotel.

However, even with the number of jobs, taxes etc. that a hotel project will provide, the bottom line is that it is very hard to get financing to either rebuild or to build a new hotel facility in the financial marketplace today. Tax credit such as these being proposed, will help a hotel project to either a rebuild or to build a new hotel.

Mahalo for allowing me to testify.

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The House of Representatives
The Twenty-Seventh Legislature
February 25, 2014, 11:45 a.m.
Room 308

LATE

Statement of the Hawaii Regional Council of Carpenters on
H.B 1594, HD1 **and** H.B. 2170, HD1, Relating to Taxation

The Hawaii Regional Council of Carpenters supports the intent of both Bills, while urging the following amendment to clarify what we believe to be intended in H.B. 1594:

"(f) To qualify for the income tax credit, the taxpayer shall be in compliance with all applicable federal state, and county statues, rules and regulations, including the Davis-Bacon Act and chapter l04. **Construction or renovation pursuant to this Section shall be subject to chapter 104, and the department or agency pre-certifying the tax credit shall be the contracting agency for the purposes of chapter 104.**"

Should H.B. 1594 be passed by the Committee, the above would amend an existing "(f)" in the HD1. Should H.B. 2170 be passed by the Committee, the Bill would be amended by adding the full paragraph. It is necessary to make clear that being "…in compliance with…" chapter 104 applies to the construction at hand, rather than the absence of past non-compliance.

Practices in administering chapter 104 for construction benefitting from Special Purpose Revenue Bonds may also be instructive in administering this tax credit State for transient accommodations.

Tax credits are State resources (funds due) through which construction projects are undertaken, and serve a State purpose. Pre-certification of the tax credit provides an agreement with the State prior to the start of construction, rather than falsely considering the State assistance to occur after, and separate from, the construction.

Thank you for considering the suggested amendment.

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

LATE

DATE: February 25, 2014

TO: Representative Sylvia Luke
Chair, Committee on Finance
Submitted Via FINtestimony@capitol.hawaii.gov

RE: **H.B. 2170 H.D.1 – Relating to Taxation**
Hearing Date: February 25, 2014 at 11:15 a.m.
Conference Room: 308

Dear Chair Luke and Members of the Committee on Finance,

We submit this testimony on behalf of Wyndham Vacation Ownership.

Wyndham Vacation Ownership offers individual consumers and business-to-business customers a broad suite of hospitality products and services through its portfolio of world-renowned brands. Wyndham has a substantial presence in Hawaii through its Wyndham Vacation Resorts and WorldMark by Wyndham brands.

Wyndham **supports** H.B. 2170 H.D.1, which would provide tax credits for hotel construction.

Rejuvenating our resort inventory is critical if Hawaii is to remain competitive. For both hotel and timeshare construction, attracting investment dollars is challenging. Tax credits are a proven means of attracting investment dollars. Accordingly, Wyndham respectfully requests your support of H.B. 2170, H.D.1.

Thank you for the opportunity to submit testimony on this measure.

Gary M. Slovin
Mihoko E. Ito
Tiffany N. Yajima
Jennifer C. Taylor

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