CHAPTER 14

TOURIST TAXES

JAMES MAK
Professor of Economics
University of Hawaii

"Are we overtaxing tourists?"

That certainly was the opinion of a tourist whose complaints were printed by a Honolulu newspaper in 1992. She was especially upset about having to pay a $2 daily tax on her rental car. Interestingly, her letter did not mention that she was taxed *twice* on her use of that car; she also had to pay a 4 percent (actually 4.16 percent) excise tax on her car rental. What probably irked her was that she didn't pay the $2 daily tax the previous time she came to Hawaii. This particular tax took effect in 1992.

She was taxed twice on her hotel room as well. Her hotel bill showed a 4.16 percent excise tax and a 5 percent (actually 5.25 percent) transient accommodation tax, for a combined rate of nearly 9.5 percent on the price of the room. The hotel room tax went into effect in 1987 and now generates about $80 million a year in tax revenues.

The unhappy tourist also paid 4.16 percent on just about everything else she bought while in Hawaii—services as well as goods—just like residents. But taxes on items such as car and hotel rentals are intentionally discriminatory. They were enacted with the understanding that the lion's share of those taxes would be paid by tourists. (Don't ask for the exact percentage, because no one knows for sure!)

In addition to the taxes levied directly on her purchases, our already-irate tourist paid a lot of taxes hidden in the price of everything she bought. For example, some of the property tax paid by the owner of her hotel no doubt showed up in the hotel room rate she paid. In Honolulu and Maui counties, the highest property tax rates are levied on hotels. In Honolulu, the 1991 tax rate on hotels was nearly triple the rate paid by homeowners and owners of apartments that are rented out to nontourists. Hotels do their best to pass along these higher taxes.

Similarly, when the restaurant she frequented bought food from a local wholesale grocer, it paid an excise tax; that tax was then passed along to her, not separately stated, but hidden in the price of the meal she ate.

When all taxes are taken into account, tourists directly and indirectly account for more than one out of every five dollars of state and county tax revenues, despite the fact that only one out of every eight people in Hawaii on any given day is a tourist.

Tourists don't vote. Hawaii is not the only state to levy taxes on tourists. Indeed, tourist taxes have become the rage in state and local public finance. The reason is simple. Since 1979, federal financial support for state and local governments has fallen dramatically. At the same time, federally mandated programs have imposed new financial responsibilities. Caught between falling resources and rising responsibilities, state and local governments have been looking desperately for new money to maintain public services. It can be difficult to cut services, and political suicide to raise taxes on residents. The politically "easy" answer is to hit the tourist. Tourists don't vote ... except with their feet. As long as not too many of them are chased away by exorbitant taxes, lots of new tax revenues can be generated without anyone getting voted out of office.

The darling of all tourist taxes is the hotel room tax, now levied virtually everywhere in the United States by local government, state government, or both. A survey of large U.S. cities during the mid-1980s found that the median hotel room tax rate was about 7 percent; by 1990 the median was 10 percent, an increase of some 40 percent. Thus, Hawaii's combined hotel room tax of nearly 9.5 percent is about average.

Are we gouging tourists when we levy taxes that fall primarily on them? Not necessarily. Since tourists don't pay our state income tax, we have to figure other ways for them to help pay for the cost of government generally, not to mention police, highways, beaches and parks.

Two studies done in the 1970s concluded that tourists in Hawaii paid more in taxes than they got back in the form of public services. Based on those studies, some tourism industry officials argue that tourists are paying more than their fair share of taxes. That's certainly one criterion for fairness, but it's not the only one. For example, few would rate the fairness of our state and federal tax systems by comparing what each one of us pays in taxes against what we receive in services. Indeed, I would be surprised to find many people who know exactly how much they are paying in federal or state and local taxes, or how to begin to calculate the value of what they are getting in return. Besides, it would be impossible to measure what tourists do get as a result of the taxes they pay.

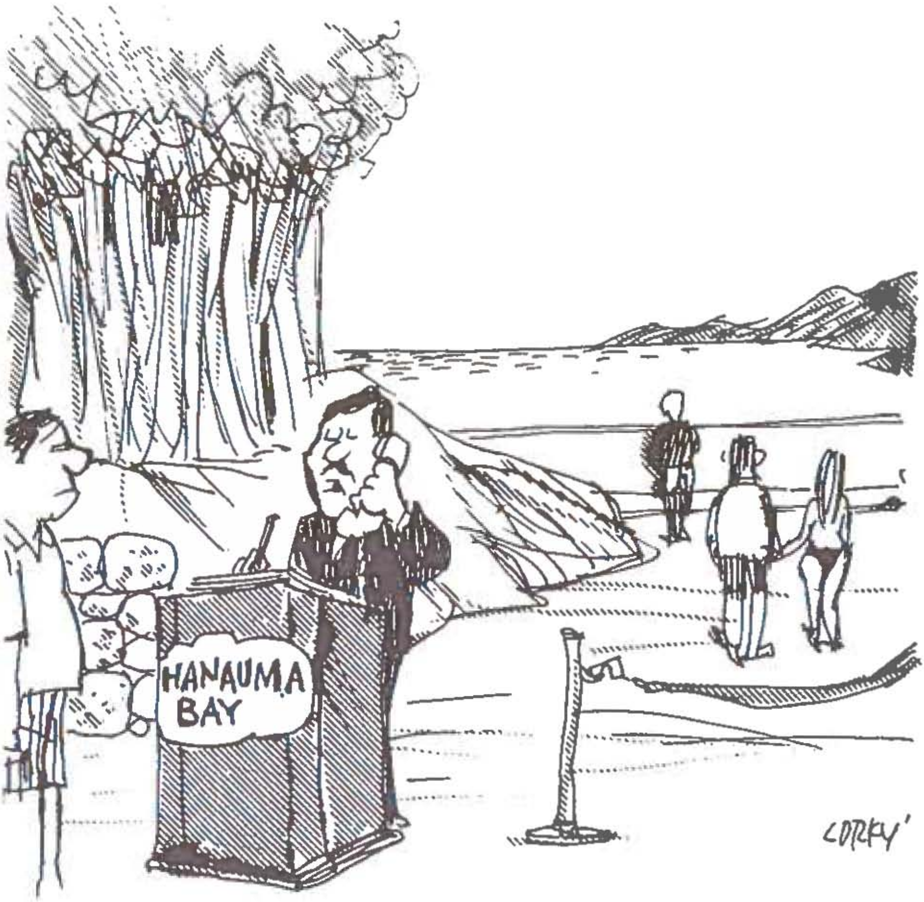
"Tax to da max." The economic rationale for taxing tourists does not rest on equating taxes paid with services received; that much is clear. But on what basis are they taxed?

The goal should be to maximize the state's economic benefits from tourism. It may sound terrible to the tourist, but this boils down to taxing them as much as they will bear.

Tourism consumes substantial resources of this state and contributes to the deterioration of the environment and the quality of residents' lives. Many benefit directly from tourism, but most do not. Tourist taxes are a form of compensation to all the residents of Hawaii, including those who do not otherwise benefit from their presence. Hawaii is not alone in taking this tack.

In Nevada, tourism directly accounts for more than half of all state tax revenues. Political leaders in that state make no bones about their goal of getting as much revenue from tourists as possible.

It is common practice among nontourist-oriented states to design their tax systems to maximize economic benefits to their own residents. Often, they do it by levying special taxes on goods that they sell in particularly large quantities to non-resident buyers. To the extent that these taxes are passed on to out-of-state consumers and producers, there is a transfer of income to residents who are the better off for it. Alaska gets most of its tax revenues from the oil industry. Wyoming gets large amounts from mining. The Pacific Northwest states generate sizable



"RESERVATIONS...FOR FOUR?... I HAVE NOTHING 'TILL NEXT TUESDAY..."

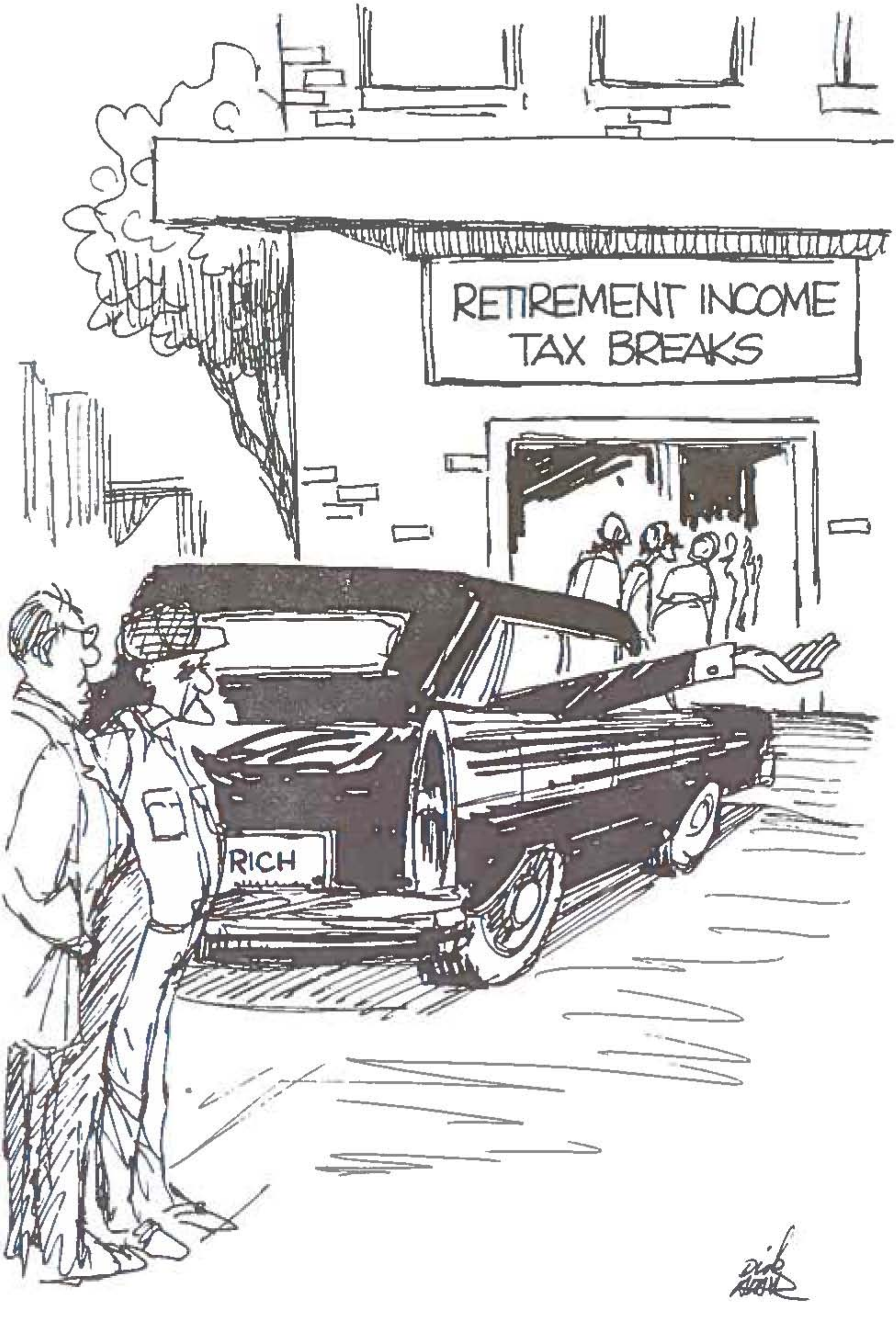
tax revenues from the timber industry. If you think of tourism as the primary export of states like Hawaii and Nevada, it is easy to see that tourist taxes have much in common with these other taxes.

There's a limit. Of course, it's possible to go too far. Just as car manufacturing companies could move from Michigan if that state were to impose a burdensome tax on them alone, tourists can choose to stay away if taxation makes vacations in Hawaii too expensive. If this happens, taxation actually reduces the net societal benefits from tourism.

Taking each of Hawaii's tourist taxes separately, it is possible to make a strong case for each one. However, we should ask: when we take all the taxes levied on tourists together, are we gouging them to the point that many will, for that reason, stay home? I say no. Taxes levied on our hotel rooms are not particularly high compared to those levied in competing destinations. Hawaii's hotel room rates, inclusive of taxes, have always been competitive. Car rental rates continue to be low in comparison to numerous other vacation destinations in the Pacific or on the Mainland.

Goods and services are more expensive in Hawaii than elsewhere, but this cannot be attributed primarily to excessive taxes on tourists. It's difficult to argue that we are overtaxing tourists when more come to Hawaii each year than to any other travel destination in the Pacific. Until Operation Desert Storm and the 1991-1992 national recession temporarily slowed the flow, the number of tourists coming to Hawaii kept rising each year, despite the imposition of new taxes.

As for the future, a greater threat to the health of the tourist industry in Hawaii is *too many* tourists. Chasing them away with high taxes may be the least of our problems. The bottom line is that Hawaii still offers good value, despite its new tourist taxes. To our tourist friends I say, "Lucky you vacation Hawaii!"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