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**STATE OF HAWAII
DEPARTMENT OF TAXATION**

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

Date: Wednesday, March 13, 2019
Time: 10:00 A.M.
Place: Conference Room 309, State Capitol

From: Linda Chu Takayama, Director
Department of Taxation

Re: S.B. 965, S.D. 1, Relating to Taxation

The Department of Taxation (Department) provides the following comments regarding S.B. 965, S.D. 1, for your consideration.

S.B. 965, S.D. 1, extends the Tax Credit for Research Activities, which was due to sunset after 2019, to an unspecified date, and increases this refundable credit from 100% of the allowed federal credit to an unspecified percentage of the allowed federal credit for work done in Hawaii. The measure also eliminates the due date of a required survey provided to the Department of Business, Economic Development and Tourism and sets a recapture of the credit if the taxpayer fails to remain in Hawaii for 5 years. The measure has a defective effective date of July 1, 2050, but would otherwise apply to taxable years beginning after December 31, 2018.

The Department notes that the calculation of the base of the credit conforms to the Internal Revenue Code. This method allows the Department to rely on determinations or adjustments made to the federal credit by the Internal Revenue Service and greatly minimizes the burden on the Department and taxpayers, thereby assisting compliance with Hawaii's tax law.

Thank you for the opportunity to provide comments.



Written Statement of
Len Higashi
Acting Executive Director
Hawaii Technology Development Corporation
before the
House Committee on Economic Development and Business
Wednesday, March 13, 2019
10:00 a.m.
State Capitol, Conference Room 309

In consideration of
SB965, SD1
RELATING TO TAXATION.

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

The Hawaii Technology Development Corporation (HTDC) submits **comments** on SB965, SD1 that increases the state tax credit for research activities to an unspecified portion of the allowable federal tax credit and requires businesses to remain in Hawaii for 5 years after receiving the tax credit and amends qualifying tax years.

HTDC does not take a position on the bill but offers the following comments. In discussions with representatives from DOTAX and DBEDT – READ, it was pointed out that the current statute requires the company to complete the DBEDT survey but does not have a mechanism to ensure the survey is completed. Also, the DBEDT survey deadline is currently set at June 30 while companies that file extensions submit their returns on October 20. Thus, not all companies are completing the survey. We support the amendment that removed the deadline for filing the DBEDT survey so companies can file the survey year-round. We suggest that the survey requirement gap be addressed if the credits are continued.

Thank you for the opportunity to offer these comments.



Statement of
Hermann Kugeler
Business Development Manager
Makai Ocean Engineering, Inc.
before the
House Committee on Economic Development & Business
Wednesday, March 13, 2019
10:00am
State Capitol, Conference Room 309
In consideration of
SB965
RELATING TO TAXATION.

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

Makai Ocean Engineering, Inc. **STRONGLY SUPPORTS SB965**. The original bill was passed in 2013 as Act 270 to support research and development in Hawaii. The main purpose of this bill is to extend the sunset of Act 270.

Makai is a locally-owned and operated technology company based in Hawai'i for over 45 years. We are currently performing R&D on a variety of exciting ocean technology projects, including autonomous underwater vehicles, ocean thermal energy conversion (OTEC) and seawater air conditioning (SWAC) systems, submarine and subsea cable systems, and a Department of Energy project to grow and harvest macroalgae offshore in Hawaiian waters to produce a renewable biofuel alternative for transportation.

Makai has been successful in bringing in tens of millions of dollars in R&D funds from federal and international sponsors to Hawai'i, helping to stem the tide of "brain drain" of talented kama'aina kids going to the mainland. Makai is not unique among Hawaii technology companies in this. There is a tech community here that has made a strong economic impact in terms of high paying jobs, and demonstrated success in commercializing federal R&D, which has increased taxable revenue for the state, and brought home kama'aina scientists and engineers.

This bill would enhance the ability of Hawaii companies like Makai to outshine mainland peers in competitive federal R&D projects, bring home R&D dollars that greatly exceed the initial investment, and create a critical mass and a truly vibrant industry of innovative R&D companies in Hawaii. It would expand and diversify Hawaii's economy, and enable our tech industry to support high-paying, highly-skilled professional jobs for our keiki here at home.

This is why we **STRONGLY SUPPORT SB965**, which supports Hawaii's R&D companies enabling them to continue spending monies on wages, materials and subcontractors **IN THE STATE OF HAWAII** and recognizes the importance of Hawaii's innovation industries to our economy.

SB-965-SD-1

Submitted on: 3/10/2019 10:26:54 PM

Testimony for EDB on 3/13/2019 10:00:00 AM

Submitted By	Organization	Testifier Position	Present at Hearing
Ann Chung	Individual	Support	Yes

Comments:

I strongly SUPPORT SB965. The original bill was passed in 2013 as Act 270 to support companies doing research and development in Hawaii. The Act sunsets at the end of 2019. Supporting this bill helps Hawaii's R&D companies enabling them to continue spending monies on wages, materials and subcontractors IN THE STATE OF HAWAII and recognizes the importance of Hawaii's innovation industries to our economy. I strongly urge you to pass this bill and extend the sunset date.

Mahalo for the opportunity to testify.

SB-965-SD-1

Submitted on: 3/12/2019 9:58:39 AM

Testimony for EDB on 3/13/2019 10:00:00 AM

Submitted By	Organization	Testifier Position	Present at Hearing
Melodie Aduja	O`ahu County Committee on Legislative Priorities of the Democratic Party of Hawai`i	Support	No

Comments:

TAX FOUNDATION OF HAWAII

126 Queen Street, Suite 304

Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: INCOME, Increase Tax Credit for Research Activities

BILL NUMBER: SB 965, SD-1

INTRODUCED BY: Senate Committee on Ways & Means

SYNOPSIS: Amends HRS section 235-110.91 to provide that for tax years beginning after December 31, 2018, the tax credit for research activities is increased to _____ times any credit calculated under section 41 of the Internal Revenue Code as it existed on December 31, 2011.

If at the close of any taxable year within a five-year period beginning with the first year that a qualified high technology business claims this tax credit, the business no longer qualifies as a qualified high technology business, the credit claimed under this section shall be recaptured. The recapture shall be equal to the amount of the total tax credit claimed under this section in the preceding five taxable years.

Removes the requirement that the annual survey be filed with DBEDT before June 30 of each calendar year.

Amends the sunset date of the credit from Dec. 31, 2019 to Dec. 31, _____.

EFFECTIVE DATE: July 1, 2050.

STAFF COMMENTS: Act 270, SLH 2013, reestablished the income tax credit for qualified research activities that expired on Dec. 31, 2010. The prior version of that law, under Act 221, SLH 2001, offered a credit for qualified research activities that was a flat percentage of qualified research expenses in Hawaii without regard to the federal base amount (the federal credit is supposed to be an incentive to increase research activities, so the federal credit is based on incremental research expenses). When Act 270 brought the credit back, it did so as an incremental credit, like the federal credit.

Under current law, the state credit is 100% of the federal credit, but the qualified research expenses on which the credit is based are not to include research expenses incurred outside of Hawaii. In addition, the credit must be claimed by a qualified high technology business as defined in HRS section 235-7.3(c).

Substantively, over the last decade, Hawaii has adopted various tax incentives to encourage the development of high technology businesses in the state. The acts provided investment and research credits as well as income exclusions providing tax relief to high tech businesses and individuals associated with high tech businesses. But it fails to recognize that investments are made with the prospect that the venture will yield a profit. If the prospects for making a profit are absent, no amount of tax credits will attract investment from outside Hawaii's capital short environment. People do not invest to lose money. It should be remembered that until Hawaii's high cost of living can be addressed, all the tax incentives in the world will not make a difference

in attracting new investment to Hawaii. The only attractive aspect for resident investors to plow money into such activities is the fact that the credit provides a way to avoid paying state taxes.

At a minimum, lawmakers should carefully examine the results that have come out of this 20-year-old incentive to see if the State has gotten its money's worth. If it hasn't, how can an extension or increase in the credit be justified?

As a technical matter, the recapture provision seems extreme. A business could fail to qualify as a QHTB by going out of business, and if that happens the recapture tax might not be collectible.

Digested 3/12/2019



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, MARCH 13, 2019 AT 10:00 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 SUPPORT OF SB 965 RELATING TO TAXATION

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 support of SB 965.

The Maui Chamber of Commerce supports tax credits to spur industry growth and supports economic diversity and industry development, so we support this bill to increase the state tax credit for research activities.

We appreciate the language included in this bill to recapture credits claimed by high technology businesses who leave the State within five years.

Mahalo for your consideration of our testimony and we hope you will move this bill forward.

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.



Chamber of Commerce HAWAII

The Voice of Business

**Testimony to the House Committee on Economic Development and Business
Wednesday March 13, 2019 at 10:00 A.M.
Conference Room 309, State Capitol**

LATE

RE: SB 965 SD1, RELATING TO TAXATION

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

The Chamber of Commerce Hawaii ("The Chamber") **supports** SB 965 SD1, which increases the refundable credit under the Tax Credit for Research Activities from 100 percent of the allowed federal credit to 125 percent of the allowed federal credit for work done in Hawaii. Additionally, this bill would also extend the tax credit for research activities to an unspecified date.

The Chamber is Hawaii's leading statewide business advocacy organization, representing 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.

The Chamber continues to support the State's efforts to promote and foster innovation research and development in Hawaii. Innovation is a proven catalyst for economic growth and the creation of high-skilled and high-paying jobs. This bill would help to provide necessary capital to help assist these small businesses in innovation research and expansion and provide support to grow their businesses to the next level and compete globally.

Thank you for the opportunity to express our views and concerns.