NEIL ABERCROMBIE
GOVERNOR

BRIAN SCHATZ
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CATHY L. TAKASE
ACTING DIRECTOR

To:	House Committee on Finance
From:	Cathy L. Takase, Acting Director
Hearing:	Wednesday, March 2, 2011, 10 a.m. State Capitol, Room 308
Re:	Testimony on H.B. No. 1308, H.D. 1 Relating to Digital Media

The Office of Information Practices (OIP), which administers the State's public records law, the Uniform Information Practices Act (Modified), HRS chapter 92F (the UIPA), takes no position on the purpose of this bill, but offers the following comment on a proposed confidentiality provision.

A proposed new subsection (l) (page 14, lines 1 thru 11) provides that information submitted by a taxpayer applying for a tax credit shall not be subject to public disclosure when the information is "considered by the taxpayer and acknowledged by the department as confidential" under criteria set forth. The section then sets forth a standard for confidentiality that is nearly identical to the standard used to withhold confidential business and financial information under the frustration exception to disclosure under the UIPA.

The UIPA provides a uniform scheme to address public disclosure and protection of government records, including confidential commercial or financial information. The proposed confidentiality statute appears to afford slightly different treatment to information submitted for the proposed tax credit than is given to other similar commercial and financial information submitted to other government agencies, which may withhold information in accordance with standards adopted for this type of information under the UIPA.

For uniform treatment of similar records, OIP suggests that, if a confidentiality provision is desired, that it be worded to require the department to keep confidential commercial and financial information to the extent that this information falls within an exception to disclosure under chapter 92F.

Thank you for the opportunity to testify on this bill.

NEIL ABERCROMBIE
GOVERNOR

BRIAN SCHATZ
LT. GOVERNOR

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HOUSE COMMITTEE ON FINANCE

TESTIMONY OF THE DEPARTMENT OF TAXATION REGARDING HB 1308, HD 1 RELATING TO DIGITAL MEDIA

TESTIFIER:	**FREDERICK D. PABLO, DIRECTOR OF TAXATION (OR DESIGNEE)**
COMMITTEE:	**FIN**
DATE:	**MARCH 2, 2011**
TIME:	**10:00AM**
POSITION:	**DEFER TO DBEDT; OPPOSED TO ASSIGNABLE CREDITS**

This measure establishes digital media enterprise subzones surrounding the University of Hawaii campus, which includes certain tax benefits.

DEFERRAL TO DBEDT—The Department defers to the Department of Business, Economic Development & Tourism on whether the enterprise zone incentives should be expanded to include this program.

ASSIGNMENT OF CREDITS - The Department of Taxation (Department) **opposes the provision allowing assignment of credits**. The Department is strongly opposed to any provision that allows Hawaii tax credits to be sold, assigned, or transferred from one taxpayer to another. Allowing taxpayers to market or sell their tax credits is fundamentally poor tax policy. Selling tax credits can be subject to abuse and suspect motivation by parties involved.

The Department's fundamental and primary concerns regarding credit transfers are the following:

- The transferability rewards a separate taxpayer unrelated to the taxpayer that generated the credit, which is fundamentally poor tax policy for encouraging behavior and directly rewarding that behavior;
- The Department is not setup to regulate credit transfers. Will the Department be required to establish a "Bureau of Credit Conveyances" in order to track transfers? If this is the case, resources will have to be dedicated to this;
- Abuse relating tax credit transfer prices will be problematic. The State will be out a $1 when taxpayers will be transferring this $1 for pennies;

- And, there will be problems on audit. The taxpayer being audited may have sold the credit to another taxpayer. It is also unclear whether the tax credit is refundable or nonrefundable.

CONCERN OVER AGGREGATE CAP—The Department generally opposes aggregate caps, especially in this measure's form. There is no legislative guidance on how the cap is to be administered. Is the cap based on who files first? Do taxpayers need to apply for the credit? Should the credit be spread evenly amongst all taxpayers? All of these issues arise when an aggregate cap is instituted. These issues become even more concerning when there are a substantial number of taxpayer claiming the credit.

RECAPTURE – The Department is concerned that the recapture provided is only 25% of the tax credit claimed in the preceding two taxable years rather than 100% of the credit claimed. The Department is also concerned that the events triggering recapture appear to be patterned after the qualified high technology business investment credit, which may not be applicable here. In general the Department suggests that any infrastructure credit be patterned after the federal low-income housing credit, section 42 of the Internal Revenue Code, which is a proven method for providing tax credits to allow financing for construction of the desired buildings.

NEIL ABERCROMBIE
GOVERNOR

RICHARD C. LIM
INTERIM DIRECTOR

DEPARTMENT OF BUSINESS, ECONOMIC DEVELOPMENT & TOURISM

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STATEMENT OF

RICHARD C. LIM, INTERIM DIRECTOR
DEPARTMENT OF BUSINESS, ECONOMIC DEVELOPMENT, AND TOURISM

BEFORE THE

HOUSE COMMITTEE ON FINANCE

Wednesday, March 2, 2011
10:00 a.m.
State Capitol, Conference Room 308
In consideration of

HB1308 H.D. 1
RELATING TO DIGITAL MEDIA

Chair Oshiro, Vice Chair Lee, and Members of the Committee.

The Department of Business, Economic Development, and Tourism (DBEDT) supports the intent of HB1308 HD1 which would establish a digital media enterprise zone and a digital media infrastructure tax credit incentive, renames the existing Hawaii Television and Film Development Fund (HRS 201-112) to the Hawaii Film Office Special Fund, and provides for additional revenue streams for the fund to support operations and personnel. The department supports this concept, provided the special fund does not supplant the current budget requests for general funds for the Creative Industries Division and its Hawaii Film Office and Arts and Culture Development branches. We defer to Department of Taxation as to the fiscal impacts of the measure and any additional impacts to operations and staffing required, should this measure pass.

Hawaii's digital media sector has increased 10% since the department began tracking creative industries activity in 2002. Collectively, Hawaii creative sectors contribute $4 billion to

Hawaii's gross domestic product annually, building the foundation of Hawaii's creative economy.

By establishing a digital media enterprise zone, the department estimates that for each $1 million dollars spent by a digital media company, 5.31 direct jobs will be created at an average annual wage of $59,572 (Bureau of Labor Statistics 2009 data), with a total of $109,679 of direct, indirect and induced tax from spending.

HB1308 HD1 recommends renaming the existing Hawaii Television and Film Special Fund to the Hawaii Film Office Special Fund. It also renames the existing Hawaii Television and Film Development Board to a Hawaii Film Office board. Though the existing Hawaii Television and Film Development board is currently inactive, the department does not believe that changing the board name will affect the status/activity level of the board, nor the intent of the statute. However, the department respectfully requests amending the language in Sections 6 and 7 to provide the director of DBEDT the ability to designate the use of these funds rather than the board.

In addition, the department also requests the measure include appropriation language in order for the department to expend funds:

> *There is appropriated out of the Hawaii Film Office Special Fund the sum of $______ Or so much thereof as may be necessary for fiscal year ________ to be expended for the purposes of §210-113, Hawaii Revised Statutes.*

We believe through Hawaii's educational programs and its entrepreneurs in the digital and emerging industries sectors, the ideas proposed in this measure would help to grow and sustain this critical component of Hawaii's creative economy.

Thank you for the opportunity to provide these comments and recommendations.

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, MISCELLANEOUS, Digital media infrastructure tax credit

BILL NUMBER: HB 1308, HD-1

INTRODUCED BY: House Committee on Economic Revitalization & Business

BRIEF SUMMARY: Adds a new part to HRS chapter 209E to establish a digital media enterprise subzone as a geographic area located within an enterprise zone which is: (1) located within a_____ mile radius of a University of Hawaii campus, on or off campus; or (2) any other delineated geographic area designated as a digital media enterprise subzone by the legislature; provided that effective July 1, 2011 to June 30, 2013 the establishment of a subzone shall be limited to an area located within a_____mile radius, on or off campus, of the University of Hawaii-West Oahu.

Allows a taxpayer to claim a tax credit for investment expenditures made for all qualified digital media infrastructure projects within a digital media enterprise subzone in the amount of_____% of the taxpayer's base investment; provided that the tax credit shall be reduced by any credit claimed by the taxpayer under HRS chapter 235 for the same base investment. No more than $_____ in total tax credits under this section shall be authorized in any one taxable year.

Tax credits in excess of a taxpayer's tax liability shall not be refunded but may be carried forward to offset net income tax liability under HRS chapter 235 in subsequent tax years for a period not to exceed 10 tax years or until exhausted, whichever occurs first. Stipulates that the credit shall be claimed after all other tax credits available to the taxpayer have been claimed. Allows a taxpayer eligible to claim a tax credit under this section to assign all or a portion of a tax credit to any assignee. Allows an assignee to subsequently assign a tax credit or any portion of a tax credit to one or more assignees. A taxpayer may claim a portion of a tax credit and assign the remaining tax credit amount. A tax credit assignment under this subsection shall be irrevocable. The tax credit assignment under this subsection shall be made on a form prescribed by the department of taxation.

Further delineates procedures to qualify for the credit including the submission of a $100 application fee and a tax credit certification fee to cover the costs of administering the tax credit certification program by DBEDT. Also delineates conditions to qualify for the credit by the taxpayer. The credit shall be repealed on June 30, 2021.

Amends HRS chapter 431 by adding Section 431:7- to provide that the digital media infrastructure tax credit shall be applicable to this article on July 1, 2011. Repeals this section on June 30, 2021.

Renames the Hawaii television and film development special fund as the Hawaii film office special fund, delineate moneys that shall be deposited into the fund and that the monies in the fund shall be used for operations of the Hawaii film office, including personnel costs of staff positions existing on

November 1, 2010; provided that the use of the fund for personnel costs shall be limited to employees performing specialized duties and assigned solely to the Hawaii film office. This section shall be effective until June 30, 2021.

Amends HRS section 201-113 to delineate uses of the Hawaii film office special fund. This section shall take effect on July 1, 2021.

EFFECTIVE DATE: July 1, 2112

STAFF COMMENTS: The proposed measure establishes a digital media enterprise subzone within enterprise zones and surrounding areas of the University of Hawaii campuses. It also proposes a tax credit for investment expenditures made for all qualified digital media infrastructure projects within a digital media enterprise subzone in the amount of _____% of the taxpayer's base investment in addition to any other tax incentives afforded to businesses in an enterprise zone. While this measure proposes tax credits that would result in a payout of state funds, it is incredulous that a proposal such as this would be submitted given the financial crisis in state finances.

In addition, while the measure allows any excess tax credit for investment expenditures to be assigned to any assignee who subsequently may assign a tax credit to one or more assignees, this would create an administrative and record keeping nightmare for the department of taxation.

In an enterprise zone, businesses are attracted and encouraged to relocate to the zone through tax incentives, bonds, and other appropriate measures. Businesses located in an enterprise zone may claim a credit against taxes paid for a period of seven years and also allows the sale of items sold by such businesses to be exempt from the general excise tax.

While it appears that it is the intent of the legislature to encourage the development of digital media in the state, enterprise zones merely exacerbate what is already considered a poor climate in which to do business. Singling out businesses for preferential treatment merely confers preferences for those businesses at the expense of all other taxpayers.

Concurrent efforts must be made to improve Hawaii's business climate to enhance the economic prospects for all businesses. Enterprise zones are merely an abdication of government's responsibility to create a nurturing and supportive business climate so that all businesses can thrive in Hawaii and provide the jobs the people of Hawaii need.

Instead of expanding the enterprise zone program, the program should be repealed in favor of across-the-board tax relief for all businesses in Hawaii. For example, the consultant to the most recent Tax Review Commission suggested that all business-to-business transactions be exempt from the general excise tax as a means of reducing not only the cost of doing business in Hawaii but the overall cost of living.

Indeed, has there been a comprehensive evaluation of the program and do lawmakers know exactly how much enterprise zone businesses have benefitted and whether or not they have created the jobs promised when the program was first established? If, in fact, lawmakers believe that they need these special zones to attract businesses and to create jobs, what does that say about those areas of the state that are not so favored? Does, in fact, Hawaii's harsh business climate and poor reputation for a place to invest come as a result of providing such tax breaks at the expense of those businesses and individuals who cannot claim these tax incentives? Does the high burden of taxes have to be maintained because "tax relief" is extended to only a chosen few? This is the problem that lawmakers have created in recent years as they single out zones like these or select industries for most favored status. If that is the case, then lawmakers should hang out a sign that says don't come to Hawaii or don't invest in Hawaii unless you can secure a tax break from the legislature.

Inasmuch as this proposal seems to benefit the University of Hawaii as the subzones would be located within an unspecified mile radius of a University campus, consideration should be given to offsetting the revenues losses with a reduction in general fund appropriations to the University. At least that trade off would insure revenue neutrality for the state general fund.

This, along with proposals from film producers, seems to have caught the eye and excitement of lawmakers. Certainly the promise of the land of milk and honey seems all too good to be true especially amidst the doom and gloom of an $850 million budget shortfall. However, the harsh reality is that on the other end taxpayers are looking at proposals to raise taxes, tax pensions, raise alcohol taxes, slap new taxes on sugary drinks and yet another round of fee and user charge increases. With the loss of millions of dollars in tax breaks and tax credits, how can local taxpayers buy into proposals like these, especially in light of the fact that lawmakers are unwilling to make cuts in other programs? Before lawmakers go off on the deep end entranced by all of these wonderful offers to bring the state to the land of milk and honey, they need to address the fiscal realities on the road before them. On top of this all, lawmakers have yet to address the unfunded liability of the state's retirement and health system.

So while there be the promise of a new industry and increased career opportunities, lawmakers must return to the cold hard reality of solving the problems at hand. The long and short of it is the due in large part to the irresponsibility of handling state finances in the past, taxpayers cannot afford proposals like this. Thanks to gushing generosity of those lawmakers who gave the state's bank away in all sorts of tax incentive schemes in recent years, taxpayers cannot afford what looks like a promising opportunity.

Digested 2/28/11

UNIVERSITY OF HAWAIʻI SYSTEM

Legislative Testimony

Testimony presented before the
House Committee on Finance
March 2, 2011 at 10:00 a.m.
By Linda K. Johnsrud
Executive Vice President for Academic Affairs & Provost, University of Hawaiʻi

HB 1308 HD1: RELATING TO DIGITAL MEDIA

Chair Oshiro, Vice Chair Lee, and members of the House Committee on Finance:

Thank you for this opportunity to testify on House Bill 1308 House Draft 1 that establishes a digital media infrastructure tax credit for projects located in enterprise zones around University of Hawaiʻi campuses and specifies how the Hawaiʻi film office special fund will be used.

The University of Hawaiʻi (UH) is not in a position to comment on the implications of the infrastructure tax credit, but we would like to state that we intend to extend digital media programs to UH West Oʻahu and appreciate the effort of this bill to assist campus in its development. The UH System has recognized a need to expand its digital media programs to include the establishment of an applied baccalaureate degree in this area at UH West Oʻahu. Toward this end, in the past year the system and campuses have held a series of systemwide academic planning meetings around the development of program pathways tied to creative media. This work will facilitate the coordination and establishment of the program at the UH West Oʻahu campus.

Thank you for the opportunity to testify.