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LATE TESTIMONY

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

Date: Tuesday, February 14, 2012

Time: 8:30 a.m.

Place: Conference Room 312, State Capitol

From: Frederick D. Pablo, Director
Department of Taxation

Re: H.B. No. 116 H.D. 1 Relating to Medical Enterprise Zones

This measure seeks to establish a pilot medical enterprise zone program in the State to encourage the development of medical and research services. The pilot program will initially cover West Maui and provides a three-year qualified income tax credit of twenty-five percent and an exemption from the general excise and use tax for qualified income earned by the facility in the medical zone. In addition, the gross proceeds received by a licensed contractor for construction of a facility within three years of qualification as a medical zone business will be exempt from the general excise tax.

The Department of Taxation (Department) defers to the Department of Health and to the Department of Business, Economic Development, and Tourism on the merits of this measure. The Department offers the following comments, however, regarding the measure.

While the Department understands the intent of the measure, which is to address the chronic shortage of medical services, especially on the outer islands, the Department would note that most medical facilities are established as a not for profit entity, and as such the income tax benefits would not be applicable. While the service provider or provider groups may be organized as a for profit business, the income tax benefits would not flow to them if the medical enterprise zone organization to which they provide services is a not for profit entity. Although these providers or provider groups could themselves organize as a medical enterprise zone business, they are unlikely to meet the increase in employees required to obtain the tax benefits.

The Department would also note that medical research facilities, and the research and development of genetically-engineered medical products, are already qualify under existing enterprise zone law. Specifically, section 209E-2, Hawaii Revised Statutes, provides that an eligible enterprise zone business activity includes medical and health care services, which is defined as "medical research, clinical trials, and telemedicine, but not routine medical treatment or services".

It is not clear from the measure whether a business could claim the medical zone benefits and

after the qualified period become an enterprise zone company for another qualified period, or vice versa. The Department suggests that inclusion of medical research facilities in the medical zone business qualification is unnecessary and that inclusion may cause confusion.

Thank you for this opportunity to provide comments.