HOUSE OF REPRESENTATIVES
TWENTY-EIGHTH LEGISLATURE, 2015
STATE OF HAWAII

H.B. NO. 1454

A BILL FOR AN ACT

RELATING TO TAXATION.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF HAWAII:

SECTION 1. The legislature finds that there is a great need for Hawaii to develop and support manufacturing in the State. Hawaii imports over ninety per cent of the products consumed each year. At the same time, there is a great demand outside the State for products that are made in Hawaii.

The purpose of this Act is to promote manufacturing in Hawaii by establishing a temporary income tax credit for taxpayers who incur expenses for manufacturing products in Hawaii.

SECTION 2. Chapter 235, Hawaii Revised Statutes, is amended by adding a new section to be appropriately designated and to read as follows:

"**§235- Manufacturing tax credit.** (a) There shall be allowed to each taxpayer subject to the tax imposed by this chapter, a manufacturing income tax credit, which shall be deductible from the taxpayer's net income tax liability, if any, imposed by this chapter for the taxable year in which the credit is properly claimed.

(b) The amount of the tax credit allowed under subsection (a) shall be twenty per cent of the qualified manufacturing costs incurred during the taxable year; provided that the total credit claimed per taxpayer shall not exceed $200,000.

In the case of a partnership, S corporation, estate, or trust, the tax credit allowable is for qualified manufacturing costs incurred by the entity for the taxable year. The cost upon which the tax credit is calculated shall be determined at the entity level. Distribution and share of credit shall be determined by rule.

If a deduction is taken under section 179 (with respect to election to expense depreciable business assets) of the Internal Revenue Code of 1986, as amended, no tax credit shall be allowed for those costs for which the deduction is taken.

The bases for eligible property for depreciation of accelerated cost recovery system purposes for state income taxes shall be reduced by the amount of the credit allowable and claimed.

(c) If the tax credit under this section exceeds the taxpayer's net income tax liability, the excess of the tax credit over liability may be used as a credit against the taxpayer's net income tax liability in subsequent years until exhausted. Every claim, including amended claims, for a tax credit under this section shall be filed on or before the end of the twelfth month following the close of the taxable year for which the credit may be claimed. Failure to comply with the foregoing provision shall constitute a waiver of the right to claim the credit.

(d) The director of taxation:

(1) Shall prepare any forms that may be necessary to claim a credit under this section;

(2) May require the taxpayer to furnish additional information to ascertain the validity of the claim for credit made under this section; and

(3) May adopt rules pursuant to chapter 91 to effectuate this section.

(e) The department of business, economic development, and tourism shall, for each taxpayer claiming a credit under this section:

(1) Maintain records of the total amount of qualified manufacturing costs claimed;

(2) Verify the amount of the qualified manufacturing costs claimed;

(3) Total all qualified manufacturing costs claimed; and

(4) Certify the total amount of the tax credit for each taxable year.

Upon each certification, the department of business, economic development, and tourism shall issue a certificate to the taxpayer verifying the qualified manufacturing costs and the credit amount certified for each taxable year.

The taxpayer shall file the certificate with the taxpayer's tax return with the department of taxation. Notwithstanding the department of business, economic development, and tourism's certification authority under this section, the director of taxation may audit and adjust the certification to conform to the facts.

(f) As used in this section:

"Net income tax liability" means income tax liability reduced by all other credits allowed under this chapter.

"Qualified manufacturing costs" means expenditures for:

(1) Costs incurred to purchase equipment to be used in manufacturing tangible personal property in the State; and

(2) Costs incurred to train employees to manufacture tangible personal property in the State."

SECTION 3. New statutory material is underscored.

SECTION 4. This Act shall take effect upon its approval and shall apply to taxable years beginning after December 31, 2015; provided that this Act shall be repealed on January 1, 2023.

INTRODUCED BY: ____________________

JAN 29 2015

H.B. NO. 1454

Report Title:
Manufacturing; Income Tax Credit

Description:
Establishes an income tax credit for taxpayers who incur certain expenses for manufacturing products in Hawaii. Applies to taxable years beginning after December 31, 2015. Sunsets January 1, 2023.

The summary description of legislation appearing on this page is for informational purposes only and is not legislation or evidence of legislative intent.

DAVID Y. IGE
GOVERNOR

LUIS P. SALAVERIA
DIRECTOR

MARY ALICE EVANS
DEPUTY DIRECTOR

DEPARTMENT OF BUSINESS, ECONOMIC DEVELOPMENT & TOURISM

No. 1 Capitol District Building, 250 South Hotel Street, 5th Floor, Honolulu, Hawaii 96813
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Statement of
LUIS P. SALAVERIA
Director
Department of Business, Economic Development, and Tourism
before the

HOUSE COMMITTEE ON ECONOMIC DEVELOPMENT AND BUSINESS

Friday, February 06, 2015
9:20 am
State Capitol, Conference Room 312

in consideration of
HB 1454
RELATING TO TAXATION.

Chair Kawakami, Vice-Chair Kong and Members of the Committee. The Department of Business, Economic Development, and Tourism (DBEDT) supports the intent of this bill provided that its passage does not replace or adversely impact priorities indicated in the Executive Budget.

The establishment of an income tax credit for taxpayers who incur certain expenses for manufacturing can encourage more manufacturing in the State. Currently, Hawaii imports ninety percent of the products consumed each year. Increased local manufacturing can reduce the volume of imports from outside the State. In addition, manufacturing can play an important role in diversifying the State's economy and providing well-paid skilled jobs for Hawaii residents.

DBEDT defers to the Department of Taxation and the Department of Budget and Finance on the fiscal impact of this bill.

Thank you for the opportunity to provide these comments.

DAVID Y. IGE
GOVERNOR

SHAN TSUTSUI
LT. GOVERNOR

MARIA E. ZIELINSKI
DIRECTOR OF TAXATION

STATE OF HAWAII
DEPARTMENT OF TAXATION
P.O. BOX 259
HONOLULU, HAWAII 96809
PHONE NO: (808) 587-1540
FAX NO: (808) 587-1560

To: The Honorable Derek S.K. Kawakami, Chair
and Members of the House Committee on Economic Development and Business

Date: Friday, February 06, 2015
Time: 9:20 A.M.
Place: Conference Room 312, State Capitol

From: Maria E. Zielinski, Director
Department of Taxation

Re: H.B. 1454, Relating to Taxation

The Department of Taxation (Department) provides the following comments regarding H.B. 1454 for your consideration.

H.B. 1454 establishes a nonrefundable income tax credit for taxpayers who incur certain expenses for manufacturing products in Hawaii. Specifically, this measure would provide a nonrefundable income tax credit of 20 percent of the costs incurred to purchase equipment to be used in the manufacture of tangible personal property in the State and the costs incurred to train employees in the manufacturing process, up to a maximum credit of $200,000 per taxpayer per year. The tax credit, as proposed, applies to taxable years beginning after December 31, 2015, and is repealed on January 1, 2023, and is effective upon approval.

The Department notes that there is no requirement in this measure that the equipment actually be installed and placed in service in order to qualify for the credit. As it is written, both the seller of equipment and machinery which would be used to manufacture tangible personal property and the taxpayer who actually utilizes the machinery and equipment to manufacture goods in the State would be eligible for the credit since the measure only requires that the equipment to be used in manufacturing tangible personal property in the State. In addition, the measure contains no timeframe in which the equipment must be placed in service. The Department recommends that such a timeframe be included, to prevent a taxpayer from simply purchasing equipment without ever placing it into service, or merely purchasing equipment in anticipation of a later expansion.

In addition, the Department believes that the credit should apply only to the taxpayer who first places such equipment or machinery in service in this State, and not to any subsequent user if the equipment is later resold. This will prevent a taxpayer who has already claimed the credit from reselling equipment and machinery so that another (possibly even related) taxpayer could again claim the credit based upon the amount that it paid.

H.B. 1454 also does not have any requirement that the costs incurred to train employees to manufacture tangible personal property in the State be reasonable. A taxpayer could therefore hire a related entity to train its personnel solely to inflate the costs eligible for the credit, or even provide training not necessary for the use of the equipment. The Legislature may also want to consider adding a lifetime cap on the credit that may be claimed by each taxpayer to prevent abuse.

For clarity, the Department recommends that "qualified manufacturing costs" be defined as follows:

"Qualified manufacturing costs" means expenditures for:

(1) Costs incurred to purchase equipment to be used by the taxpayer in manufacturing tangible personal property in the State and which is placed in service within one (1) year after the date of purchase, provided that the credit under this section has not been previously claimed by any taxpayer in this State on such equipment; and

(2) Reasonable and necessary costs incurred to train employees to manufacture tangible personal property in the State."

Finally, the Department notes that some jurisdictions consider electricity to be tangible personal property. Historically, the Department has not deemed electricity to be tangible personal property. Therefore, in order to avoid disagreements with taxpayers over whether electricity generation is an eligible activity, and in light of the existing Renewable Energy Technologies Income Tax Credit at Hawaii Revised Statutes section 235-12.5, and the tax credit for energy storage being considered by the Legislature this year, the Department suggests that a provision be added to specifically exclude costs related to the production of electricity. The following language could be added after the last sentence in subsection (a) to accomplish the preclusion:

Provided that qualified manufacturing costs shall not include any costs related to the production of electricity.

Thank you for the opportunity to provide comments.

Written Statement of
ROBBIE MELTON
Executive Director & CEO
High Technology Development Corporation
before the
HOUSE COMMITTEE ON ECONOMIC DEVELOPMENT & BUSINESS
Friday, February 6, 2015
9:20 a.m.
State Capitol, Conference Room 312
In consideration of

HB1454 RELATING TO TAXATION.

Chair Kawakami, Vice Chair Kong, and Members of the Committee on Economic Development & Business.

The High Technology Development Corporation (HTDC) **supports the intent of** HB1454 relating to establishing an income tax credit for taxpayers who incur certain expenses for manufacturing products in Hawaii.

HTDC supports local manufacturers through our federally funded INNOVATE Hawaii program. The manufacturing industry provides export and import substitution opportunities that improve our economy and has been identified nationally as a key driver for innovation. Hawaii manufacturers currently receive limited support from the state while facing the challenges of high energy and shipping costs. The tax credit can assist to make the manufacturers more competitive.

As part of our 80/80 vision to create 80,000 new innovation and creative jobs paying $80,000 or more by 2030, HTDC supports incentives for manufacturers to improve their capacity to reduce imports and increase exports. SB1001 alternatively proposes to offer benefits through a grant program administered by HTDC. The grant program would help reduce costs for manufacturers and expand capacity through similar incentives and offers some discretionary oversight to award projects that show potential for growing the Hawaii economy. On the other hand, a tax credit program can be easy to understand and can follow the model from other industries. HTDC prefers the grant program, but would be supportive of either. HTDC defers to the appropriate departments regarding the impact of administering the tax credit.

Thank you for the opportunity to offer these comments.

SUBJECT: INCOME, Manufacturing tax credit

BILL NUMBER: SB 1365; HB 1454 (Identical)

INTRODUCED BY: SB by Wakai; HB by Kawakami, Cullen, Morikawa, Tokioka

EXECUTIVE SUMMARY: Establishes an income tax credit of 20% of qualified manufacturing costs incurred in a table year, not to exceed $200,000. The adoption of this credit would result in a subsidy of state funds. Lawmakers should consider the criteria established by the 2001-2003 Tax Review Commission (discussed below) before enacting this or any other new business incentive that operates through the tax system.

BRIEF SUMMARY: Adds a new section to HRS chapter 235 to allow taxpayers to claim an income tax credit of 20% of the qualified manufacturing costs incurred in a taxable year provided that the total credit claimed per taxpayer shall not exceed $200,000.

In the case of a partnership, S corporation, estate, or trust the tax credit allowable is for qualified manufacturing costs incurred by the entity for the taxable year with distribution and share of the credit to be determined by section 704(b) of the Internal Revenue Code. If a deduction is taken under IRC section 179 (with respect to election to expense depreciable business assets), no credit shall be allowed for that portion for which the deduction is taken. The basis of eligible property for depreciation or accelerated cost recovery system purposes for state income tax purposes shall be reduced by the amount of credits allowable and claimed.

Credits in excess of a taxpayer's income tax liability shall be applied to subsequent tax liability until exhausted. Claims for the credit, including any amended claims, must be filed on or before the end of the twelfth month following the close of the taxable year. The director of taxation may adopt rules pursuant to HRS chapter 91 and prepare the necessary forms to claim the credit and may require proof of the claim for the credit. Requires the director of business, economic development, and tourism (DBEDT) to: (1) maintain records of the total amount of the qualified manufacturing costs for each taxpayer claiming the credit; (2) verify the amount of the qualified manufacturing costs claimed; (3) total all qualified manufacturing costs claimed; and (4) certify the total amount of the tax credit for each taxable year. DBEDT shall issue a certificate to the taxpayer verifying the qualified manufacturing costs and the credit amount certified for each taxable year. Requires the taxpayer to file the certificate with the taxpayer's tax return with the department of taxation.

Defines "qualified manufacturing costs" as costs incurred to: (1) purchase equipment to be used in manufacturing tangible personal property in the state; and (2) train employees to manufacture tangible personal property in the state.

This act shall be repealed on January 1, 2023.

EFFECTIVE DATE: Tax years beginning after December 31, 2015

STAFF COMMENTS: It appears that this measure is intended to provide an incentive in the form of an income tax credit to encourage manufacturing in the state. It should be noted that tax credits generally are designed to reduce the tax burdens of certain groups by refunding a portion of taxes paid on purchases of essential items and services. This credit of 20% of qualified manufacturing costs amounts to nothing more than a subsidy of state funds as there is no obvious undue burden of taxes.

It should be remembered that the 2001-2003 Tax Review Commission set forth recommended requirements for new tax incentives such as this one:

(I) *Cost-benefit studies*. Cost-benefit studies should be required prior to inaugurating new or revised tax credit programs. Policy makers should use only those programs with quantifiable and demonstrable benefits over costs. Such costs and benefits should not only look at fiscal and economic effects, but should examine social ones as well.

(ii) *Periodic evaluations* of all tax incentive programs should be required.

(iii) *Truth and disclosure reporting* separate and apart from a taxpayer's tax returns should generally be required of all taxpayers benefitting from tax incentive programs, making public all aspects of these subsidies for private investment.

(iv) *Strategic planning*. Embed tax incentives in strategic plans, leveraging as much of the State's scarce resources as possible. Rather than promoting diverse incentives in search of a cohesive strategy, the State should employ only incentives that make strategic sense.

(v) *Public participation*. Encourage public participation in and comment on tax incentive use to foster public accountability. There should at least be as much public discussion over generous multi-million dollar business incentive tax credits as there is over $50,000 renovations to school libraries.

(vi) *Sunset provisions* should be required to ensure that the above processes will be implemented before an incentive can be extended. It should be demonstrated to the Legislature that the targeted benefit to the State was in fact received, what the tax cost of that benefit was, and whether the continuation of the tax incentive is appropriate and necessary.

(vii) *Enforcement*. Given the magnitude and the complexity of these business incentive tax credits, the small chance of audit, ambiguous statutory requirements as to what can be claimed as a credit, there must be legislative oversight of these credits. In addition, the Department of Taxation must be given sufficient resources to police these credits.

If lawmakers are inclined to enact this credit, amendments should be considered addressing the criteria set forth above.

Digested 2/5/15

HAWAII FOOD INDUSTRY ASSOCIATION

Executive Officers:
John Schilf, RSM Hawaii - Chairperson
Derek Kurisu, KTA Superstores - Vice Chair
Lisa DeCoito, Aloha Petroleum - Treasurer
John Erickson, Frito-Lay - Secretary
Lauren Zirbel, Executive Director

1050 Bishop St. PMB 235
Honolulu, HI 96813
Fax : 808-791-0702
Telephone : 808-533-1292

TO:
COMMITTEE ON ECONOMIC DEVELOPMENT & BUSINESS
Representative Derek S.K. Kawakami, Chair
Representative Sam Satoru Kong, Vice Chair

FROM: HAWAII FOOD INDUSTRY ASSOCIATION
Lauren Zirbel, Executive Director

DATE: February 6, 2015
TIME: 9:20am
PLACE: Conference Room

RE: HB1454

Position: Support

The Hawaii Food Industry Association is comprised of two hundred member companies representing retailers, suppliers, producers, and distributors of food and beverage related products in the State of Hawaii.

The tax credit proposed in this bill would help grow and diversify our economy, keep more dollars in Hawaii, decrease our dependence on imports, and grow and strengthen the Made in Hawaii brand.

Research has shown that a diversified economy and a business friendly tax climate are both key factors in keeping unemployment low. This bill could allow current manufacturers in our state to grow their businesses and can open the door for even more production here in Hawaii. This means more jobs and a stronger economy for the entire state.

Increasing manufacturing will also mean we are less reliant on imported goods. We currently import over 90% of the products we use here in the state. This situation leaves us vulnerable to any supply chain interruptions, adds shipping cost to almost all goods, and sends millions of dollars a year out of the state. Importing less and making more can have wide reaching positive impacts for everyone from the manufacturers to the consumers.

This bill will also open the door for more products to earn the distinction of being Made in Hawaii. The products we currently make here in the state have a worldwide reputation for quality and excellence. There is strong demand both in and out of the state for more products of that high caliber, and this bill can help grow our manufacturing industry to meet that demand.

For these reasons we ask that you please vote yes on this measure.

Thank you for the opportunity to testify.

KYD, Inc. dba k. yamada distributors
An independent leader in packaging and wholesale distribution
P.O. BOX 29669, Honolulu, Hawaii 96820 Phone: (808) 836-3221 Fax: (808) 833-8995

HB 1454, Relating to Taxation
House EDB Committee – Friday, February 6, 2015
9:20 am - Room 312
Written Testimony by: Dexter Yamada
Position: Support

Chair Kawakami and Members of the House EDB Committee:

I am Dexter Yamada, President of KYD, Inc. dba: K. Yamada Distributors. KYD, Inc. is a local family run business that originated in the 1940's as a florist and florist supply distributor, and in 1958, evolved into a packaging company. Today, KYD, Inc and its sister company, Hawaii Foam Products, LLC, employ about 90 to 100 employees and contribute to Hawaii's economy through taxes and payroll. Our companies manufacture packaging materials such as food-grade EPS (Expanded Polystyrene) food containers, and distribute a variety of supplies, to include compostable containers, for food processors, food establishments, supermarkets, hotels hospitals and other institutions.

We appreciate this measure that supports Hawaii's manufacturing industry. Locally manufactured products contribute to import replacement, and help with local job creation. The proposed temporary tax credit for expenditures to be used in manufacturing tangible personal property in the State and for costs incurred to train employees to manufacture tangible personal property in the State will be of help to local manufacturing businesses. This in turn, lends to greater efficiency and reduction in the cost of products to customers.

Thank you for the opportunity to testify.

WILL CALL, G&A, AND WAREHOUSE OFFICES: 2949 Koapaka Street, Honolulu, Hawaii 96819-1923 Phone: (808) 836-3221 Fax: (808) 833-8995

Meadow Gold Dairies

HB 1454, Relating to Taxation
House EDB Committee
Friday, February 6, 2015
9:20 am, Room 312
Written Testimony By: Glenn Muranaka

Position: Support

Chair Kawakami and Members of the House EDB Committee:

My name is Glenn Muranaka, President and General Manager of Meadow Gold Dairies. Our company has been in Hawaii since 1897—118 years, providing Hawaii consumers with a variety of milk products and juices. Meadow Gold's long history has not come without effort. We continually adapt to our customers' and consumers' ever-changing needs, and we constantly evolve along with our industry, our community and our market. Over the years, this has required that we struggle, tighten our belts, innovate and work extremely hard, making us a better company in the process. The foundation of this work rests with the 330 employees that are committed to providing superior quality products.

There are approximately 1000 active manufacturers in the state that employ almost 17,000 people at an average compensation rate of $42,896 or over $6,000 more than the average private non-farm employee. Manufacturers helped Hawaii's economy by contributing nearly $570 million in manufactured goods exported in 2012.

The proposed temporary tax credit for the specific purposes of manufacturing tangible personal property and to train employees to manufacture such tangible personal property will help fuel manufacturing in Hawaii to grow and provide more products for both local consumption and export. There is movement to begin to manufacture more in the continental United States. At the same time, Hawaii still has some competitive disadvantages. This program will help companies in Hawaii start or grow their operations.

Your support of this measure is appreciated. Thank you for the opportunity to submit testimony.

925 Cedar Street P.O. Box 1880, Honolulu, Hawaii 96805 (808) 949-6161 (808) 944-5901 fax

From: mailinglist@capitol.hawaii.gov
Sent: Friday, February 06, 2015 9:23 AM
To: edbtestimony
Cc: carl.campagna@kamakagreen.com
Subject: *Submitted testimony for HB1454 on Feb 6, 2015 09:20AM*

LATE

HB1454
Submitted on: 2/6/2015
Testimony for EDB on Feb 6, 2015 09:20AM in Conference Room 312

Submitted By	Organization	Testifier Position	Present at Hearing
Carl	Individual	Support	No

Comments:

Please note that testimony submitted less than 24 hours prior to the hearing, improperly identified, or directed to the incorrect office, may not be posted online or distributed to the committee prior to the convening of the public hearing.

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HAWAIʻI FARM BUREAU

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LATE

February 6, 2015

HEARING BEFORE THE
HOUSE COMMITTEE ON ECONOMIC DEVELOPMENT & BUSINESS

TESTIMONY ON HB 1454
REALTING TO TAXATION

Room 312
9:20 AM

Chair Kawakami, Vice Chair Kong, and Members of the Committee:

I am Christopher Manfredi, President of the Hawaii Farm Bureau (HFB). Organized since 1948, the HFB is comprised of 1,932 farm family members statewide, and serves as Hawaii's voice of agriculture to protect, advocate and advance the social, economic and educational interest of our diverse agricultural community.

HFB supports HB 1454, which is part of the Chamber of Commerce's economic development package. There are approximately 1,000 active manufacturers in the state that employ almost 17,000 people at an average compensation rate of $42,896 or over $6,000 more than the average private non-farm employee. Manufacturers helped Hawaii's economy by contributing nearly $570 million in manufactured goods exported in 2012.

The bill gives a tax credit to companies on their expenditures for manufacturing equipment and the training of their employees. We believe that this credit will help fuel manufacturing in Hawaii to grow and provide more products for both local consumption and export. There is an ongoing movement to revitalize manufacturing in the U.S, yet Hawaii still has some competitive disadvantages. This credit will help companies in Hawaii to start or grow their operations.

According to the National Association of Manufacturers, every new manufacturing job created adds another 1.6 jobs to the local service economy, and for every dollar in manufacturing sales, another $1.34 is added to the economy. Investments in manufacturing have a stronger impact than investments most other economic sector. This is a wise investment for Hawaii.

Thank you for the opportunity to comment on this measure.

Testimony to the House Committee on Economic Development & Business
Friday, February 6, 2015 at 9:20 A.M.
Conference Room 312, State Capitol

LATE

RE: HOUSE BILL 1454 RELATING TO TAXATION

Chair Kawakami, Vice Chair Kong, and Members of the Committee:

The Chamber of Commerce of Hawaii ("The Chamber") **strongly supports** HB 1454, which establishes an income tax credit for taxpayers who incur certain expenses for manufacturing products in Hawaii.

The Chamber is the largest business organization in Hawaii, representing over 1,000 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 supports this bill as part of its economic development package. There are approximately 1,000 active manufacturers in the state that employ almost 17,000 people at an average compensation rate of $42,896 or over $6,000 more than the average private non-farm employee. Manufacturers helped Hawaii's economy by contributing nearly $570 million in manufactured goods exported in 2012.

The bill gives a 20% tax credit to companies on their expenditures for manufacturing equipment and the training of their employees. We believe that this credit will help fuel manufacturing in Hawaii to grow and provide more products for both local consumption and export. There is movement to begin to manufacture more back in the U.S. At the same time Hawaii still has some competitive disadvantages. This credit will help companies in Hawaii to start or grow their operations.

According to the National Association of Manufacturers, every new manufacturing job created adds another 1.6 jobs to the local service economy, and for every dollar in manufacturing sales, another $1.34 is added to the economy. Investments in manufacturing have a stronger impact than investments in most other economic sectors.

Thank you for the opportunity to testify on this matter.

1132 Bishop Street, Suite 2105 • Honolulu, Hawaii 96813 • Phone: (808) 545-4300 • Facsimile: (808) 545-4369