DAVID Y. IGE
GOVERNOR

JOSH GREEN M.D.
LT. GOVERNOR

ISAAC W. CHOY
DIRECTOR OF TAXATION

STATE OF HAWAII
DEPARTMENT OF TAXATION
P.O. BOX 259
HONOLULU, HAWAII 96809
PHONE NO: (808) 587-1540
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To: The Honorable Sean Quinlan, Chair;
The Honorable Daniel Holt, Vice Chair;
and Members of the House Committee on Economic Development

From: Isaac W. Choy, Director
Department of Taxation

Date: Wednesday, February 2, 2022
Time: 10:00 A.M.
Place: Via Video Conference, State Capitol

Re: H.B. 2002, Relating to Taxation

The Department of Taxation (Department) appreciates the intent of H.B. 2002 and offers the following comments for the committee's consideration.

H.B. 2002 reinstates the Renewable Fuels Production Tax Credit (RFPTC), which was previously codified at section 235-110.31, Hawaii Revised Statutes (HRS), before its duly scheduled repeal on December 31, 2021. The credit is equal to 20 cents per seventy-six thousand British thermal units of renewable fuels sold for distribution in Hawaii; provided that the taxpayer's production of renewable fuels is not less than two billion five hundred million British thermal units of renewable fuels per calendar year. The Department of Business, Economic Development, and Tourism (DBEDT) is responsible for certifying the credit and for administering the $3,000,000 annual aggregate cap for all eligible taxpayers. Taxpayers must also provide written notice to the Department and to DBEDT of their intention to begin production of renewable fuels prior to production of any renewable fuels in a calendar year. The measure applies to taxable years beginning after December 31, 2021.

The Department also notes that Section 2 describes the credit as having a "five-year credit period," much like the previous version of the credit did. This limitation applies per taxpayer, thus, a taxpayer could form a new entity and qualify for a new five-year credit period. One way to address this would be to include a provision as follows:

> Each taxpayer, together with all of its related entities (as determined under Internal Revenue Code section 267(b)) and all business entities under common control (as determined under Internal Revenue Code sections 414(b), 414(c), and 1563(a)), shall not be eligible for more than a

single five-year credit period.

Thank you for the opportunity to provide comments.

HB-2002
Submitted on: 2/1/2022 9:06:14 AM
Testimony for ECD on 2/2/2022 10:00:00 AM

Submitted By	Organization	Testifier Position	Remote Testimony Requested
Scott Glenn	Hawaii State Energy Office	Support	Yes

Comments:

Kirsten Baumgart Turner would also like access to join this hearing.

LATE *Testimony submitted late may not be considered by the Committee for decision making purposes.

DAVID Y. IGE
GOVERNOR

CRAIG K. HIRAI
DIRECTOR

GLORIA CHANG
DEPUTY DIRECTOR

EMPLOYEES' RETIREMENT SYSTEM
HAWAI'I EMPLOYER-UNION HEALTH BENEFITS TRUST FUND
OFFICE OF THE PUBLIC DEFENDER

STATE OF HAWAIʻI
DEPARTMENT OF BUDGET AND FINANCE
P.O. BOX 150
HONOLULU, HAWAIʻI 96810-0150

ADMINISTRATIVE AND RESEARCH OFFICE
BUDGET, PROGRAM PLANNING AND MANAGEMENT DIVISION
FINANCIAL ADMINISTRATION DIVISION
OFFICE OF FEDERAL AWARDS MANAGEMENT (OFAM)

<u>WRITTEN ONLY</u>

TESTIMONY BY CRAIG K. HIRAI
DIRECTOR, DEPARTMENT OF BUDGET AND FINANC
TO THE HOUSE COMMITTEE ON ECONOMIC DEVELOPM
ON
HOUSE BILL NO. 2002

LATE

February 2, 2022
10:00 a.m.
Room 312 and Videoconference

RELATING TO TAXATION

The Department of Budget and Finance (B&F) offers comments on this bill.

House Bill No. 2002 adds a new section to Chapter 235, HRS, that reinstates the Renewable Fuels Production Tax Credit (RFPTC) which was originally repealed on December 31, 2021. For each taxpayer that produces renewable fuels, the RFPTC would be equal to 20 cents per 76,000 British thermal units (BTUs) per calendar year up to a maximum of $3,000,000 annually over a five-year period, provided that the taxpayer's production of renewable fuels is not less than 2,500,000,000 BTUs per calendar year.

B&F notes that the federal American Rescue Plan (ARP) Act restricts states from using ARP Coronavirus State Fiscal Recovery Funds (CSFRF) to directly or indirectly offset a reduction in net tax revenue resulting from a change in law, regulation, or administrative interpretation beginning on March 3, 2021, through the last day of the fiscal year in which the CSFRF have been spent. If a state cuts taxes during this period, it must demonstrate how it paid for the tax cuts from sources other than the CSFRF, such as:

- By enacting policies to raise other sources of revenue;
- By cutting spending; or
- Through higher revenue due to economic growth.

If the CSFRF provided have been used to offset tax cuts, the amount used for this purpose must be repaid to the U.S. Treasury.

The U.S. Department of Treasury has issued rules governing how this restriction is to be administered. B&F will be working with the money committees of the Legislature to ensure that the State of Hawaiʻi complies with this ARP restriction.

Thank you for your consideration of our comments.

February 2, 2022

Hawaii House of Representatives
House Committee on Economic Development
Hawaii State Capitol
415 South Beretania St.
Honolulu, HI 96813

RE: Hawaii House Bill 2002 – Renewable fuels production tax credit

Dear Chair Quinlan, Vice Chair Holt, and Members of the Committee:

The Pet Food Institute (PFI) appreciates the opportunity to provide comments regarding House Bill 2002.

Established in 1958, PFI is the trade association and the voice of U.S. cat and dog food and treat manufacturers. Our members account for the vast majority of pet food and treats made in the United States and feed 180 million pets in U.S. households. Our members operate under regulations issued by the U.S. Food and Drug Administration and enforced by both federal and state officials. This means dog and cat owners throughout the United States and around the world benefit from science-based regulations that provide the safest animal food supply available globally.

PFI recognizes and supports responsible efforts to address climate change and utilize additional energy sources that reduce carbon emissions. However, we have serious concerns that government incentives and mandates promoting renewable fuel growth have created unintended consequences in supply and demand for animal- and plant-based oils and fats.

Renewable fuel tax credits and mandates for biodiesel create an unfair government-driven market advantage to the energy sector and a disadvantage to companies purchasing ingredients for pet food. Tax credits that favor fuel production over food production create market distortions, producing one problem in a heavy-handed attempt to address another. While other industries reap tax credits for their commodities' use in renewable fuel, the feed industry bears the brunt of this disadvantaged domestic supply, facing significant burdens of cost and sourcing for these critical ingredients. Our members have seen notable input price increases we believe are attributable in large part to the competition for grains by both food and fuel producers.

Renewable fuel demand, particularly renewable diesel, has spiked the price for animal- and plant-based oils and fats to two times their current market value, thus drastically increasing the cost of critical ingredients that pet food makers source for the nutrition and palatability of cat and dog food. Pet food makers rely on the essential fatty acids, found in oils and fat, to formulate foods that deliver nutrients that perform key functions in dog and cat immune and visual systems, as well as supporting a healthy skin and coat. Our members' commitment to long and healthy lives for pets means that they rely on access to dozens of animal- and plant-based oil and fat ingredients. This access is threatened by increased competition for animal protein by-products, grains and grain by-products as a result of tax incentives and mandates.

PFI's members report facing an unprecedented increase in the price of plant-origin ingredients, such as soybean oil, that we believe is attributable to the competition for grains from renewable fuel producers. Our members also reported dwindling access to these ingredients in 2021. While the U.S. historically was able to meet domestic soybean oil needs, our country alarmingly became a net importer of soybean oil in September and October of 2021, and food makers have been forced to import foreign soybean oil, which is more expensive due to heavy tariffs.

Left unchecked, these incentives and drivers for growth of demand for renewable fuels will continue to distort markets for food inputs, effectively making these critical pet food inputs inaccessible for many pet food makers and forcing companies to develop product formulations primarily based more on ingredient access than on ideal complete and balanced formulation considerations.

Now more than ever, it is important to people in the U.S. and around the world to find comfort and companionship with their pets. The human-animal bond is the documented occurrence of a positive connection established between you and your pet, that benefits both of you. In addition to providing companionship, numerous studies have documented the positive effects of the human-animal bond, which provides profound mental, social and physical health benefits for both owners and their companion animals. For example, studies indicate that sharing your life with a dog or cat can help reduce blood pressure and reduce levels of stress, and data indicate that animals can play a role in managing depression.

The last two years have been very challenging, and 2022 will continue to present significant sourcing challenges for pet food makers. Now is not the time to favor the energy sector and disadvantage the feed industry by increasing ingredient costs, risking supply shortages, and adding another layer of stress to pet food makers, pet parents and the pets they love. **PFI respectfully requests that the committee reject tax incentives for biodiesel fuels that use or include animal- and plant-based oils and fats that are historically used in human and pet food.**

On behalf of PFI members, whose nearly 25,000 employees in 32 states provide safe food for the 180 million pets across the U.S., we thank you for the opportunity to share our views. I would be happy to discuss this issue in more detail.

Sincerely,

Savonne Caughey

Savonne Caughey
Senior Director of Advocacy and Government Relations
Pet Food Institute

HAWAII CLEAN POWER ALLIANCE

Testimony to the Committee on Economic Development

Wednesday, February 2, 2022
10:00 AM
VIA Video Conference
Conference Room 312, Hawaii State Capitol
HB 2002

Chair Quinlan, Vice Chair Holt, and members of the committee,

Hawaii Clean Power Alliance (HCPA) **supports** HB 2002, which reinstates the renewable fuels production tax credit.

Hawaii Clean Power Alliance is a nonprofit alliance organized to advance and sustain the development of clean energy in Hawaii. Our goal is to support the state's policy goal of 100 percent renewable energy by 2045. We advocate for utility-scale renewable energy, which is critical to meeting the state's clean energy and carbon reduction goals.

Tax credits have proven essential in building momentum and scale in the development and distribution of diverse renewable fuel sources. Grid stability is essential to resiliency, and it's clear that Hawaii's grid will need to depend on a more diverse variety of resources as it transitions to no fossil fuel generation. These production tax credits provide incentives for the production of a diverse renewable fuel supply.

These types of renewable fuels, such as hydrogen, can be used to transform the electric grid into a zero emissions grid, enable long-term storage and power zero emissions vehicles. This type of fuel is innovative but also the technology requires a considerable amount of financial resources. The recently passed Federal Infrastructure legislation recognizes the importance of grid resiliency as well as hydrogen.

Hawaii is known for its clean energy initiatives, and this bill can attract many developers to the islands to showcase Hawaii's embracing of industry leading technologies. Renewable fuels can spur innovation, economic development and many well-paying jobs. We therefore request consideration of the committee to increase the cap for individual taxpayers, increase the state cap for the credit, and consider a discounted refund clause in order to incentivize more development in Hawaii.

We ask the committee to pass this bill.

Thank you for the opportunity to testify

HAWAI'I GAS
THE CLEAN ENERGY COMPANY

Testimony to
The Committee on Economic Development

Wednesday, February 2, 2022
10:00 AM
VIA Video Conference
Conference Room 312, Hawaii State Capitol

HB 2002

Chair Quinlan, Vice Chair Holt, and members of the committee,

Hawaii Gas **supports** **HB 2002,** which reinstates the renewable fuels production tax credit.

Hawaii Gas is a national leader in the production and distribution of renewable gas in a gas utility system and has committed to support the state's march towards carbon neutrality by 2045. Despite representing less than 1% of the greenhouse gases emitted into Hawaii's atmosphere, we agree that it's everyone's responsibility to do everything we can to make sure Hawaii meets that milestone.

Renewable feedstocks are key components to creating renewable natural gas, hydrogen, and other renewable biofuels, all of which are important fuel replacements for fossil fuels.

Tax incentives have proven to be an effective tool in encouraging the development of innovative new technologies, just as seen in the burgeoning solar and wind industry decades ago. These incentives also provide a method for ratepayers to be provided lower costs for new technologies that have not had time to mature and scale. Hawaii recognized the impact of this concept when it created a production tax credit six years ago, which unfortunately sunset on December 31, 2021. It was during this time that Hawaii Gas developed a unique project in partnership with the City and County of Honolulu to take gas emissions from the wastewater treatment process, which were previously being released into the atmosphere, and capture it to create renewable natural gas. This project was equivalent to taking up to 400 cars off the road every year. This project was among the first in the country to inject that gas into the pipeline.

Reinstating this credit will be pivotal to generate more of these innovative clean energy alternatives.

We ask the committee to consider the following amendments to the bill:

- Add "wastewater" in the definition of a renewable source;
- Include a "refundable tax credit" amendment similar to the section in the renewable energy investment tax credit (HRS § 235-12.5) because new developers may not have a state tax appetite for many years, allowing the credits to benefit the ratepayers;
- Increase the maximum cap per project in recognition of the large investment necessary to produce renewable fuels;
- Increase the state cap to encourage more producers to create the fuel that will replace fossil fuels.

We appreciate the benefits this legislation will bring to allow Hawaii to benefit from affordable energy while sustaining our reliability and resiliency, so critical to Hawaii's infrastructure especially in times of natural disasters.

We respectfully request the committee to include these amendments and pass HB 2002.

Thank you for the opportunity to testify.

LEGISLATIVE TAX BILL SERVICE

TAX FOUNDATION OF HAWAII

126 Queen Street, Suite 305 Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: INCOME, Renewable Fuels Production Tax Credit

BILL NUMBER: HB 2002, SB 2478

INTRODUCED BY: HB by NISHIMOTO, SB by DELA CRUZ

EXECUTIVE SUMMARY: Reinstates the renewable fuels production tax credit. Our view is that a direct appropriation to buy or subsidize energy production would be far superior because (1) we know how much we are spending and (2) we know what we are buying.

SYNOPSIS: Adds a new section to HRS chapter 235 to establish a nonrefundable renewable fuels production tax credit. The credit shall be allowed to taxpayers producing qualifying renewable fuels provided the credit shall not be claimed for more than five years beginning from the first taxable year in which a taxpayer begins renewable fuels production at a level of at least 2.5 billion British thermal units (BTU) of renewable fuels per calendar year.

The annual dollar amount of the credit shall be 20 cents per 76,000 BTUs of renewable fuels using the lower heating value sold for distribution in Hawaii; provided that the taxpayer's production of renewable fuels is not less than 2.5 billion BTUs of renewable fuels per year. Limits the amount of tax credit that may be claimed by a taxpayer to $3 million per taxable year.

Defines "renewable fuels" as fuels produced from renewable feedstocks provided that the fuels shall be sold as a fuel in Hawaii, and meet the relevant ASTM International specifications for the particular fuel or other industry specifications, including but not limited to: (1) methanol, ethanol, or other alcohols; (2) hydrogen; (3) biodiesel or renewable diesel; (4) biogas; (5) other biofuels; (6) renewable jet fuel or renewable gasoline; or (7) logs, wood chips, wood pellets, or wood bark.

Defines "renewable feedstocks" as (1) biomass crops and other renewable organic material, including but not limited to logs, wood chips, wood pellets, and wood bark; (2) agricultural residues; (3) oil crops, including but not limited to algae, canola, jatropha, palm, soybean, and sunflower; (4) sugar and starch crops, including but not limited to sugar cane and cassava; (5) other agricultural crops; (6) grease and waste cooking oil; (7) food wastes; (8) municipal solid wastes and industrial wastes; (9) water; and (10) animal residues and wastes, to the extent that they can be used to generate energy.

Requires the department of business, economic development and tourism (DBEDT) to verify and certify each claim for the credit including the total amount of credit for each taxable year and the cumulative amount of tax credit during the credit period. The department shall issue a certificate to qualifying taxpayers who shall file the certificate with the department of taxation (DOTAX).

If in any year the annual amount of certified credits reaches $3 million in the aggregate, DBEDT shall discontinue certifying credits and notify the department of taxation.

If the amount of credits exceeds the taxpayer's income tax liability, the excess of credit over liability may be used as a credit against the taxpayer's income tax liability in subsequent years until exhausted. All claims for a credit under this section shall be properly 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.

Prior to production of any qualifying renewable fuels for the year, the taxpayer is to provide written notice of the taxpayer's intention to begin production of qualifying renewable fuels to DOTAX and DBEDT with information on the taxpayer, facility location, facility production capacity, anticipated production start date, and the taxpayer's contact information. The taxpayer shall also provide written notice to the director of taxation and the director of DBEDT within 30 days following the start of production and include the production start date and expected renewable fuel production for the next year.

In each calendar year during the credit period, the taxpayer shall provide information to the director of DBEDT on the number of BTU of renewable fuels produced and sold during the previous calendar year, the type of fuels, feedstocks used for renewable fuels production, the number of employees of the facility and each employee's state of residency, and the projected number of BTU of renewable fuels production for the succeeding year.

In the case of a partnership, S corporation, estate, or trust, distribution and share of the tax credit for renewable fuels production shall be determined pursuant to section 704(b) (with respect to partner's distributive share) of the Internal Revenue Code.

Directs the director of DBEDT, following each year in which a credit under this section has been claimed, to submit a written report to the governor and legislature regarding the production and sale of renewable fuels. The report shall include the number, location, and production of renewable fuels production facilities in the State and outside the State that have claimed a credit under this section; the total number of British thermal units of renewable fuels, broken down by type of fuel, produced and sold during the previous year; and the projected number of BTU of renewable fuels production for the succeeding year.

Requires DOTAX to prepare the necessary forms to claim the credit, and DOTAX may require the taxpayer to furnish information to validate a claim for the credit, and may adopt rules necessary to effectuate the purpose of the law pursuant to chapter 91.

EFFECTIVE DATE: Applies to taxable years beginning after December 31, 2021.

STAFF COMMENTS: Act 202, SLH 2016, enacted a renewable energy credit with a five-year life. The credit sunset on December 31, 2021. This bill revives the credit with some modifications. First, the bill requires an annual production of 2.5 billion BTU of renewable energy per year, while Act 202 required an annual production of 15 billion BTU. Next, the bill explicitly allows logs, wood chips, wood pellets, or wood bark to qualify as renewable fuels.

While the idea of providing a tax credit to encourage such activities may have been acceptable a few years ago when the economy was on a roll and advocates could point to credits like those to encourage construction and renovation activities, what lawmakers and administrators have learned in these past few years is that unbridled tax incentives, where there is no accountability or limits on how much in credits can be claimed, are irresponsible as the cost of these credits goes far beyond what was ever intended. Instead, lawmakers should encourage alternative energy production through the appropriation of a specific number of taxpayer dollars. The State could directly purchase energy or it could give a subsidy to developers. Then, lawmakers would have a better idea of what is being funded and hold the developers of these alternate forms of energy to a deliberate timetable or else lose the funds altogether. A direct appropriation would be preferable to the tax credit as it would: (1) provide some accountability for the taxpayers' funds being utilized to support this effort; and (2) not be a blank check.

Digested: 1/28/2022

LATE *Testimony submitted late may not be considered by the Committee for decision making purposes.

PACIFIC BIODIESEL TECHNOLOGIES

40 Hobron Avenue
Kahului, Hawaii 96732
(808) 877-3144
www.biodiesel.com

Hearing at 10:00am February 2, 2022

LATE

IN SUPPORT OF HB2002

Committee on Economic Development

Chair Quinlan and Committee:

Pacific Biodiesel is in support of HB2002 with modifications. This production tax credit gives a small but very important incentive to invest further in renewable fuel production in Hawaii. We request the time be increased to 10 years, and the aggregate cap be increased to $6,000,000 per year. We are not opposed to deleting item (G) on the definition of renewable fuels to more closely mirror HB1809.

Speaking for the liquid biofuels industry, it is well known that the cost to move from 70% to 100% renewables will be extremely expensive using any other technology. Biodiesel can cost effectively optimize battery sizing by providing firm renewable power, quickly dispatched at any time. Fast-start clean diesel engines – when fueled with clean, locally made biodiesel - are enabling higher penetration of intermittent PV and wind assets while maintaining grid stability. Biodiesel is a 100% renewable advanced biofuel and is a crucially important "firm power" source to back up other renewables on the grid. The further we move towards our goal of 100% renewable, the more critical these liquid biofuel sources will be. Yet building up the supply is a long process. We must accelerate implementation now to meet the needs later.

The first five years of this production tax credit was successful. Pacific Biodiesel now generates over $40MM per year in revenue, with 80+ employees in Hawaii. The cost to the State was minimal relative to the benefit. Continuing this credit sends the correct signal for new investments in this area.

Mahalo,

Robert O. King

Robert King, President
Pacific Biodiesel Technologies, LLC