

ACT 178

S.B. NO. 1583

A Bill for an Act Relating to Technology.

*Be It Enacted by the Legislature of the State of Hawaii:*

PART I

SECTION 1. The legislature finds that Hawaii is one of the most geographically isolated communities on earth, and for many years, our economic opportunities were limited by this isolation. Recent advances in telecommunications, information technology, and the explosive growth of the Internet, however, present significant new opportunities for the State to develop and diversify its economy, opening the global market to Hawaii businesses.

Fiber optic cables, connecting Hawaii with the mainland United States and Asia, and new communications satellites have dramatically increased both the volume of information sent and the range of transmittal. While transmission capacity increases, costs continue to fall. Today, Internet commerce represents a small fraction of all business transacted, but industry watchers estimate that within the next seven years, half of all business and consumer purchases will be done by computer. In this new era, connection is everything.

The legislature further finds that Hawaii's opportunities also represent new challenges. Businesses—particularly the small, start-ups associated with high technology—no longer need to factor in Hawaii's geographic isolation, but must still consider the cost of doing business in the State. They also face a confusing, often overlapping, group of state agencies that provide support for technology-related business. Providing targeted assistance to these businesses, as well as a clear focus of responsibility within state government for aggressive development and support of high technology resources, will better serve the burgeoning technology industry.

The legislature also finds that education will be forever changed as businesses and workers alike demand new skills and rapid-response delivery of these skills. Our schools must move beyond the traditional book and classroom delivery and embrace a technologically-connected model for learning. In 1998, the legislature appropriated funds to provide high-speed Internet access to the University of Hawaii and all state agencies, including schools. As a result, establishing schools and libraries as community access points can be accelerated.

If Hawaii is to become a state known for leading its people effectively into the twenty-first century, the legislature believes progress and change must begin immediately. The purpose of this Act is to support the growth and development of high technology industries in Hawaii by:

- (1) Consolidating the State's high technology agencies, divisions, and offices under the coordination and direction of a special advisor for technology development and creating a governor's special advisory council for technology development to assist the advisor;
- (2) Integrating technology with Hawaii's tourism and marketing industries;
- (3) Prohibiting the imposition of discriminatory taxes on Internet commerce;
- (4) Focusing work force development programs to ensure a pool of technology professionals;
- (5) Accelerating high speed access to the Internet for the University of Hawaii and the public schools, and establishing educational technology programs within public schools;
- (6) Exempting stock options from qualified high technology businesses from income taxation;
- (7) Exempting royalties from qualified high technology businesses and other similar sources from gross income for income tax purposes; and
- (8) Creating tax credits for investment in high technology businesses and increasing research activities.

## PART II

**SECTION 2.** Over the years, the legislature has created a number of state agencies charged with promoting the development of a variety of technological industries. While these agencies provide valuable services, they lack focus, and in some cases, their original missions have changed considerably. Consolidation of these agencies under a single entity to coordinate their activities will provide a more focused effort in attracting high technology businesses to Hawaii.

**SECTION 3.** The Hawaii Revised Statutes is amended by adding two new sections to be appropriately designated and to read as follows:

**"§ - Special advisor for technology development.** (a) There is established within the office of the governor a special advisor for technology development to be appointed by the governor as provided in section 26-34.

(b) The duties of the special advisor shall include but not be limited to:

- (1) Developing, coordinating, and implementing short- and long-range state policies and directions to enhance the development of high technology industries in Hawaii;
- (2) Coordinating all state high technology agencies while developing a plan for reorganization or consolidation of these agencies in the interests of greater efficiency and cost effectiveness;

- (3) Advising the private sector in the development of high technology activities and resources and providing technical or other assistance to private industry upon request;
- (4) Creating, disseminating, and updating a listing of all high technology assistance programs in the State and where they can be reached;
- (5) Pursuing appropriate public-private sector business partnerships;
- (6) Coordinating the State's promotion and marketing of the high technology industry, including a review of current marketing efforts;
- (7) Arranging for the conduct of research through contractual services with the University of Hawaii or any agency or other qualified persons;
- (8) Encouraging the development of educational, training, and career programs in high technology industries; and
- (9) Performing other necessary or desirable functions to facilitate the intent of this section.

(c) In carrying out the duties of this section, the special advisor for technology development may utilize the services of the State's high technology agencies, including those of the University of Hawaii, as appropriate.

(d) In carrying out the duties of this section, the special advisor for technology development shall seek and utilize any available funding sources, including grant moneys.

**§ - Governor's special advisory council for technology development; establishment; appointment, number, and term of members; duties.** (a) There is established within the office of the governor, for administrative purposes, an advisory council to be known as the governor's special advisory council for technology development, that shall review and make recommendations on matters relating to the marketing and promotion of Hawaii as a location for high technology companies. The council shall be composed of at least eleven but no more than twenty-five members appointed in accordance with section 26-34, and shall include representatives of the high technology industry, business leaders, educators, government leaders, and legislators.

(b) The members shall be appointed by the governor for four years, except that the terms of the members first appointed shall be for two and four years, respectively, as designated by the governor at the time of appointment. The council shall elect a chairperson from among its members.

(c) In appointing members, the governor shall select persons who have knowledge of the high technology industry, the educational needs of the industry, or in the marketing and promotion of high technology industries. The members of the council shall serve without compensation but shall be reimbursed for expenses, including travel expenses, necessary for the performance of their duties.

(d) The council shall assist the special advisor for technology development in developing and coordinating the marketing and promotion of the high technology industry in Hawaii.

(e) In carrying out the duties of this section, the council shall seek and utilize any available funding sources, including grant moneys.

(e)<sup>1</sup> This section is repealed on December 31, 2005."

**SECTION 4.** There is appropriated out of the general revenues of the State of Hawaii the sum of \$100,000, or so much thereof as may be necessary for fiscal year 1999-2000, and the same sum, or so much thereof as may be necessary for fiscal year 2000-2001, for the special advisor for technology development and the governor's special advisory council for technology development. The sums appropriated shall be expended by the office of the governor for the purposes of section 3.

## PART III

SECTION 5. The purpose of this Part is to foster the development of knowledge-based industries by integrating those industries with Hawaii's economy in a way that enhances and strengthens the tourism industry.

SECTION 6. Section 201-97, Hawaii Revised Statutes, is amended to read as follows:

**“[[§201-97]] Integration and development of the tourism industry.** The office shall be responsible for planning for the integrated and coordinated development and expansion of the tourism industry of the State. The office shall investigate and recommend to appropriate governmental officers, agencies, legislative committees, and private groups ways and means of coordinating promotional activities on behalf of tourism with the development of recreational and other facilities, and with existing and potential information and communications technology networks and services in the State, for improved tourism development. The office shall also review the expenditure of governmental funds for tourism-related activities and shall prepare an annual report on the expenditures, together with any recommendations the office may have. The annual report shall be submitted to the legislature as part of the annual report required under section 201-98.”

SECTION 7. Section 201B-6, Hawaii Revised Statutes, is amended by amending subsection (a) to read as follows:

“(a) The authority shall be responsible for developing a strategic tourism marketing plan [which] that shall be updated every three years[, that] and includes the following:

- (1) Identification and evaluation of current and future tourism needs for the different regions of the State;
- (2) Goals and objectives in accordance with identified needs;
- (3) Statewide promotional efforts and programs;
- (4) Targeted markets;
- (5) Efforts to enter into brand marketing projects that make effective use of cooperative advertising programs;
- (6) Measures of effectiveness for the authority's promotional programs; and
- (7) Coordination of marketing plans of all destination marketing organizations receiving state funding prior to finalization of the authority's marketing plan.

The authority shall also develop and include in its marketing plan, goals and objectives for marketing the State to the techno-tourism niche as well as for integrating marketing objectives with existing and potential state telecommunications and information resources in the public and private sectors. The authority shall also coordinate the requirements for and availability of the State's existing and potential telecommunications and information resources with the department of accounting and general services.”

## PART IV

SECTION 8. Economic development opportunities are changing. The playing field is now the world and not the next state or country. The Internet is the catalyst, and the enabling infrastructure is technology and telecommunications. The legislature finds that exempting Internet commerce from state taxation will be a key element that allows Hawaii's businesses to establish a global presence.

SECTION 9. Chapter 231, Hawaii Revised Statutes, is amended by adding a new section to be appropriately designated and to read as follows:

**“§231- Hawaii Internet Tax Freedom Act.** (a) No discriminatory tax shall be imposed under chapter 235 (relating to income tax), chapter 237 (relating to the general excise tax), or chapter 238 (relating to the use tax) on electronic commerce or Internet access.

(b) As used in this section “discriminatory tax” means:

- (1) Any tax imposed by the State or county on electronic commerce that:
  - (A) Is not generally imposed and legally collectible by the State or county on transactions involving similar property, goods, services, or information accomplished through other means;
  - (B) Is not generally imposed and legally collectible at the same rate by such State or county on transactions involving similar property, goods, services, or information accomplished through other means;
  - (C) Imposes an obligation to collect or pay the tax on a different person or entity than in the case of transactions involving similar property, goods, services, or information accomplished through other means;
  - (D) Establishes a classification of Internet access service providers or online service providers for purposes of establishing a higher tax rate to be imposed on those providers than the tax rate generally applied to providers of similar information services delivered through other means; or
- (2) Any tax imposed by the State or county if:
  - (A) The sole ability to access a site on a remote seller’s out-of-State computer server is considered a factor in determining a remote seller’s tax collection obligation; or
  - (B) A provider of Internet access service or online services is deemed to be the agent of a remote seller for determining tax collection obligations solely as a result of:
    - (i) The display of a remote seller’s information or content on the out-of-State computer server or a provider of Internet access service or online services; or
    - (ii) The processing of orders through the out-of-State computer server of a provider of Internet access service or online services.

(c) As used in this section:

“Electronic commerce” means any transaction conducted over the Internet or through Internet access, comprising the sale, lease, license, offer, or delivery of property, goods, services, or information, whether or not for consideration, and includes the provision of Internet access.

“Internet” means collectively the myriad of computer and telecommunications facilities, including equipment and operating software that comprise the interconnected world-wide network of networks that employ the Transmission Control Protocol/Internet Protocol, or any predecessor or successor protocols to that protocol, to communicate information of all kinds by wire or radio.

“Internet access” means a service or license that enables users to access content, information, electronic mail, or other services or licenses offered over the Internet, and may also include access to proprietary content, information, and other services or licenses as part of a package of services or licenses offered to users. The term does not include telecommunications service as defined in section 269-1.

(d) This section shall not apply to taxable years beginning after December 31, 2005.”

SECTION 10. Notwithstanding section 304-7.8, Hawaii Revised Statutes, or any other law to the contrary, the University of Hawaii office of technology transfer and economic development may expend amounts up to \$4,000,000 from the discoveries and inventions revolving fund in section 304-8.92, Hawaii Revised Statutes, for the purposes of that fund in fiscal year 1999-2000.

## PART V

SECTION 11. The legislature finds that a training program to improve the skills of new and existing workers for jobs in new and emerging industries would help stimulate the State’s economy. Industries such as biotechnology, health care, information technology, environmental science and technology, and telecommunications must often import their workers because the State’s existing workforce lacks necessary skills. A state-funded training program would lessen the need to import workers and increase the opportunities for Hawaii’s residents to move upward in the job market by improving their skills.

SECTION 12. The Hawaii Revised Statutes is amended by adding a new section to be appropriately designated and to read as follows:

“§ - **Millennium workforce development training program.** (a) There is established a millennium workforce development training program, herein-after referred to as the program, that shall be placed with the department of labor and industrial relations for administrative purposes. The program shall provide education and training at the post-high-school to graduate levels, and shall include public, private, and for-profit educational institutions. In the design and delivery of training, the program may cooperate or contract with other public, private, and for-profit institutions.

(b) The program shall seek and encourage partnerships with private sector industries such as biotechnology, information technology, environmental science and technology, and telecommunications, as may be appropriate, to provide pre-employment or employment training, or on-the-job training for employees and perspective employees.

(c) The department of labor and industrial relations shall establish and lead a public and private partnership task group, that shall include representatives from the department of business, economic development, and tourism, the University of Hawaii at Manoa, the University of Hawaii community colleges, and private sector representatives to advise on the program design, industry, recruitment, and training delivery activities of participating entities.

(d) In carrying out the duties of this section, the department of labor and industrial relations and the University of Hawaii shall seek and utilize any available funding sources, including grant moneys.”

SECTION 13. There is appropriated out of the general revenues of the State of Hawaii the sum of \$50,000, or so much thereof as may be necessary for fiscal year 1999-2000, and the same sum, or so much thereof as may be necessary for fiscal year 2000-2001, to provide funds to the department of labor and industrial relations to establish a millennium workforce development program. The sums appropriated shall be expended by the department of labor and industrial relations for the purposes of this Part.

SECTION 14. There is appropriated out of the general revenues of the State of Hawaii the sum of \$436,200, or so much thereof as may be necessary for fiscal year 1999-2000, and the same sum, or so much thereof as may be necessary for fiscal year 2000-2001, to provide funds to the University of Hawaii to implement programs pursuant to the millennium workforce development program. The sums appropriated shall be expended by the University of Hawaii for the purposes of this Part.

## PART VI

SECTION 15. The legislature finds that students must be afforded opportunities in new educational technologies, such as the E Academy concept, that will provide relevant, challenging, and meaningful course offerings for students interested in pursuing a career in advanced technology fields. The purpose of this Part is to provide Hawaii's students with meaningful and relevant preparation for immediate opportunities in entry level technology positions and advanced studies in post secondary information technology, science, engineering, and math.

SECTION 16. Chapter 302A, Hawaii Revised Statutes, is amended by adding a new section to be appropriately designated and to read as follows:

**“§302A- E-mail accounts for students.** (a) The department of education, in conjunction and coordination with the University of Hawaii, shall provide e-mail accounts at no charge to any student who applies to the department for such an account.

(b) As used in this section, the term “student” means any person attending public school in ninth grade or above, including:

- (1) Both degree and nondegree candidates;
- (2) Individuals attending school on a full-time, part-time, or occasional basis, including continuing education or other nondegree courses;
- (3) Individuals in educational, technical, or vocational programs; and
- (4) Individuals attending public undergraduate or postgraduate college and university programs.

(c) The department of education, in cooperation with the University of Hawaii, shall adopt rules pursuant to chapter 91 as may be necessary to implement this section.”

SECTION 17. (a) The department of education shall establish E Academies throughout the State with onsite locations based at selected public high schools in each departmental school district. The department of education shall also develop new challenging high school course offerings in math, science, and technology content areas and include the new courses in the authorized course code and number guide, for the purposes of the E Academies. The department of education shall provide an innovative training program for E Academy teachers, and conduct instructional assessment activities beginning in the 1999-2000 school year. In carrying out the duties of this section, the department of education shall seek and utilize any available funding sources, including grant moneys.

(b) As used in this section, “E Academy” means a virtual, site-based school that provides students with industry and academic standards-based instruction and assessments in technology, science, math, and engineering.

SECTION 18. Section 226-107, Hawaii Revised Statutes, is amended to read as follows:

tion: **“§226-107 Quality education.** Priority guidelines to promote quality educa-

- (1) Pursue effective programs which reflect the varied district, school, and student needs to strengthen basic skills achievement[.];
- (2) Continue emphasis on general education “core” requirements to provide common background to students and essential support to other university programs[.];
- (3) Initiate efforts to improve the quality of education by improving the capabilities of the education work force[.];
- (4) Promote increased opportunities for greater autonomy and flexibility of educational institutions in their decisionmaking responsibilities[.];
- (5) Increase and improve the use of information technology in education [and encourage] by the availability of telecommunications equipment for:
  - (A) The electronic exchange of information;
  - (B) Statewide electronic mail; and
  - (C) Access to the Internet.Encourage programs [which] that increase the public’s awareness and understanding of the impact of information technologies on our lives[.];
- (6) Pursue the establishment of Hawaii’s public and private universities and colleges as research and training centers of the Pacific[.];
- (7) Develop resources and programs for early childhood education[.];
- (8) Explore alternatives for funding and delivery of educational services to improve the overall quality of education[.]; and
- (9) Strengthen and expand educational programs and services for students with special needs.”

SECTION 19. There is appropriated out of the general revenues of the State of Hawaii the sum of \$163,800, or so much thereof as may be necessary for fiscal year 1999-2000, and the same sum, or so much thereof as may be necessary for fiscal year 2000-2001, to provide funds for the establishment of E Academies statewide at selected schools in each of the departmental school districts. The sums appropriated shall be expended by the department of education for the purposes of section 17.

## PART VII

SECTION 20. Chapter 235, Hawaii Revised Statutes, is amended by adding a new section to be appropriately designated and to read as follows:

**“§235-A Stock options from qualified high technology businesses exempt from taxation.** (a) Notwithstanding any law to the contrary, all income received from stock options from a qualified high technology business by an employee that would otherwise be taxed as ordinary income or as capital gains to those employees is exempt from taxation under this chapter.

(b) For the purposes of this section:

“Computer software” means a set of computer programs, procedures, or associated documentation concerned with the operation and function of a computer system, and includes both systems and application programs and subdivisions, such as assemblers, compilers, routines, generators, and utility programs.

“Qualified high technology business” means a business performing qualified research. The term “qualified high technology business” does not include:

- (1) Any trade or business involving the performance of services in the field of law, architecture, accounting, actuarial science, performing arts, consulting, athletics, financial services, or brokerage services;



- (2) Any banking, insurance, financing, leasing, rental, investing, or similar business; any farming business, including the business of raising or harvesting trees; any business involving the production or extraction of products of a character with respect to which a deduction is allowable under section 611 (with respect to allowance of deduction for depletion), 613 (with respect to basis for percentage depletion), or 613A (with respect to limitation on percentage depleting in cases of oil and gas wells) of the Internal Revenue Code;
- (3) Any business operating a hotel, motel, restaurant, or similar business; and
- (4) Any trade or business involving a hospital, a private office of a licensed health care professional, a group practice of licensed health care professionals, or a nursing home.

“Qualified research” means:

- (1) The same as in section 41(d) of the Internal Revenue Code; or
- (2) Developing, designing, modifying, programming, and licensing computer software.”

## PART VIII

SECTION 21. The legislature finds that there is a need to encourage the creative community in Hawaii in order to support Hawaii’s growth in the high technology business sector. The legislature further finds that exempting both individuals and high technology businesses from taxes on royalties received from copyrights and patents will help to encourage this creative community, which in turn will help produce its own synergy to foster electronic commerce in Hawaii. The purpose of this part is therefore to exempt individuals and qualified high technology businesses in Hawaii from taxation on royalties owned by those individuals or businesses and developed or arising out of those businesses.

SECTION 22. Chapter 235, Hawaii Revised Statutes, is amended by adding a new section to be appropriately designated and to read as follows:

**“§235-B Royalties and other income from high technology business excluded from gross income.** (a) In addition to the exclusions in section 235-7, there shall be excluded from gross income, adjusted gross income, and taxable income, amounts received by an individual or a qualified high technology business as royalties and other income derived from patents and copyrights:

- (1) Owned by the individual or qualified high technology business; and
- (2) Developed and arising out of a qualified high technology business.

(b) For the purposes of this section:

“Computer software” means a set of computer programs, procedures, or associated documentation concerned with the operation and function of a computer system, and includes both systems and application programs and subdivisions, such as assemblers, compilers, routines, generators, and utility programs.

“Qualified high technology business” means a business performing qualified research. The term “qualified high technology business” does not include:

- (1) Any trade or business involving the performance of services in the field of law, architecture, accounting, actuarial science, performing arts, consulting, athletics, financial services, or brokerage services;
- (2) Any banking, insurance, financing, leasing, rental, investing, or similar business; any farming business, including the business of raising or harvesting trees; any business involving the production or extraction of products of a character with respect to which a deduction is allowable

under section 611 (with respect to allowance of deduction for depletion), 613 (with respect to basis for percentage depletion), or 613A (with respect to limitation on percentage depleting in cases of oil and gas wells) of the Internal Revenue Code;

- (3) Any business operating a hotel, motel, restaurant, or similar business; and
- (4) Any trade or business involving a hospital, a private office of a licensed health care professional, a group practice of licensed health care professionals, or a nursing home.

“Qualified research” means:

- (1) The same as in section 41(d) of the Internal Revenue Code; or
- (2) Developing, designing, modifying, programming, and licensing computer software.”

## PART IX

SECTION 23. While the advantages of Hawaii’s proximity to Pacific and Asian markets are a lure for technology business in Hawaii, the costs of doing business are high. The purpose of this Part is to assist in the creation of opportunities for high technology companies through the creation of tax credits for investing in high technology businesses and for increasing research activities.

SECTION 24. Chapter 235, Hawaii Revised Statutes, is amended by adding to part VI a new section to be appropriately designated and to read as follows:

**“§235-C High-technology business investment tax credit.** (a) There shall be allowed to each taxpayer, subject to the taxes imposed by this chapter, a high technology investment tax credit that 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. The tax credit shall be an amount equal to ten per cent of the investment made by the taxpayer in each qualified high technology business, up to a maximum allowed credit of \$500,000 for the taxable year for the investment made by the taxpayer in a qualified high technology business.

(b) The credit allowed under this section shall be claimed against the net income tax liability for the taxable year. For the purpose of this section, “net income tax liability” means net income tax liability reduced by all other credits allowed under this chapter.

(c) If the tax credit under this section exceeds the taxpayer’s income tax liability, the excess of the tax credit over liability may be used as a credit against the taxpayer’s income tax liability in subsequent years until exhausted. All claims, including any amended claims, for tax credits 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) As used in this section:

“Computer software” means a set of computer programs, procedures, or associated documentation concerned with the operation and function of a computer system, and includes both systems and application programs and subdivisions, such as assemblers, compilers, routines, generators, and utility programs.

“Investment” means a nonrefundable investment, at risk, as that term is used in section 465 (with respect to deductions limited to amount at risk) of the Internal Revenue Code, in a qualified high technology business, of cash that is transferred to the qualified high technology business, the transfer of which is in connection with a transaction in exchange for stock, interests in partnerships, joint

ventures, or other entities, licenses (exclusive or nonexclusive), rights to use technology, marketing rights, warrants, options, or any items similar to those included herein, including but not limited to options or rights to acquire any of the items included herein. The nonrefundable investment is entirely at risk of loss where repayment depends upon the success of the qualified high technology business. If the money invested is to be repaid to the taxpayer, no repayment except for dividends or interest shall be made for at least three years from the date the investment is made. The annual amount of any dividend and interest payment to the taxpayer shall not exceed twelve per cent of the amount of the investment.

(b)<sup>1</sup> For the purposes of this section:

“Qualified high technology business” means:

- (1) A business, employing or owning capital or property, or maintaining an office, in this State; and which
- (2) (A) Conducts one hundred per cent of its activities in performing qualified research in this State; or  
(B) Receives one hundred per cent of its gross income derived from qualified research; provided that the income is received from products sold from, manufactured, or produced in the State; or services performed in this State.

The term “qualified high technology business” does not include:

- (1) Any trade or business involving the performance of services in the field of law, architecture, accounting, actuarial science, performing arts, consulting, athletics, financial services, or brokerage services;
- (2) Any banking, insurance, financing, leasing, rental, investing, or similar business; any farming business, including the business of raising or harvesting trees; any business involving the production or extraction of products of a character with respect to which a deduction is allowable under section 611 (with respect to allowance of deduction for depletion), 613 (with respect to basis for percentage depletion), or 613A (with respect to limitation on percentage depleting in cases of oil and gas wells) of the Internal Revenue Code;
- (3) Any business operating a hotel, motel, restaurant, or similar business; and
- (4) Any trade or business involving a hospital, a private office of a licensed health care professional, a group practice of licensed health care professionals, or a nursing home.

“Qualified research” means:

- (1) The same as in section 41(d) of the Internal Revenue Code; or
- (2) Developing, designing, modifying, programming, and licensing computer software;

except that it shall not include research conducted outside the State.

(e)<sup>1</sup> This section shall not apply to taxable years beginning after December 31, 2005.”

SECTION 25. Chapter 235, Hawaii Revised Statutes, is amended by adding to part VI a new section to be appropriately designated and to read as follows:

“**§235-D Tax credit for increasing research activities.** (a) Section 41 (with respect to the credit for increasing research activities) and section 280C(c) (with respect to certain expenses for which the credit for increasing research activities are allowable) of the Internal Revenue Code shall be operative for the purposes of this chapter as provided in this section.

(b) All references to Internal Revenue Code sections within sections 41 and 280C(c) of the Internal Revenue Code shall be operative for purposes of this section.

(c) There shall be allowed to each taxpayer, subject to the tax imposed by this chapter, an income tax credit for increased research activities that 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.

(d) The tax credit for increased research activities shall be equal to the sum of:

- (1) 2.5 per cent of the excess (if any) of:
  - (A) The qualified research expenses for the taxable year; over
  - (B) The base amount;
 and
- (2) 2.5 per cent of the basic research payments determined under section 41(e)(1)(A) of the Internal Revenue Code.

(e) For purposes of this section:

- (1) The alternative incremental credit in section 41(c)(4) of the Internal Revenue Code shall be equal to the sum of 12.5 per cent of:
  - (A) 1.65 per cent of so much of the qualified research expenses for the taxable year as exceeds one per cent of the average described in section 41(c)(1)(B) but does not exceed 1.5 per cent of such average;
  - (B) 2.2 per cent of so much of those expenses as exceeds 1.5 per cent of the average but does not exceed two per cent of the average; and
  - (C) 2.75 per cent of so much of those expenses as exceeds two per cent of the average;
- (2) The term "qualified research" under section 41(d)(1) of the Internal Revenue Code shall not include research conducted outside of the State; and
- (3) The term "basic research" under section 41(e) of the Internal Revenue Code shall not include research conducted outside of the State.

(f) The amount of reduced credit in section 280C(c)(3)(B) of the Internal Revenue Code shall be equal to the excess of:

- (1) The amount of credit determined under section 41(a) (as provided for in this section) (without regard to this paragraph); over
- (2) The product of:
  - (A) The amount described in subsection (f)(1); and
  - (B) 12.5 per cent of the maximum rate of tax under section 11(b)(1) of the Internal Revenue Code.

(g) If the tax credit for increased research activities claimed by a taxpayer exceeds the amount of income tax payment due from the taxpayer, the excess of the tax credit over payments due may be used as a credit against the taxpayer's income tax liability in subsequent years until exhausted.

(h) All claims for a tax credit under this section must 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 properly claim the credit shall constitute a waiver of the right to claim the credit.

(i) The director of taxation may adopt any rules under chapter 91 and forms necessary to carry out this section.

(j) This section shall not apply to taxable years beginning after December 31, 2005."

SECTION 26. Chapter 241, Hawaii Revised Statutes, is amended by adding a new section to be appropriately designated and to read as follows:

**“§241- High-technology business investment tax credit.** The high-technology business investment tax credit provided under section 235-C shall be operative for this chapter on the effective date of this Act.”

SECTION 27. Chapter 431, article 7, part II, Hawaii Revised Statutes, is amended by adding a new section to be appropriately designated and to read as follows:

**“§431:7- High-technology business investment tax credit.** The high-technology business investment tax credit provided under section 235-C shall be operative for this chapter on the effective date of this Act.”

SECTION 28. Section 235-2.3, Hawaii Revised Statutes, is amended by amending subsection (b) to read as follows:

“(b) The following Internal Revenue Code subchapters, parts of subchapters, sections, subsections, and parts of subsections shall not be operative for the purposes of this chapter, unless otherwise provided:

- (1) Subchapter A (sections 1 to 59A) (with respect to determination of tax liability), except section 1(h)(3) (relating to net capital gain reduced by the amount taken into account as investment income), except section 41 (with respect to the credit for increasing research activities), except section 42 (with respect to low-income housing credit), and except sections 47 and 48, as amended, as of December 31, 1984 (with respect to certain depreciable tangible personal property). For treatment, see sections 235-D, 235-110.7, and 235-110.8;
- (2) Section 78 (with respect to dividends received from certain foreign corporations by domestic corporations choosing foreign tax credit);
- (3) Section 86 (with respect to social security and tier 1 railroad retirement benefits);
- (4) Section 103 (with respect to interest on state and local bonds). For treatment, see section 235-7(b);
- (5) Section 120 (with respect to amounts received under qualified group legal services plans). For treatment, see section 235-7(a)(9) to (11);
- (6) Section 122 (with respect to certain reduced uniformed services retirement pay). For treatment, see section 235-7(a)(3);
- (7) Section 135 (with respect to income from United States savings bonds used to pay higher education tuition and fees). For treatment, see section 235-7(a)(1);
- (8) Subchapter B (sections 141 to 150) (with respect to tax exemption requirements for state and local bonds);
- (9) Section 151 (with respect to allowance of deductions for personal exemptions). For treatment, see section 235-54;
- (10) Section 196 (with respect to deduction for certain unused investment credits);
- (11) Sections 241 to 247 (with respect to special deductions for corporations). For treatment, see section 235-7(c);
- (12) Section 280C (with respect to certain expenses for which credits are allowable)[;]. For treatment see, section 235-D;
- (13) Section 291 (with respect to special rules relating to corporate preference items);
- (14) Section 367 (with respect to foreign corporations);
- (15) Section 501(c)(12), (15), (16) (with respect to exempt organizations);
- (16) Section 515 (with respect to taxes of foreign countries and possessions of the United States);

- (17) Subchapter G (sections 531 to 565) (with respect to corporations used to avoid income tax on shareholders);
- (18) Subchapter H (sections 581 to 597) (with respect to banking institutions), except section 584 (with respect to common trust funds). For treatment, see chapter 241;
- (19) Section 642(a) and (b) (with respect to special rules for credits and deductions applicable to trusts). For treatment, see sections 235-54(b) and 235-55;
- (20) Section 668 (with respect to interest charge on accumulation distributions from foreign trusts);
- (21) Subchapter L (sections 801 to 848) (with respect to insurance companies). For treatment, see sections 431:7-202 and 431:7-204;
- (22) Section 853 (with respect to foreign tax credit allowed to shareholders). For treatment, see section 235-55;
- (23) Subchapter N (sections 861 to 999) (with respect to tax based on income from sources within or without the United States), except sections 985 to 989 (with respect to foreign currency transactions). For treatment, see sections 235-4, 235-5, and 235-7(b), and 235-55;
- (24) Section 1042(g) (with respect to sales of stock in agricultural refiners and processors to eligible farm cooperatives);
- (25) Section 1055 (with respect to redeemable ground rents);
- (26) Section 1057 (with respect to election to treat transfer to foreign trust, etc., as taxable exchange);
- (27) Sections 1291 to 1298 (with respect to treatment of passive foreign investment companies);
- (28) Subchapter Q (sections 1311 to 1351) (with respect to readjustment of tax between years and special limitations); and
- (29) Subchapter U (sections 1391 to 1397F) (with respect to designation and treatment of empowerment zones, enterprise communities, and rural development investment areas). For treatment, see chapter 209E."

## PART X

SECTION 29. In codifying the new sections added by this Act, the revisor of statutes shall substitute the appropriate section numbers for the letters used in designating the new sections in this Act.

SECTION 30. Statutory material to be repealed is bracketed. New statutory material is underscored.<sup>2</sup>

SECTION 31. This Act shall take effect upon its approval; provided that:

- (1) Sections 4, 10, 13, 14, and 19 of this Act shall take effect on July 1, 1999;
- (2) Sections 9, 20, 22, 25, and 28 of this Act shall apply to taxable years beginning after December 31, 1999; and
- (3) Section 24 of this Act shall apply to taxable years beginning after December 31, 1998, for investments made pursuant to section 235-C, Hawaii Revised Statutes, on or after the effective date of this Act.

(Approved July 1, 1999.)

### Notes

1. So in original.

2. Edited pursuant to HRS §23G-16.5.