HOUSE OF REPRESENTATIVES
TWENTY-FIFTH LEGISLATURE, 2010
STATE OF HAWAII

H.B. NO. 2436

A BILL FOR AN ACT

RELATING TO BIOFUEL FACILITIES.

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

SECTION 1. In 2008, Hawaii imported 41.5 million barrels of crude oil at a cost and loss to the State's economy of approximately $4.1 billion. Unfortunately, well intended discussions and plans over many years have not been fruitful, and the outflow of Hawaii's scarce dollars for off-shore fuel purchases continues unabated. It is time for meaningful action that can result in significant, near-term commercial production of biomass-based fuels in Hawaii.

Given Hawaii's growing energy and economic security needs, it is imperative that Hawaii begin in earnest to generate its own fuel from local feedstock production and biofuel conversion. Hawaii's climate and rich natural resources provide a solid foundation upon which this local industry can be built and successfully sustained. Advanced and second generation feedstocks, including sugarcane, sweet sorghum, and algae, hold tremendous potential to displace fossil fuel imports given their relatively low input requirements, exceptionally high yields, and potential to produce a portfolio of products, including liquid fuels, renewable power, feed, and other bio-based co-products, through various bioconversion pathways.

Notwithstanding its great potential to reduce fossil fuel imports and stimulate the local economy, bio-based fuel production in Hawaii can only be realized through near-term initial investments in feedstock production and bioconversion facilities. While the existing ethanol facility credit under section 235-110.3, Hawaii Revised Statutes, was created to provide such support, its current scope limits the State's ability to diversify its fuel mix and displace other imported fossil fuels upon which Hawaii is critically dependent, including, but not limited to, diesel and aviation fuel. For example, in 2008 alone, Hawaii consumed over 208.4 million gallons of highway and off-highway diesel at an average cost per gallon of $4.63, resulting in an approximate outflow of $965 million dollars based on statistics from the department of business, economic development, and tourism. The State consumed an additional 195 million gallons of aviation fuel at an average of $3.08 per gallon, for another $600.6 million in estimated outflows over the same period. Expanding production of bio-based fuel capable of displacing both gasoline and diesel fuels is imperative if Hawaii is to increase its energy security and meet its stated renewable energy targets.

Hawaii's ability to secure the substantial capital required for large-scale commercial facilities requires providing a degree of assurance to private investors (banks, organizations, and individuals) that they will be able to recover their investment within a reasonable time horizon. Extending the current ethanol facility tax credit to incorporate biofuels more broadly would help to attract a broader set of investors and provide additional financial support needed to stimulate and diversify Hawaii's renewable energy base.

Senate Concurrent Resolution No. 132, S.D. 1 (2009), established a task force to determine the economic contributions of the construction industry in Hawaii. As directed in the concurrent resolution, the task force has developed a series of proposals for state actions to preserve and create new jobs in the local construction industry. The intent of this Act is to implement one of the task force's proposals.

This Act provides tax credit incentives designed to attract needed renewable fuel investment to the State, minimize capital investment requirements of production facilities, and retain billions of dollars in the State's economy. The incentive program would be self-sustaining, as the additional business and income tax revenue generated by the industry would be applied to future tax credits. As such, this Act directly ties the incentives to the local market, enables the removal of the current 40 million gallon production cap, and provides support to a range of advanced and more efficient production technologies.

The purpose of this Act is to enhance Hawaii's economic vitality through renewable energy resources that are self-sufficient, affordable, and produced locally.

SECTION 2. Section 235-110.3, Hawaii Revised Statutes, is amended to read as follows:

"**§235-110.3 [~~Ethanol~~] Biofuel facility tax credit.** (a) Each year during the credit period, there shall be allowed to each taxpayer subject to the taxes imposed by this chapter, [~~an ethanol~~] a biofuel facility tax credit that shall be applied to the taxpayer's net income tax liability, if any, imposed by this chapter for the taxable year in which the credit is properly claimed.

For each [~~qualified ethanol~~] qualifying biofuel production facility, the annual dollar amount of the [~~ethanol~~] biofuel facility tax credit during the eight-year period shall be equal to thirty per cent of its nameplate capacity [~~if the nameplate capacity is greater than five hundred thousand but less than~~] up to the first fifteen million gallons of production[~~.~~] of production. A taxpayer may claim this credit for each qualifying [~~ethanol~~] biofuel production facility; provided that:

(1) The claim for this credit by any taxpayer of a qualifying [~~ethanol~~] biofuel production facility shall not exceed one hundred per cent of the total of all investments made by the taxpayer in the qualifying [~~ethanol~~] biofuel production facility during construction of the facility and the credit period;

(2) The qualifying [~~ethanol~~] biofuel production facility operated at a level of production of at least seventy-five per cent of its nameplate capacity on an annualized basis;

(3) The qualifying biofuel production facility shall be located within the State and use locally grown feedstock for at least seventy-five per cent of its production output;

[~~(3)~~] (4) The qualifying [~~ethanol~~] biofuel production facility [~~is in~~] commences production on or after

January 1, 2012, and before January 1, [~~2017,~~] 2020; and

[~~(4)~~] (5) No taxpayer that claims the credit under this section shall claim any other tax credit under this chapter for the same taxable year.

(b) As used in this section:

"Credit period" means a maximum period of eight years beginning from the first taxable year in which the qualifying [~~ethanol~~] biofuel production facility begins production even if actual production is not at seventy-five per cent of nameplate capacity.

"Investment" means a nonrefundable capital expenditure related to the development and construction of any qualifying [~~ethanol~~] biofuel production facility, including processing equipment, waste treatment systems, pipelines, and liquid storage tanks at the facility or remote locations, including expansions or modifications. Capital expenditures shall be those direct and certain indirect costs determined in accordance with section 263A (with respect to capitalization and inclusion in inventory costs of certain expenses) of the Internal Revenue Code, relating to uniform capitalization costs, but shall not include expenses for compensation paid to officers of the taxpayer, pension and other related costs, rent for land, the costs of repairing and maintaining the equipment or facilities, inventory, training of operating personnel, utility costs during construction, property taxes, costs relating to negotiation of commercial agreements not related to development or construction, or service costs that can be identified specifically with a service department or function or that directly benefit or are incurred by reason of a service department or function. For the purposes of determining a capital expenditure under this section, the provisions of section 263A of the Internal Revenue Code shall apply as it read on March 1, 2004. For purposes of this section, investment excludes land costs and includes any investment for which the taxpayer is at risk, as that term is used in section 465 (with respect to deductions limited to amount at risk) of the Internal Revenue Code [~~(with respect to deductions limited to amount at risk)~~].

"Nameplate capacity" means the qualifying [~~ethanol~~] biofuel production facility's production design capacity, in gallons of [~~motor~~] fuel grade [~~ethanol~~] biofuel per year. Nameplate capacity shall be determined by the facility owner and shall not exceed the amount of production actually recorded during a consecutive seven-day period multiplied by fifty-two.

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

"Qualifying [~~ethanol~~] biofuel production" means ethanol, biodiesel, biobutanol, bio-based diesel, bio-based gasoline, or bio-based jet fuel produced from renewable, [~~organic~~] feedstocks, or waste materials, including fats, oils, grease, algae, and municipal solid waste. All qualifying production shall be fermented, distilled, gasified, or produced by physical chemical conversion methods such as reformation and catalytic conversion and dehydrated at the facility.

"Qualifying [~~ethanol~~] biofuel production facility" or "facility" means a facility located in Hawaii [~~which~~] that, if intended for transport vehicles, produces [~~motor~~] fuel grade [~~ethanol~~] biofuel meeting the minimum specifications by the American Society of Testing and Materials [~~standard D-4806,~~] standard D-4806 or D-6751, as amended.

(c) In the case of a taxable year in which the cumulative claims for the credit by the taxpayer of a qualifying [~~ethanol~~] biofuel production facility exceeds the cumulative investment made in the qualifying [~~ethanol~~] biofuel production facility by the taxpayer, only that portion that does not exceed the cumulative investment shall be claimed and allowed.

(d) The department of business, economic development, and tourism shall:

(1) Maintain records of the total amount of investment made by each taxpayer in a facility;

(2) Verify the amount of the qualifying investment;

(3) Total all qualifying and cumulative investments that the department of business, economic development, and tourism certifies; and

(4) Certify the total amount of the tax credit for each taxable year and the cumulative amount of the tax credit during the credit period.

Upon each determination, the department of business, economic development, and tourism shall issue a certificate to the taxpayer verifying the qualifying investment amounts, the credit amount certified for each taxable year, and the cumulative amount of the tax credit during the credit period. 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 certification to conform to the facts.

If in any year, the annual amount of certified credits reaches [~~$12,000,000~~] <u>$20,000,000</u> in the aggregate, the department of business, economic development, and tourism shall immediately discontinue certifying credits and notify the department of taxation. In no instance shall the total amount of certified credits exceed [~~$12,000,000~~] <u>$20,000,000</u> per year. Notwithstanding any other law to the contrary, this information shall be available for public inspection and dissemination under chapter 92F.

(e) If the credit under this section exceeds the taxpayer's income tax liability, the excess of credit over liability shall be refunded to the taxpayer; provided that no refunds or payments on account of the tax credit allowed by this section shall be made for amounts less than $1. All claims for a credit under this section [~~must~~] <u>shall</u> 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.

(f) If a qualifying [~~ethanol~~] biofuel production facility or an interest therein is acquired by a taxpayer prior to the expiration of the credit period, the credit allowable under subsection (a) for any period after [~~such~~] the acquisition shall be equal to the credit that would have been allowable under subsection (a) to the prior taxpayer had the taxpayer not disposed of the interest. If an interest is disposed of during any year for which the credit is allowable under subsection (a), the credit shall be allowable between the parties on the basis of the number of days during the year the interest was held by each taxpayer. In no case shall the credit allowed under subsection (a) be allowed after the expiration of the credit period.

[~~(g) Once the total nameplate capacities of qualifying ethanol production facilities built within the State reaches or exceeds a level of forty million gallons per year, credits under this section shall not be allowed for new ethanol production facilities. If a new facility's production capacity would cause the statewide ethanol production capacity to exceed forty million gallons per year, only the ethanol production capacity that does not exceed the statewide forty-million gallon per year level shall be eligible for the credit.~~]

[~~(h)~~] (g) Prior to construction of any new qualifying [~~ethanol~~] biofuel production facility, the taxpayer shall provide written notice of the taxpayer's intention to begin construction of a qualifying [~~ethanol~~] biofuel production facility. The information shall be provided to the department of taxation and the department of business, economic development, and tourism on forms provided by the department of business, economic development, and tourism, and shall include information on the taxpayer, facility location, facility production capacity, anticipated production start date, and the taxpayer's contact information. Notwithstanding any other law to the contrary, this information shall be available for public inspection and dissemination under chapter 92F.

[~~(i)~~] (h) The taxpayer shall provide written notice to the director of taxation and the director of business, economic development, and tourism within thirty days following the start of production. The notice shall include the production start date and expected [~~ethanol fuel~~] biofuel production for the next twenty-four months. Notwithstanding any other law to the contrary, this information shall be available for public inspection and dissemination under chapter 92F.

[~~(j)~~] (i) If a qualifying [~~ethanol~~] biofuel production facility fails to achieve an average annual production of at least seventy-five per cent of its nameplate capacity for two consecutive years, the stated capacity of that facility may be revised by the director of business, economic development, and tourism to reflect actual production for the purposes of determining [~~statewide production capacity under subsection (g) and~~] allowable credits for that facility under subsection (a). Notwithstanding any other law to the contrary, this information shall be available for public inspection and dissemination under chapter 92F.

[~~(k)~~] (j) Each calendar year during the credit period, the taxpayer shall provide information to the director of business, economic development, and tourism on the number of gallons of [~~ethanol~~] biofuel produced and sold during the previous calendar year, how much was sold in Hawaii versus overseas, percentage of Hawaii-grown feedstocks and other feedstocks used for [~~ethanol~~] biofuel production, the number of employees of the facility, and the projected number of gallons of [~~ethanol~~] biofuel production for the succeeding year.

[~~(l)~~] (k) In the case of a partnership, S corporation, estate, or trust, the tax credit allowable is for every qualifying [~~ethanol~~] biofuel production facility. The cost upon which the tax credit is computed shall be determined at the entity level. Distribution and share of credit shall be determined pursuant to section 235-110.7(a).

[~~(m)~~] (l) Following each year in which a credit under this section has been claimed, the director of business, economic development, and tourism shall submit a written report to the governor and legislature regarding the production and sale of [~~ethanol.~~] biofuel. The report shall include:

(1) The number, location, and nameplate capacities of qualifying [~~ethanol~~] biofuel production facilities in the State;

(2) The total number of gallons of [~~ethanol~~] biofuel produced and sold during the previous year; and

(3) The projected number of gallons of [~~ethanol~~] biofuel production for the succeeding year.

[~~(n)~~] (m) The director of taxation shall prepare forms that may be necessary to claim a credit under this section. Notwithstanding the department of business, economic development, and tourism's certification authority under this section, the director may audit and adjust certification to conform to the facts. The director may also require the taxpayer to furnish information to ascertain the validity of the claim for credit made under this section and may adopt rules necessary to effectuate the purposes of this section pursuant to chapter 91."

SECTION 3. Statutory material to be repealed is bracketed and stricken. New statutory material is underscored.

SECTION 4. This Act shall take effect on January 1, 2012 and shall apply to taxable years beginning after December 31, 2011.

INTRODUCED BY: Calvin K.Y. Say

BY REQUEST

JAN 22 2010

H.B. NO. 2436

Report Title:
Biofuel Facilities; Nameplate Capacity; Certified Credits

Description:
Expands the facility tax credit to include various biofuels; amends the definition of nameplate capacity; requires a qualifying facility to be located within the State and to utilize locally grown feedstock for at least 75% of its production output; increases the amount of certified credits from $12 million to $20 million; and removes the 40 million gallon production per year cap.

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