LATE TESTIMONY

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HOUSE COMMITTEE ON ECONOMIC REVITALIZATION, BUSINESS & MILITARY AFFAIRS
TESTIMONY REGARDING HB 2168
RELATING TO TAX CREDITS

TESTIFIER: KURT KAWAFUCHI, DIRECTOR OF TAXATION (OR DESIGNEE)
DATE: FEBRUARY 2, 2010
TIME: 8:30AM
ROOM: 312

This bill a new section proposes conforming to Section 45D, Internal Revenue Code, providing for a New Markets Tax Credit.

The Department of Taxation (Department) **opposes this measure because it has not been factored into the Executive Budget.**

I. NEW MARKETS TAX CREDIT, GENERALLY.

The purpose of the New Markets Tax Credit is to encourage investment in qualifying entities that provide business and economic development in targeted low-income communities. The tax credit is provided to the investors in these entities.

In order to claim the New Markets Tax Credit, the community development entity (CDE) must be certified at the federal level before the credits may be claimed. Once certified, the entities may apply to the United States Treasury Department for allocation of the credits. The Internal Revenue Code provides the aggregate amount of New Markets Tax Credits that can be allocated each year.

II. COMMENTS REGARDING THE PROPOSED HAWAII NEW MARKETS TAX CREDIT.

The Department has the following comments regarding a proposed conforming amendment to Section 45D, Internal Revenue Code—

Hawaii Connection—The Department opposes that this measure does not have a Hawaii connection. This measure should be amended to connect this credit activity with Hawaii. The intent of tax incentives paid out of the Hawaii treasury should be to provide benefits to entities that benefit Hawaii.

Recapture—To insure that the benefit to Hawaii remains in order to qualify for the credit, the bill needs to provide some form of recapture provisions. While section 45D of the Internal Revenue Code has recapture provisions, these provisions will not insure the connection to Hawaii.

Multiple Issue—This bill will allow multiple allocation amongst investors. The Department opposes decoupling from well-settled principles of partnership taxation. Though tax credits do not inherently have economic effect, credit allocations should follow something that does have economic effect. Moreover, there is added concern over the decoupling from partnership tax principles from experiences with the High Technology Business Investment Tax Credit under Act 221. Businesses abused the concept of allocating credits amongst partners, which led to law changes to reign-in wild allocations. The Department recommends eliminating this provision.

Limited Impact Program—The Department points out that this bill is far narrower than other New Markets Tax Credit proposals. This bill allows a credit only for those taxpayers that hold a federal claim. Though this may be simpler to administer, the Department raises the issue for the Committee because it could be that only one or two taxpayers in the entire State may qualify. When it appears that the general public cannot reasonably qualify, a tax credit begins to look more like a directed subsidy to those few that qualify. The Department suggests the Committee determine whether this is a strict "piggy back" credit or if a new "stand-alone" New Markets Tax Credit is desired.

Resources—Administration of the New Markets Tax Credit is extremely complex. Taxpayers need advice from experienced attorneys and consultants to apply and qualify for this credit. Likewise, in order to assure maximum compliance and minimize revenue leakage, the Department would need an unbudgeted appropriation to staff its compliance and legal offices with training on this federal tax credit. The New Markets Tax Credit is as complicated, if not more complicated than the state high technology credit; therefore additional personnel would be needed.

III. OPPOSED TO UNBUDGETED REVENUE LOSS

The Department cannot support the tax provision in this measure because it is not factored into the budget. The Department must be cognizant of the biennium budget and financial plan. This measure has not been factored into either. Given the forecasted decrease in revenue projections, this measure would add to the budget shortfall.