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HOUSE COMMITTEES ON FINANCE
TESTIMONY REGARDING HB 2870
RELATING TO TAXATION

TESTIFIER: KURT KAWAFUCHI, DIRECTOR OF TAXATION (OR DESIGNEE)
DATE: FEBRUARY 10, 2010
TIME: 3PM
ROOM: 308

This bill removes the refunding feature of the capital goods excise tax credit, instead allowing a taxpayer to claim the credit only to extent the taxpayer has tax liability.

The Department of Taxation is **not opposed** to this measure.

In a time when revenue raisers are needed to balance the state budget, the Department is not opposed to making the capital goods excise tax credit nonrefundable. The Department is confident that the tax incentives provided by Congress through the stimulus measure and otherwise are sufficient incentives for business to invest in capital assets. This measure will provide taxpayers with carry-over credit that may be used in the future. Taxpayers will receive the same benefit, only losing the time value of money. Suspending the payout of this otherwise refundable credit is responsible fiscal policy during current times.

L E G I S L A T I V E

TAXBILLSERVICE

126 Queen Street, Suite 304 TAX FOUNDATION OF HAWAII Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: INCOME, Capital goods excise tax credit

BILL NUMBER: HB 2870

INTRODUCED BY: Say

BRIEF SUMMARY: Amends HRS section 235-110.7 to provide that the capital goods excise tax credit shall be nonrefundable between January 1, 2010 and December 31, 2015.

EFFECTIVE DATE: Tax years beginning after December 31, 2009

EFFECTIVE DATE: The legislature by Act 178, SLH 2009, suspended the capital goods excise tax credit for the calendar year 2009. Currently the capital goods excise tax credit is refundable so that any credit in excess of a taxpayer's income tax liability is refunded to the taxpayer. It appears that this measure proposes that the capital goods excise tax credit shall be made temporarily nonrefundable until December 31, 2015 to address the state's fiscal crisis. However, one has to question the prudence of this strategy as one has to assume that when the moratorium expires in 2015, the capital goods excise tax credit will once more become refundable. If it is assumed that the current economic conditions continue for some time to come and businesses do not turn a profit because of the slump in the economy, they will probably have very little income tax liability.

If that is the case, when the refundable feature is restored in 2015 there will, no doubt, be an onslaught of claims with the general fund taking a huge hit as claims for the refundable credit are filed. Currently, the tax credit has a $23.5 million cost to the state general fund. Multiply this by the six years of nonrefundable status and the state could be hit with a tab of nearly $120 million.

More importantly, it should be remembered that this credit was adopted to reduce the cost of capital goods which everyone acknowledges are crucial to the creation of jobs. Given the rising unemployment rate as a result of the downturn in the economy and it makes no sense to eliminate the refundable feature of this credit. Unlike many other targeted business tax credits, the capital goods excise tax credit is available to any and every industry. The refundable feature insures that businesses see an immediate return of this tax which supplements their cash flow, keeping them in business during these tough times.

It should be remembered that when this credit was enacted in 1987, it was considered preferable to an exemption from the general excise tax as the use of the capital equipment could be verified that it was to be used in the production of income. Since the credit is claimed by the purchaser, the purchaser was held responsible to prove that the capital equipment was used in the production of income. More importantly, the credit was to provide a return of the tax on an immediate basis so the reduction in the cost of the equipment could be redirected to other costs associated with the creation of jobs. Thus, the delay in realizing the reduction in the cost of the capital equipment defeats the purpose of the credit, that is, to encourage the creation of new employment opportunities, a need that is sorely wanting at this time

Digested 2/9/10