LINDA LINGLE
GOVERNOR

JAMES R. AIONA, JR.
LT. GOVERNOR

KURT KAWAFUCHI
DIRECTOR OF TAXATION

STANLEY SHIRAKI
DEPUTY DIRECTOR

STATE OF HAWAII
DEPARTMENT OF TAXATION
P.O. BOX 259
HONOLULU, HAWAII 96809

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HOUSE COMMITTEE ON FINANCE
TESTIMONY REGARDING SB 2144 SD 2 HD 1
RELATING TO ECONOMIC DEVELOPMENT

TESTIFIER: KURT KAWAFUCHI, DIRECTOR OF TAXATION (OR DESIGNEE)
DATE: MARCH 29, 2010
TIME: 6PM
ROOM: 308

As amended, this measure extends the tax credit for research activities until 2011 and repeals the high technology business investment tax credit and the technology infrastructure renovation tax credit, among other things. The Department limits its comments to Part I of this measure.

The Department of Taxation (Department) **supports the intent** of repealing the high tech and technology infrastructure tax credits; however is **concerned over potential revenue loss** from extending the research credit.

The Department supports what this measure accomplishes, which is a continuation of the research credit and financing that continuation by repealing other tax incentives. The Department's primary concern relates to the cost of the extension, which results in a revenue loss in Year 2. This cost has not been factored into the Executive Budget. The Department suggests that this measure be passed out of committee in order to continue the discussion of maintaining tax incentives for high technology.

Part I of this measure will result in the following revenue impacts—

Revenue Gain:	Revenue Loss:
FY 2011, $13.1m	
	<FY 2012, $7.6m>
FY 2013, $ 7.5m	
FY 2014, $ 3.8m	
FY 2015, $ 3.8m	

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, Extend tax credit for research activities

BILL NUMBER: SB 2144, HD-1

INTRODUCED BY: House Committee on Economic Revitalization, Business & Military Affairs

BRIEF SUMMARY: Amends HRS section 235-110.91 to extend the expiration of the tax credit for research activities from December 31, 2010 to December 31, 2011. Amends HRS section 235-110.51 to repeal the technology infrastructure renovation tax credit.

Amends HRS section 235-110.9 to repeal the high technology business investment tax credit.

Provides that funding of community-based economic development program staff, nonprofit community-based organizations, and for-profit entities in enterprise zones shall be one of the responsibilities of the Hawaii community-based economic development revolving fund.

EFFECTIVE DATE: July 1, 2020

STAFF COMMENTS: The legislature by Act 178, SLH 1999, and Act 221, SLH 2001, enacted various tax incentives to encourage the development of high technology businesses in the state. These acts provided investment and research credits, as well as income exclusions, providing tax incentives to encourage high tech businesses and individuals associated with high tech businesses. This measure repeals the technology infrastructure renovation tax credit and the high technology business investment tax credit and it proposes to extend the expiration of the tax credit for research activities from December 31, 2010 to December 31, 2011, which will perpetuate the financial drain on the state's revenues. It should also be remembered that the research credit is a refundable tax credit. Thus, should the amount of the credit exceed the taxpayer's income tax liability, any excess credit is a cash payment out of the state treasury to the claimant.

While the focus on high technology in the last few years is commendable, it fails to recognize that investments are made with the prospect that the venture will yield a profit. If the prospects for making a profit are absent, no amount of tax credits will attract investment from outside Hawaii's capital short environment. People do not invest to lose money. It should be remembered that until Hawaii's high cost of living can be addressed, all the tax incentives in the world will not make a difference in attracting new investment to Hawaii. The only attractive aspect for resident investors to plough money into such activities is the fact that the credit provides a way to avoid paying state taxes.

A former Hawaii resident who has been a success in the field of high technology pointed out recently what will make Hawaii conducive to high tech businesses and they are: (1) entrepreneurs, not capital, that comes first; (2) entrepreneurs coming from engineering schools and technology companies; (3) building a world class engineering school in Hawaii; (4) supporting internships at technology companies; (5) allowing our best children to go away to get a worldwide perspective; (6) not broadband passing through Hawaii that is a selling point; (7) that people fly direct and therefore is Hawaii's location in the middle of the Pacific an advantage?; (8) learning the rules of the game; (9) looking at Israel and learning from them; and (10) doing your own thing, being a copy cat does not work. At the heart of his remarks was the fact that in order to produce a high technology industry in Hawaii, those companies need to have access to institutions of higher education that are producing the people needed by the high technology industry. Without the academic synergy, Hawaii will never become a center for high technology activity. Thus, all of the tax incentives, like this measure embodies, will fall short of luring high technology firms to Hawaii.

Further, the tremendous tax burden, the draconian regulatory environment, and the dramatic increase in fees that go with the permitting process make Hawaii an unattractive place to do business. It should be remembered that while the high technology credits may look like a good incentive or enticement to undertake research activities in Hawaii, those who would conduct this research must live in the same high cost-of-living environment with which other taxpayers continue to struggle. Thus, the cost of maintaining those researchers will be higher than to do so where the cost of living is much lower. Let's not bet the farm on high technology without really understanding what makes this industry tick.

Obviously the authors of this proposal would like to ignore the evaluation of these tax incentives done by UHERO last year which basically condemned the credits as a waste of state resources as there is little evidence that the current program of tax credits has created substantial new employment or on-going enterprises. It is truly amazing that given the dire condition of the state's financial condition that lawmakers would continue to support unbridled drains of resources while at the same time proposing that the tax burden be increased on all other taxpayers. With declining revenues, every program from education to corrections to health services will be severely curtailed. If the state doesn't have the money to put textbooks in the schools why then do we need the highly touted, high-paying jobs the advocates for the industry promise? The next generation may not even know how to read given the cuts to the education budget.

Again, lawmakers must ask themselves whether or not this incentive is appropriate in these dire financial times. Given that there are many other proposals in the legislature to hike tax rates for either the general excise or net income taxes, taxpayers will find the continuance of these targeted business tax credits frightening. Frightening because these very lawmakers are supposed to represent the best interest of their constituents. Raising taxes on constituents while still handing out money to favored groups will engender the ire of constituents. The finger of blame for these potential increases in tax burden should not stop at lawmakers, but be placed squarely on those in the community who continue to push for these targeted tax credits. Perhaps those proponents should be asked to pick up the tab for this reckless expenditure of precious tax dollars.

It should be noted that this measure, which repeals two of the high technology credits, would become effective July 1, 2020. Given that they are credits against the income tax and there are investments made to qualify for the credit, the effective date should be certain and apply to a specified tax year, e.g., "Upon approval and shall not apply to investments made after June 30 and for tax years beginning after July 1, 2010."

Digested 3/29/10

PACIFICAP
GROUP

PACIFICAP GROUP, LLC
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March 28, 2010

Testimony for Hearing before the
House Committee on Finance
Monday, March 29 , 2010, 6:00 pm

State Capitol, Conference Room 308
415 South Beretania Street
Honolulu, Hawaii 96813

Re: Testimony in STRONG OPPOSITION to SB 2144 HD1
Relating to Economic Development

Chair Oshiro, Vice-Chair Lee, and Committee Members:

Thank you for the opportunity to submit testimony in STRONG OPPOSITION to SB 2144 HD1.

This bill, among other things, seeks to extend the Act 221 Research Credit for a year while repealing the Act 221 Investment Credit.

While I support the Act 221 Research Credit, I do not think it would be fair or prudent to extend it at the expense of the Act 221 Investment Credit. According to Tax Department data, the Act 221 Investment Credit has **attracted more than $1.3 billion of cash investments** and has been utilized by many more local high tech and media companies than the Act 221 Research Credit. According to Tax Department data, **Act 221 companies paid more than $232 million in job compensation in 2008 alone.**

In the middle of the Great Recession, Hawaii's economy needs now, more than ever, successful tax incentive programs such as the Act 221 Investment Credit, which has a proven track record of attracting capital and creating jobs for Hawaii's economy, at much lower costs to taxpayers than State government spending and even federal stimulus dollars.

Continuing what has been annual repeated efforts to undermine the Act 221 for ideological and political reasons, while turning a blind eye to the FACTS of hundreds of millions of dollars of cash and jobs that Act 221 has brought to our economy each year, at a time when our local community needs this cash and these jobs more than ever, is irresponsible, and indeed tragic, for our State.

We are all acutely aware of the large budget deficit facing our State. However, pretending to balance the budget "on paper" with false financial assumptions is financially irresponsible and may even violate the State Constitution.

Specifically, any retroactive repeal of existing rights to earn Act 221 Investment Credits for investments already made should not and cannot be relied upon to balance the State budget.

In "pricing" this bill for budgetary purposes, each of you, as members of the House Finance Committee, have a legal and fiduciary duty to the State, your fellow legislators and your constituents to ensure that your projected "cost savings" from this bill do not include "savings" from the unconstitutional or otherwise illegal repeal or restriction of tax credits from investments that already have been made.

In our system of checks and balances, each of you as legislators has the legal responsibility to independently exercise due diligence to ensure that the "pricing" and budgetary estimates for this bill submitted to you by the Administration are not inaccurate or misleading and do not include projected "cost savings" from retroactive, unconstitutional or otherwise illegal repeals or restrictions of tax credits for investments that already have been made.

As you know, the Act 221 Investment Credit gives investors the right to earn tax credits over a five year period for qualified investments they make in the first year. This is analogous to a five year "installment payment plan" that one might agree to for the purchase of a car, or installment payments that the State makes over multiple years to repay the cash that the State receives from the sale of State bonds.

Any new law passed by the State to unilaterally repeal or restrict Act 221 Investment Credits for investments already made would be just as illegal, financially irresponsible and simply wrong, as would be a car buyer's unilateral decision to stop making car payments on his five year installment payment plan, or the State's unilateral decision to simply stop making installment payments on the bonds that the State has issued. Because it involves State government action, such law would also violate the U.S. Constitution.

The immediate and long term implications for the State also would be the same. Lawsuits would likely be immediately filed against the State, potentially by thousands of Act 221 investors, and over the longer term, private investors would no longer trust the State to invest in any future financing program, or even future bonds offered by the State.

Litigation and judicial appeals against the State would likely drag on for several years, most likely longer than the recession itself, before the State could start to collect any tax revenues under this bill, in the unlikely event that the State should prevail in such litigation.

If there is evidence that you as legislators, or members of the Administration, chose to pass this bill while knowingly or recklessly disregarding its unconstitutionality and illegality, in spite of this and other public testimony making you aware of these problems, the State's legal position would be further damaged.

While somewhat unclear, it appears that Section 6 of this bill may be attempting to address some retroactivity concerns in the language that reads:

> This Act does not affect rights and duties that matured, penalties that were incurred, and proceedings that were begun before its effective date, including carryover tax credits.

However, if (to purport to balance the State budget) this bill is interpreted by the State to repeal the right to earn credits during the full five year period for investments already made, such retroactivity would be unconstitutional and trigger massive litigation against the State, would not result in real budgetary savings and would instead increase the budget deficit from the resulting massive (and avoidable) litigation costs.

By completely repealing and wiping off the books HRS Section 235-110.9, which is the statutory authority for the Act 221 Investment Credit, this bill would make it extremely difficult and confusing for the Tax Department to administer the law in future years for investments already made. It would also create serious legal ambiguities and confusion for investors and Act 221 companies. It would make it more difficult for attorneys and CPA's to find and research the law if it is wiped off the books and legal databases, and it would help to reinforce Hawaii's reputation of having an extremely inefficient, hostile and toxic investment and business environment.

There is no reason to artificially create such legal confusion and chaos, which would result in a tremendous waste of time and resources for both the State and the private sector.

No matter how serious the State's budget deficit may be, violating the U.S. Constitution or otherwise breaking the law to balance the budget is no more a solution than robbing a bank or selling drugs would be for an individual.

Please also remember that each of you as legislators, as well as the Governor, has personally taken a solemn oath that you will "support and defend the Constitution of the United States."

Thank you for the opportunity to submit testimony on this very important matter.

Respectfully submitted,

Jeffrey K. D. Au
Managing Director and General Counsel
PacifiCap Group, LLC

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MEMORANDUM

TO: Representative Marcus R. Oshiro
Chair, House Committee on Finance
Via Facsimile: 586-6001

FROM: Anne Horiuchi

DATE: March 29, 2010

RE: **S.B. 2144, SD2, HD1 – Relating to Economic Development**
Hearing: Monday, March 29, 2010 at 6:00 p.m. (Agenda #5), Room 308

Dear Chair Oshiro and Members of the Committee:

I am Anne Horiuchi, testifying on behalf of USAA. USAA, a diversified financial services company, is the leading provider of competitively priced financial planning, insurance, investments, and banking products to members of the U.S. military and their families. USAA has over 82,000 members in Hawaii.

USAA has concerns regarding S.B. 2144, SD2, HD1.

Part I of S.B. 2144, SD2, HD1 repeals the remaining Act 221 tax credits. Part III of the measure provides that the Act will not affect the "rights and duties that matured . . . before [the Act's] effective date, including carryover tax credits."

For USAA, it is unclear whether the provisions of S.B. 2144 will impact its business. Currently, USAA has an outstanding $4.2 million in Act 221 tax credits. USAA is in the process of determining whether its rights in these credits have "matured," as described in Part III. USAA acknowledges that, if its credits have matured, then USAA will not be impacted by S.B. 2144. However, if the credits have not matured, then USAA is concerned that it has invested $4.2 million in outstanding credits that will be lost if S.B. 2144 is passed.

Thank you for the opportunity to submit testimony on this measure.

ADVANTAGE
CAPITAL
PARTNERS

March 29, 2010

Testimony for Hearing before the
House Committee on Finance
Monday, March 29, 2010, 6:00 pm

State Capitol, Conference Room 308
415 South Beretania Street
Honolulu, Hawaii 96813

Re: Testimony in STRONG OPPOSITION to SB 2144 HD1
Relating to Economic Development

Chair Oshiro, Vice-Chair Lee, and Committee Members:

Thank you for the opportunity to submit testimony in OPPOSITION to SB 2144 HD1.

Because of ACT 221 Advantage Capital Partners has been a very active mainland based investor with investments in eight Hawaii based companies. The elimination of ACT 221 will prevent Advantage Capital from making future investments in Hawaii based companies. While we understand the budget issues the State of Hawaii is facing and are disappointed that ACT 221 may be a casualty of those budget shortfalls, the current draft of SB 2144 is ambiguous regarding the treatment of tax credits ALREADY earned from investments made prior to the law's potential repeal. Specifically, the language is not clear about the treatment of future tax credits owed to investors based on past investments in QHTB companies under ACT 221. Advantage Capital is asking the committee to CLARIFY the language of SB 2144 HD1 to ensure that future tax credits owed to investors under existing ACT 221 investments are allowed under the current rules of the program.

Because of ACT 221 and the five year flow of tax credits, Advantage Capital was able to raise capital from mainland sources and invest in Hawaii. Without the inducement of the tax credits and the investors' faith that the State of Hawaii would adhere to the law for the full five year term the tax credits are allowed, Advantage could never have raised these funds. As such, if the future tax credits to be earned on existing tax credits were to be delayed or otherwise impaired in any way, we and our investors would have no choice but to seek legal redress for the economic harm such an action caused. Perhaps worse, these important institutional investors will likely never again consider an investment in Hawaii in conjunction with a State economic development program and will write off the State as a potential business location. This will include important programs like low-income housing projects and investments through the New Markets Tax Credit program. This obstruction will cripple Hawaii's economic development efforts for decades to come.

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www.advantagecap.com

Because of the possible severe economic consequences to Advantage Capital, its investors and the State of Hawaii that any ambiguity may cause, we ask that the committee clarify that the intent of SB 2144 HD1 is NOT to restrict or delay the use of QHTB tax credits to be earned in future years from investments made prior to the end of ACT 221.

Regards,

Ryan Brennan

Ryan M. Brennan
Managing Director

puko'a
SCIENTIFIC

SB2144 SD2 HD1 - Relating to Economic Development

DATE: March 29, 2010
TIME: 6:00 P.M.
PLACE: Room 308
TO: House Committee on Finance
Representative Oshiro, Chair
Representative Lee, Vice Chair

FROM: James P. Karins
President and CEO
Pukoa Scientific

Re: Testimony in Support of SB2144 SD2 HD1, with amendments to Section 3.

Chair, Vice-Chair and Committee Members:

Thank you for the opportunity to submit testimony in support to SB2144 SD2 HD1. My name is Jim Karins and I am the President of Pukoa Scientific. Pukoa Scientific is a 17 person company started in 2004 specializing in the interpretation of image and signal data to identify objects, threats or targets for military, security, medical and industrial applications. Pukoa Scientific is in the dual use sector which has proven to be one of the fastest growing technology sectors. Even during the trying year of 2009 we were able to grow to 17 employees; 13 of our 17 employees are full time and 16 of those 17 reside in Hawaii. Of the 12 full time staff in Hawaii, 10 graduated from high schools in Hawaii, 10 graduated from the University of Hawaii or Hawaii Pacific University and at least 4 worked on the mainland prior to finding work in Hawaii. We currently generate more than \$2.5M in revenue and pay over \$1.5M in compensation.

All of us understand the difficult financial condition of the state and industry wants to help. One of the best ways for industry to help is to maintain and grow the workforce. Without job creation, all the cost cutting and all the tax increases will only create a downward spiral, requiring more costs and more tax increases. The state must maximize its return by spending money that generates multiples of increased spending, garnering the most jobs and job income from the least amount of tax dollars. Research and development is one of those areas. In comparing the R&D tax credit to other tax credits, we observe that R&D tax credit is more effective in generating and maintaining a higher number of jobs per tax dollar, generates significantly higher tax revenues for dollar spent, and stimulates significantly more economic activity in the state per dollar of tax credit. Additionally, companies leveraging the R&D tax credits tend to be more mature companies, some of which are on the cusp of becoming much larger firms, further increasing the number of employees and generating tax revenue. As such, I feel that state benefits greatly from extending the R&D tax credit and making the legislatively determined trade-offs to fund this extension.

However, these trade-offs need to be fair and legal. I am concerned that repealing Section 235-110.9 Hawaii Revised Statutes will create the following problems: (1) It eliminates the definition of a QHTB which is referred to in Section 235-110.91, (2) It may be unconstitutional in the retroactivity and will probably result in lawsuits and possibly no savings to the state, and (3) It is not the right message to the world – Hawaii should stand by its agreements to all. End allowing tax credits on new investments, but please don't punish those who invested in companies in good faith. I recommend that Section 3 be amended to add an earlier end date to Section 235-110.9 but not repeal it. Section 6 tries to alleviate the issue of retroactivity, but it seems to be more confusing than just changing the end date.

Research and development is a highly critical component to a sustainable economy. R&D provides high-paying jobs to highly educated employees. These employees pay significant taxes back to the state and spend significant amounts of their income within the state for goods and services. Additionally as the R&D matures it creates product companies that increase the number of jobs and tax base significantly.

Some important facts related to R&D tax credits are:

(1) The cost of the R&D tax credit is between $13 and $14 million per year, but R&D employees are highly paid and pay income taxes at high rates and generate significant other economic activity within the state (see Appendix A for analysis),
(2) R&D is so important to the economy of the United States that the federal government is considering making the federal R&D tax credit permanent,
(3) R&D is so important to the economy of states, that approximately 33 states provide R&D tax credits of various kinds and of the 17 that don't, 4 have no corporate income taxes (see Appendix B),
(4) R&D is becoming more competitive world-wide. Some countries are offering vastly larger tax credits to lure R&D companies, for example small companies in Quebec are eligible for a 37.5% tax credit in addition to the Canadian tax credits. Additionally, for the first time, China has increased its R&D at a rate higher than the United States (see Appendix C),
(5) A tax credit of 20% on wages and supplies amounts to about 10% of the cost of doing R&D,
(6) The tax credits for R&D are comparable or less than those given to other critical industries to economic diversity such as Act 88 (15% credit on costs not just salaries and supplies) for the movie industry or 35% tax credits on renewable energy,
(7) R&D funds are highly leveraged by imported monies, thus generating more economic activity than economic activities that just move money from one in-state entity to another,
(8) R&D tax credits are only received after the company has expended the funding, generating tax revenues to the state first,
(9) R&D tax credits typically go back into additional R&D through additional salaries,
(10) Studies have shown that for every $1 in tax credits or lower costs of operation, R&D increases by approximately $2-$3.

While these positive aspects are fairly defined, there have been some people who have expressed concerns about the competitiveness of Hawaii's R&D tax credit levels and their refundability. But several factors that are not considered in those concerns include:

(1) Comparisons are only made to other states and not to other countries. R&D is becoming a economic driver worldwide and Hawaii companies compete worldwide,
(2) Hawaii's tax credits have been defined to a very small but high payoff group of high technology companies defined as QHTBs while most states provide their tax credits to any company that can qualify under federal tax credit laws,
(3) The entire cost of doing R&D is the most important factor. Hawaii has a number of competitive disadvantages such as high income tax rates, high cost of living, high unemployment insurance costs, and high transportation costs, and
(4) R&D returns are highest after several years when R&D turns into products, resulting in significant growth in job opportunities, increased intellectual property owned by Hawaii residents, and increased travel to the state by customers and technology related conferences

In summary the Hawaii R&D tax credit has been effective in generating new taxes, generating new companies and employing approximately 1100 residents. It is important that there not be a gap in the R&D tax credit while the 2011 legislature addresses the longer term impact of R&D on the state. Companies need to make long term plans when doing R&D. It is critical to the industry that the tax credit be in place long enough to encourage R&D and its commiserate high paying jobs, potential job growth, and its impact on the sustainability of the states economy.

I therefore strongly encourage the committee to pass this bill with Amendment to Section 3 to sunset Section 235.110.9 early, such as July 1, 2010, instead of repealing it.

Thank you for the opportunity to testify.

/s/James P Karins

James P. Karins
President and CEO
Pukoa Scientific
karins@pukoa.com

APPENDICES

A. Revenue generated to the state by R&D companies compares favorably to the expenses of the R&D tax credit. The table below demonstrates a fairly simple model of the tax revenue generated by the R&D efforts and supporting structure of the companies. In 2008 $13.4M in tax credits was claimed. Since the credit is 20% of qualified expenses, the qualified expenses are 5 times the credit ($67M). Typically about half of an R&D companies expenses are qualified, yielding expenses of about $134M by companies relating to qualified R&D. Wages are about 60% of those expenses and 40% goes to a variety of expenses including rent. I used a 6% income tax rate and a 4.5% GET rate to estimate the taxes directly paid by these companies. An economic multiplier of 2 was used since most of the wages and most the other expenses are recycled in the economy. Total revenue of about $14.4M is calculated to be attributable to the R&D efforts of the companies receiving $13.4M in R&D tax credits.

2008		Income Tax	GET
R&D Tax Credit	$13.4 M		
Qualified Expenses	$67 M		
Total R&D Related Expenses	$134 M		
Wages	$80.4 M	$4.8 M	
Other Expenses	$53.6 M		$2.4 M
Economic Multiplier Effect		$9.6 M	$4.8 M
TOTAL REVENUE	$14.4 M		

B. State R&D tax credits vary greatly from state to state. In some respects Hawaii's tax credit is very good. In a couple it lags other states. For example the credit rate is the best in Hawaii, however only a few states such as Hawaii restrict it to certain companies or R&D areas.

R&D Credit Topic		**Notes**
R&D Tax Credits	33 States	Of the 17 that do not 4 have no income taxes
Non-incremental	3 States	HI, CT, WV
Credit Refundable	8 States	
Limited Availability	2 States	HI, AR
Taxes the Credit Received	1	HI
Tax Credit	2.5-20%	Average rate is 6.5%

C. International tax credits vary even more and are particularly favorable in some countries. The table below is a summary of some of the tax credits offered by competing nations. A direct comparison is difficult since the incentives are in various forms such as tax abatements or enhanced deductions. One noteworthy example is Quebec Province in Canada where overall tax credits can reach 72.5%.

Country	R&D Tax Incentive
Australia	• Allows a 125% deduction for R&D expenses • *Plus* a 175% deduction for R&D expenditures exceeding a base amount of prior-year spending.
Canada	• Offers a permanent 20% flat (i.e., first-dollar) R&D tax credit for large companies Small companies receive 35% flat R&D tax credit Quebec province offers an additional 37.5% for small companies Other provinces offer other incentives
China	• Offers foreign investment enterprises a 150% deduction for R&D expenditures, provided that R&D spending has increased by 10% from the prior year.
France	• Allows a 50% R&D credit, includes a 10% flat credit and a 40% credit for R&D expenditures in excess of average R&D spending over the two previous years.
India	• Companies carrying on scientific research and development are entitled to a 100% deduction of profits for 10 years. • Automobile industry also is entitled to a 150% deduction for expenditures on in-house R&D facilities.
Ireland	• Offers a 20% R&D tax credit, plus a full deduction, as well as a low generally applicable 12.5% corporate income tax rate. • Capital expenditures may also qualify for a separate flat credit.
Japan	• Offers a flat 10% R&D tax credit (a 15% flat credit is provided for small companies), in addition to other incentives.
Korea	• Tax holidays, up to 7 years, are provided for high-technology businesses. • In addition, a variety of tax credits are provided for R&D type expenditures.
Singapore	• "R&D and Intellectual Property Management Hub Scheme" offers U.S. companies a 5-year tax holiday for foreign income earned with respect to Singapore-based R&D.
United Kingdom	• Allows a 125% deduction for R&D expenses Plus a 175% deduction for R&D expenditures exceeding a base amount of prior-year R&D spending.

Testimony of

John A. Chock

before the

HOUSE COMMITTEE ON FINANCE
Rep. Marcus R. Oshiro, Chair
Rep. Marilyn B. Lee, Vice Chair

SB 2144 SD2 HD1 RELATING TO ECONOMIC DEVELOPMENT

DATE: Monday, March 29, 2010
TIME: 6:00 P.M.
PLACE: Conference Room 308
State Capitol
415 South Beretania Street

Chair Oshiro, Vice Chair Lee, and Committee Members:

It has been said that if we're going to invest in the education of our young people, we need to invest in good, high-paying jobs for them in the future as well. For this reason I would like to express my opposition to those portions of SB 2144 SD2 HD1 which would eliminate support for Hawaii's Qualified High Technology Businesses and also potentially deny credits to investors who had invested in QHTBs to support the growth of those businesses. Those investors made their investment decisions with the expectation that credits in support of those investments would be available to them in accord with existing law.

Hawaii's early-stage companies have done a good job on developing technology to commercialize. They are sorely hampered by a lack of access to growth capital for commercialization, and this bill will make it more difficult to raise capital and only exacerbate economic diversification efforts for our state.

Capital formation policy for Hawaii's emerging companies should be looked at holistically. Early stage R&D through grants and credits, angel investment, venture capital for expansion, follow-on funding, and sources of debt are all discrete and necessary elements of a healthy capital market, and all are needed for Hawaii's business success.

I have been involved in economic diversification, technology development, and capital formation for a long time in both the public and private sectors, and I early on learned that it's tough to convince people to invest in diversification when the economy's strong, and there is no need for diversification. It's equally tough to promote diversification when the economy's down and it's not affordable, so a long-term vision clearly is needed. Right now is no different, and the provisions of SD 2144 HD1 with respect to QHTB's and technology investment will only make it that much more difficult to diversify Hawaii's economy over the long term.

Thank you for the opportunity to provide testimony on SD 2144 SD2 HD1.

John A. Chock
1949 Kakela Drive
Honolulu, Hawaii 96822

Bill: SB 2144 HD1

Date: March 29, 2010
Time: 6:00pm
Place: Room 308

Committee: FIN
Chair: Representative Oshiro
Vice Chair: Representative Lee

I Strongly Oppose this bill

Aloha Chair, Vice Chair, and Members of the Committee,

My name is Mike Curtis and I run a local software development company called SDC Hawaii, LLC. We employ seven people, five of whom are software designers and developers. We are a start-up company owned and funded by local investors and members of our own employee team.

It pains me to oppose this legislation because I support the extension of the R&D tax credit and I support the development of the local technology industry as a whole. However, this bill as currently written repeals the Act 221 investment tax credit which will result in irreparable harm to my company's investors, the company itself, and my employee partners. It will also result in further damage to our state's reputation as a stable place to do business.

Repealing Act 221 prior to its established sunset date continues a dangerous precedent set last year wherein the Legislature upset what investors and local tech companies considered to be stable law. The sunset date was put into effect four years ago. Major provisions within the law were then changed last session, critically impacting companies (and costing jobs) throughout the state. Despite last year's changes, local companies revamped their capital financing strategies and proceeded to build their businesses. Now, one year later, we face a great deal of uncertainty and the possibility that our financing strategies will be destroyed and possibly many of our companies in the process. The proposed legislation and resultant uncertainty has itself effectively put a hold on funding since the introduction of the bills.

In addition, the extension of the R&D tax credit beyond the current sunset date is a new promise to industry. Financing this new commitment should not come at the expense of breaking an existing promise. Doing so now upsets existing law and will result in damage to those companies that have relied on the investor tax credit to develop their financing plans for the remainder of this year.

In closing, I want to share with you the impact that your decision on this bill will likely have on our company. Right now our business plan calls for us to add five employees each year for the foreseeable future, with our employees (mostly software engineers) continuing to earn an average of roughly $75,000 annually. Our capital structure has been designed for local investors based on Act 221 and the expectation that Act 221 would sunset 12/31/10. Last year's changes were damaging to us, pay cuts were required and several of our employees had to be laid off due to a shortfall in anticipated funding. The proposed laws would likely eliminate our ability to obtain further funding. Without further funding, it is likely that most of our current employees will lose their jobs and these new hires will not happen. Past changes to the investor tax credit, along with the bills proposed this year, have already injected a great deal of uncertainty into investors' minds and reduced our ability to raise funds. The change proposed in this bill will almost certainly eliminate further funding this year when we need it most.

Thank you for the opportunity to testify on this bill.

Sincerely,

Name: Mike Curtis
Title: Chief Operating Officer
Company: SDC HAWAII, LLC
Phone: 808-292-6862
Email: mcurtis@hawaii.rr.com

Bill: SB2144 HD1

Hearing Date: March 29, 2010
Time: 6:00 pm
Place: Room 308

Committee: House Committee on Finance

Chair Oshiro, Vice Chair Lee and Committee Members:

I STRONGLY OPPOSE BILL SB2144 HD1

Thank you for the opportunity to submit testimony in STRONG OPPOSITION to SB2144 HD1.

This bill, among other things, seeks to extend the Act 221 Research Credit for a year while repealing the Act 221 Investment Credit. While I support the Act 221 Research Credit, I do believe it would be fair or prudent to extend it at the expense of the Act 221 Investment Credit.

My name is Dew-Anne Langcaon and I am President and Co-Founder of Ho'okele Health Technologies, LLC a high tech start up company whose mission is to develop and deploy advanced touchscreen wireless technologies into the homes of the elderly to enable them to live safely, healthy, independently and affordably in their own homes. Our goal is to help seniors, their families and the State of Hawaii to improve the quality and reduce the cost of eldercare which already is having a crushing impact to budgets and our economy through the deployment of technology.

We employ 5 employees including 2 software developers, a physician, an RN and a Social Worker, as well as contract with several local companies for software developers. Our work is focused on developing the technologies and conducting the research as to the efficacy and adoption of such technologies by seniors and their loved ones. Our company is a QHTB and has been funded through investors who believe in our mission and who have been able to mitigate some of their downside risk in our early stage company through the Act 221/215 Investment Tax Credit. This has directly allowed us to raise enough capital to bring our vision to near fruition.

While I am a big supporter of the high tech industry and the R&D credit, this bill results in the repeal of the investment tax credit which will be harmful to my company and its investors. We are nearing the end of our pilot phase of product development and are in process of raising additional capital to bring our product to the next level in order to launch to market. However, the uncertainty which this and other bills have caused is making it impossible for our current and potential new investors to make an informed investment decision. Without sufficient follow on capital, our ability to complete the development of such leading edge technologies which could bring peace of mind and reduce the cost of eldercare for so many families will be jeopardized.

Additionally, my company is only one of many QHTB's whose future is jeopardized not by the state of the economy or the company's failure to execute, but due to this reversal of a promise to maintain the investment tax credit through its scheduled sunset date at the end of 2010. Our business plan and investors counted on the ability of the company to raise sufficient funding through the end of 2010 to get to the point of revenue generation and self-sustainability. By cutting the investment tax credit prematurely, our and other QHTB's futures are endangered on the cusp of reaching our potential. The State made an investment in QHTB's through the form of the tax credit, and by prematurely ending the credit it is also prematurely ending the State's own ability to enjoy any return on its investment in the form of tax revenue from GET on sales, payroll taxes and income taxes.

I urge you to strongly fulfill the promise to the high tech industry to maintain the investment tax credit through the end of 2010 so that the companies, investors and the State can realize the expected benefits that were envisioned for Act 221/215.

Thank you for the opportunity to testify on this important matter.

Mahalo,

Dew-Anne Langcaon
President
Ho'okele Health Technologies, LLC
808-457-1656
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FINTestimony

From: mailinglist@capitol.hawaii.gov
Sent: Monday, March 29, 2010 1:26 PM
To: FINTestimony
Cc: jachock@gmail.com
Subject: Testimony for SB2144 on 3/29/2010 6:00:00 PM

Testimony for FIN 3/29/2010 6:00:00 PM SB2144

Conference room: 308
Testifier position: oppose
Testifier will be present: No
Submitted by: John Chock
Organization: Individual
Address: 1949 Kakela Dr Honolulu HI
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E-mail: jachock@gmail.com
Submitted on: 3/29/2010

Comments: