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HOUSE COMMITTEE ON FINANCE

TESTIMONY OF THE DEPARTMENT OF TAXATION REGARDING HB 797 RELATING TO TAXATION

TESTIFIER:	**FREDERICK D. PABLO, DIRECTOR OF TAXATION (OR DESIGNEE)**
COMMITTEE:	**FIN**
DATE:	**FEBRUARY 25, 2011**
TIME:	**11:00AM**
POSITION:	**NO POSITION**

This measure extends the limitations for claiming the technology infrastructure renovation credit and the qualified high technology business investment credit for an additional two years. The Department takes no position on this measure.

The revenue impact is a gain of approximately $19.8 million in fiscal year 2012 and $11.7 million in 2013.

HSDC HAWAII STRATEGIC DEVELOPMENT CORPORATION

No. 1 Capitol District Building
250 South Hotel Street, Suite 508
P.O. Box 2359
Honolulu, Hawaii 96804
Telephone: (808) 587-3830

Written Statement of

Karl Fooks
President
Hawaii Strategic Development Corporation

before the
HOUSE COMMITTEE ON FINANCE
February 25, 2011
11:00 AM
State Capitol, Conference Room 308

In consideration of
HB 797 RELATING TO TAXATION

Chair Oshiro, Vice Chair Lee and Members of the Committee on Finance:

The Hawaii Strategic Development Corporation (HSDC) opposes HB 797, which extends the limitations on taxpayers' ability to claim the full amount of the high technology business investment tax credit they earned by investing capital in Hawaii-based high technology business.

The high technology business investment tax credit was an incentive offered to investors to invest capital in Hawaii-based high technology businesses. Investors had to first invest their capital in a qualified business and then claim the credit over a five-year period. As the high technology business investment tax credit sunset at the end of calendar year 2010, HB 797 will affect tax credits already earned by investors for investments made in previous years: it effectively changes the rules in the middle of the game. In fact, this bill changes the rules that were themselves a result of changing the rules in legislation enacted previously.

Continually retroactively changing the economic contract the State of Hawaii offered to investors to attract their investment capital will only reinforce Hawaii's reputation as an unattractive investment destination. This is the very problem the high technology business investment tax credit was supposed to address: the State committed nearly $1.7 billion over the last 10 years to attract investment capital to the state under this tax credit program. For innovative Hawaii businesses to start-up, expand and create high-wage opportunities for Hawaii residents, they require access to investment capital. This bill discourages investment in Hawaii businesses and will encourage Hawaii entrepreneurs to locate their businesses elsewhere.

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

HTDC Cultivating Hawaii's tech sector
HIGH TECHNOLOGY DEVELOPMENT CORPORATION

Written Statement of
YUKA NAGASHIMA
Executive Director & CEO
High Technology Development Corporation
before the
HOUSE COMMITTEE ON FINANCE
February 25, 2011
11:00 AM
State Capitol, Conference Room 308

In consideration of
HB 797 RELATING TO TAXATION

Chair Oshiro, Vice Chair Lee and Members of the Committee on Finance:

The High Technology Development Corporation (HTDC) strongly opposes HB 797, which extends the limitations on taxpayers' ability to claim the full amount of the high technology business investment tax credit they earned by investing capital in Hawaii-based high technology business.

HTDC's main concern with this bill is that it is trying to amend a piece of previous legislation, which already restricted the benefits of Act 215, which amended Act 221. While HTDC realizes the tight fiscal environment, the amount of liabilities to the State minimized by this measure is insignificant compared to the damage in the State's credibility it would cause. The State of Hawaii already suffers from poor perception as an unfriendly place to do business for several reasons. Retroactively changing the rules of the game is not something investors expect or take kindly. Their response will be reflected in the market for Hawaii's State tax credits (e.g., Affordable Housing tax credit, future tax credit sale as a financial mechanism to fund other State initiatives, etc.).

Continually retroactively changing the economic contract the State of Hawaii offered to investors to attract their investment capital will only reinforce Hawaii's reputation as an unattractive investment destination. It is unfair to the existing investors, and sabotages future State initiatives.

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

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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 claim of adjusted tax credits

BILL NUMBER: HB 797

INTRODUCED BY: Say

BRIEF SUMMARY: Amends HRS section 235-109.5(a) to extend the deadline for which credits may be claimed at a reduced amount from January 1, 2011 to January 1, 2013.

EFFECTIVE DATE: Tax years beginning after December 31, 2010

STAFF COMMENTS: The legislature by Act 178, SLH 2009, provided that for tax years beginning on 1/1/09 and ending on 12/31/10, any tax credit claimed under HRS sections 235-110.51, 235-110.9, 241-4.8 or 431-:7-209, shall not exceed 80% of a taxpayer's tax liability for the taxable year in which the credit is claimed and any tax credit claimed shall not result in any credit carryovers for any investments made on or after 5/1/09. While this provision lapses on 12/31/10, this measure extends this provision to 1/1/13. These high technology tax credits were adopted by the legislature by Act 178, SLH 1999, and Act 221, SLH 2001, 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 to locate in the state. Due to the financial crisis that the state government is experiencing, this measure proposes to alleviate the drain of state revenue due to these tax credits.

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 a few years ago 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.

Given the generosity of the tax credit to begin with, it does not seem unfair to ask taxpayers who availed themselves of the generous benefit to pay at least something into the pot during these difficult economic times. Given that other taxpayers who did not dance to the tune of the high tech incentives are now faced with proposals to increase their burden of taxes, it would seem only fair that those so favored pay something. Limiting the amount of the taxpayer's liability that can be offset by the tax credit does not seem unduly burdensome.

Digested 2/24/11