HB2626 HD2

Establishes a nonrefundable income tax credit for taxpayers who incur certain expenses for manufacturing products in Hawaii. Applies to taxable years beginning after December 31, 2014. Repeals on January 1, 2023. Effective January 20, 2050. (HB2626 HD2)

NEIL ABERCROMBIE
GOVERNOR

RICHARD C. LIM
DIRECTOR

MARY ALICE EVANS
DEPUTY DIRECTOR

DEPARTMENT OF BUSINESS, ECONOMIC DEVELOPMENT & TOURISM

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Statement of
RICHARD C. LIM
Director
Department of Business, Economic Development, and Tourism
before the

SENATE COMMITTEE ON ECONOMIC DEVELOPMENT, GOVERNMENT OPERATIONS AND HOUSING

Monday, March 10, 2014
2:45 p.m.
State Capitol, Conference Room 16
In consideration of

HB 2626, HD2
RELATING TO TAXATION.

Chair Dela Cruz, Vice Chair Slom, and Members of the Committee.

Thank you for the opportunity to testify on HB 2626 HD2, a bill that establishes an income tax credit for taxpayers who incur certain expenses for manufacturing products in Hawaii.

DBEDT supports this bill, but notes that it does not currently have the staffing or funding to fulfill the obligation in Section 235(e) that requires DBEDT to "maintain records" for each taxpayer, "verify" the amounts, and "certify" the amount of the tax credits.

DBEDT prefers the approach taken in Act 270 (13) to provide the Legislature with information on the utilization of the tax credits to create jobs.

DBEDT defers to the Department of Taxation on the tax implications and fiscal impacts on their programs in carrying out this initiative.

Thank you for the opportunity to comment.

HSDC HAWAII STRATEGIC DEVELOPMENT CORPORATION

Written Statement of

KARL FOOKS
President
Hawaii Strategic Development Corporation

Before the
COMMITTEE ON ECONOMIC DEVELOPMENT, GOVERNMENT OPERATIONS & HOUSING

March 10, 2014
2:45 PM
State Capitol, Conference Room 16

In consideration of
HB 2626 HD 2 RELATING TO TAXATION

Chair Dela Cruz, Vice Chair Slom, and Members of the Committee on Economic Development, Government Operations & Housing:

The Hawaii Strategic Development Corporation (HSDC) respectfully submits testimony in support of the intent of HB 2626 HD 2.

A vibrant manufacturing sector will be important to grow a viable and sustainable export economy. HSDC supports efforts that can help to develop Hawaii's manufacturing capacity.

We recommend the Legislature consider a comprehensive strategy to link support for the manufacturing sector with entrepreneurial development and investment capital to stimulate an entire ecosystem that supports the goal of this legislation of building a globally competitive manufacturing sector.

Thank you for the opportunity to provide testimony.

HTDC Cultivating Hawaii's tech sector
HIGH TECHNOLOGY DEVELOPMENT CORPORATION

Written Statement of
ROBBIE MELTON
Executive Director & CEO
High Technology Development Corporation
before the
COMMITTEE ON ECONOMIC DEVELOPMENT, GOVERNMENT OPERATIONS AND HOUSING
Monday, March 10, 2014
2:45 p.m.
State Capitol, Conference Room 016
In consideration of

HB 2626 HD2 RELATING TO TAXATION.

Chair Dela Cruz, Vice Chair Slom, and Members of the Committee on Economic Development, Government Operations and Housing.

The High Technology Development Corporation (HTDC) **supports** HB 2626 HD2 relating to Taxation. HTDC supports the growth of manufacturing in Hawaii and this bill has the potential to financially benefit businesses and incentivize others to manufacture products in Hawaii. Hawaii needs more "Made in Hawaii" to decrease our dependence on imported goods as well as export revenues.

HTDC defers to DBEDT and DOTAX on the reporting and filing requirements included in the bill. HTDC respectfully requests the correction of the defective effective date.

Thank you for the opportunity to offer these comments.

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NEIL ABERCROMBIE
GOVERNOR

SHAN TSUTSUI
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STATE OF HAWAII
DEPARTMENT OF TAXATION
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PHONE NO: (808) 587-1530
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To: The Honorable Donovan M. Dela Cruz, Chair
and Members of the Senate Committee on Economic Development, Government Operations and Housing

Date: Monday, March 10, 2014
Time: 2:45 p.m.
Place: Conference Room 016, State Capitol

From: Frederick D. Pablo, Director
Department of Taxation

Re: H.B. No. 2626, H.D. 2, Relating to Taxation

The Department of Taxation (Department) shares the following comments and recommendations regarding H.B. 2626, H.D. 2, for your consideration. The Department defers to the Department of Business, Economic Development, and Tourism regarding the certification and reporting requirements proposed under subsection (e).

H.B. 2626, H.D. 2, establishes a non-refundable income tax credit for taxpayers who incur certain expenses for manufacturing products in Hawaii. Specifically, the measure would provide a non-refundable tax credit of twenty percent of the costs incurred to purchase equipment to be used in the manufacture of tangible personal property in the State, as well as costs incurred to train employees in the manufacturing process. This measure would be repealed on January 1, 2023 and has a defective effective date of January 20, 2050.

The Department notes that there is no requirement in this measure that the equipment actually be installed and put to use in order to qualify for the credit. In other words, both the seller of equipment and machinery which would be used to manufacture tangible personal property in the State and the taxpayer actually placing the equipment in service, would be eligible for the credit. The Department recommends that this issue be clarified, as it does not seem to align with the purpose of the bill.

In addition, the measure contains no time frame in which the equipment must be placed in service. The Department recommends that such a time frame be included, to prevent a taxpayer from purchasing equipment to resell at a later date. The Department recommends that "qualified manufacturing costs" be defined as follows:

"Qualified manufacturing costs" means expenditures for:

(1) Costs incurred to purchase equipment to be used by the taxpayer in manufacturing tangible personal property in the State and which is placed in service within one year after the date of purchase; and

(2) Costs incurred to train employees to manufacture tangible personal property in the State."

Finally, the Department notes that some jurisdictions consider electricity to be tangible personal property. Historically, the Department has not deemed electricity to be tangible personal property. However, to avoid future potential audit and enforcement problems regarding whether electricity generation is an eligible activity, and in light of the existing Renewable Energy Technologies Income Tax Credit at Hawaii Revised Statutes section 235-12.5, and the tax credit for energy storage being considered by the Legislature this year, the Department suggests that a provision be added to specifically exclude costs related to the production of electricity. The following language should be added after the last sentence in subsection (a) to address the issue:

Provided that qualified manufacturing costs shall not include any costs related to the production of electricity.

Thank you for the opportunity to provide comments.

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, Manufacturing tax credit

BILL NUMBER: HB 2626, HD-2

INTRODUCED BY: House Committee on Finance

EXECUTIVE SUMMARY: Establishes an income tax credit of 20% of qualified manufacturing costs incurred in a table year, not to exceed $200,000. The adoption of this credit would result in a subsidy of state funds. Lawmakers should consider the criteria established by the 2001-2003 Tax Review Commission (discussed below) before enacting this or any other new business incentive that operates through the tax system.

Difference with SB 3082, SD-2: SB 3082, SD-2 contains unspecified tax credit and cap amounts.

BRIEF SUMMARY: Adds a new section to HRS chapter 235 to allow taxpayers to claim an income tax credit of 20% of the qualified manufacturing costs incurred in a taxable year provided that the total credit claimed per taxpayer shall not exceed $200,000.

In the case of a partnership, S corporation, estate, or trust the tax credit allowable is for qualified manufacturing costs incurred by the entity for the taxable year with distribution and share of the credit to be determined by section 704(b) of the Internal Revenue Code. If a deduction is taken under IRC section 179 (with respect to election to expense depreciable business assets), no credit shall be allowed for that portion for which the deduction is taken. The basis of eligible property for depreciation or accelerated cost recovery system purposes for state income tax purposes shall be reduced by the amount of credits allowable and claimed.

Credits in excess of a taxpayer's income tax liability shall be applied to subsequent tax liability until exhausted. Claims for the credit, including any amended claims, must be filed on or before the end of the twelfth month following the close of the taxable year. The director of taxation may adopt rules pursuant to HRS chapter 91 and prepare the necessary forms to claim the credit and may require proof of the claim for the credit. Requires the director of business, economic development, and tourism (DBEDT) to: (1) maintain records of the total amount of the qualified manufacturing costs for each taxpayer claiming the credit; (2) verify the amount of the qualified manufacturing costs claimed; (3) total all qualified manufacturing costs claimed; and (4) certify the total amount of the tax credit for each taxable year. DBEDT shall issue a certificate to the taxpayer verifying the qualified manufacturing costs and the credit amount certified for each taxable year. Requires the taxpayer to file the certificate with the taxpayer's tax return with the department of taxation.

Defines "qualified manufacturing costs" as costs incurred to: (1) purchase equipment to be used in manufacturing tangible personal property in the state; and (2) train employees to manufacture tangible personal property in the state.

This act shall be repealed on January 1, 2023.

EFFECTIVE DATE: January 20, 2050; applicable to tax years beginning after December 31, 2014

STAFF COMMENTS: It appears that this measure is intended to provide an incentive in the form of an income tax credit to encourage manufacturing in the state. It should be noted that tax credits generally are designed to reduce the tax burdens of certain groups by refunding a portion of taxes paid on purchases of essential items and services. This credit of 20% of qualified manufacturing costs amounts to nothing more than a subsidy of state funds as there is no obvious undue burden of taxes.

It should be remembered that the 2001-2003 Tax Review Commission set forth recommended requirements for new tax incentives such as this one:

(i) *Cost-benefit studies*. Cost-benefit studies should be required prior to inaugurating new or revised tax credit programs. Policy makers should use only those programs with quantifiable and demonstrable benefits over costs. Such costs and benefits should not only look at fiscal and economic effects, but should examine social ones as well.

(ii) *Periodic evaluations* of all tax incentive programs should be required.

(iii) *Truth and disclosure reporting* separate and apart from a taxpayer's tax returns should generally be required of all taxpayers benefitting from tax incentive programs, making public all aspects of these subsidies for private investment.

(iv) *Strategic planning*. Embed tax incentives in strategic plans, leveraging as much of the State's scarce resources as possible. Rather than promoting diverse incentives in search of a cohesive strategy, the State should employ only incentives that make strategic sense.

(v) *Public participation*. Encourage public participation in and comment on tax incentive use to foster public accountability. There should at least be as much public discussion over generous multi-million dollar business incentive tax credits as there is over $50,000 renovations to school libraries.

(vi) *Sunset provisions* should be required to ensure that the above processes will be implemented before an incentive can be extended. It should be demonstrated to the Legislature that the targeted benefit to the State was in fact received, what the tax cost of that benefit was, and whether the continuation of the tax incentive is appropriate and necessary.

(vii) *Enforcement*. Given the magnitude and the complexity of these business incentive tax credits, the small chance of audit, ambiguous statutory requirements as to what can be claimed as a credit, there must be legislative oversight of these credits. In addition, the Department of Taxation must be given sufficient resources to police these credits.

If lawmakers are inclined to enact this credit, amendments should be considered addressing the criteria set forth above.

Digested 3/8/14

Chamber *of* Commerce HAWAII
The Voice of Business

Testimony to the Senate Committee on Economic Development, Government Operations and Housing
Monday, March 10, 2014 at 2:45 P.M.
Conference Room 016, State Capitol

RE: HOUSE BILL 2626, HD2 RELATING TO TAXATION

Chair Dela Cruz, Vice Chair Slom, and Members of the Committee:

The Chamber of Commerce of Hawaii ("The Chamber") **strongly supports** and asks for some **amendments** on HB 2626, HD2 Relating to Taxation.

The Chamber is the largest business organization in Hawaii, representing over 1,000 businesses. Approximately 80% of our members are small businesses with less than 20 employees. As the "Voice of Business" in Hawaii, the organization works on behalf of members and the entire business community to improve the state's economic climate and to foster positive action on issues of common concern.

The Chamber supports this bill as part of its economic development package. There are approximately 1,000 active manufacturers in the state that employ almost 17,000 people at an average compensation rate of $42,896 or over $6,000 more than the average private non-farm employee. Manufacturers helped Hawaii's economy by contributing nearly $570 million in manufactured goods exported in 2012.

The bill gives a 20% tax credit to companies on their expenditures for manufacturing equipment and the training of their employees. We believe that this credit will help fuel manufacturing in Hawaii to grow and provide more products for both local consumption and export. There is movement to manufacture more back in the U.S. At the same time, Hawaii still has some competitive disadvantages. This credit will help companies in Hawaii to start or grow their operations.

According to the National Association of Manufacturers, every new manufacturing job created adds another 1.6 jobs to the local service economy, and for every dollar in manufacturing sales, another $1.34 is added to the economy. Investments in manufacturing have a stronger impact than investments in most other economic sectors.

While we understand the Department of Taxation's concern over double dipping, we ask that the double dipping provision **not** apply for businesses planning to use the tax benefits of the Enterprise Zone Program. Many businesses utilize this program to start or help grow their business. While there may be some overlap with the manufacturing credit in this bill, the manufacturing credit is an investment credit for equipment and training, which for many will be a onetime expense. The Enterprise Zone Program is to attract and support businesses who invest in rural or depressed areas and is based on operational income. Limiting businesses to one tax program may hamper efforts to support manufacturing especially on the neighbor islands and certain rural parts of Oahu. Therefore we ask that the bill be amended to allow companies to utilize both tax programs. Also we would appreciate language to make the credit refundable.

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

HAWAI'I FARM BUREAU

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March 10, 2014

HEARING BEFORE THE
SENATE COMMITTEE ON ECONOMIC DEVELOPMENT, GOVERNMENT OPERATIONS AND HOUSING

TESTIMONY ON HB 2626, HD2
RELATING TO TAXATION

Room 016
2:45 PM

Aloha Chair Dela Cruz, Vice Chair Slom, and Members of the Committee:

I am Christopher Manfredi, President of the Hawaii Farm Bureau Federation (HFB). Organized since 1948, the HFB is comprised of 1,832 farm family members statewide, and serves as Hawaii's voice of agriculture to protect, advocate and advance the social, economic and educational interest of our diverse agricultural community.

HFB supports HB 2626, HD2, which is part of the Chamber of Commerce's economic development package. There are approximately 1000 active manufacturers in the state that employ almost 17,000 people at an average compensation rate of $42,896 or over $6,000 more than the average private non-farm employee. Manufacturers helped Hawaii's economy by contributing nearly $570 million in manufactured goods exported in 2012.

The bill gives a 20% tax credit to companies on their expenditures for manufacturing equipment and the training of their employees. We believe that this credit will help fuel manufacturing in Hawaii to grow and provide more products for both local consumption and export. There is movement to begin to manufacture more back in the U.S. At the same time Hawaii still has some competitive disadvantages. This credit will help companies in Hawaii to start or grow their operations.

According to the National Association of Manufacturers, every new manufacturing job created adds another 1.6 jobs to the local service economy, and for every dollar in manufacturing sales, another $1.34 is added to the economy. Investments in manufacturing have a stronger impact than investments most other economic sector. This is a wise investment for Hawaii.

Please support HB 2626, HD2.

Thank you.

HFIA
HAWAII FOOD INDUSTRY ASSOCIATION

Executive Officers:
Stanley Brown, ConAgra Foods - Chairperson
John Schilf, RSM Hawaii - Vice Chair
Derek Kurisu, KTA Superstores - Treasurer
Lisa DeCoito, Aloha Petroleum - Secretary
Lauren Zirbel, Executive Director

1050 Bishop St. PMB 235
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TO:
SENATE COMMITTEE ON ECONOMIC DEVELOPMENT, GOVERNEMNT OPERATIONS, AND HOUSING
Senator Dela Cruz, Chair
Senator Slom, Vice Chair

FROM: HAWAII FOOD INDUSTRY ASSOCIATION
Lauren Zirbel, Executive Director

DATE: March 10, 2014
TIME: 2:45pm
PLACE: Conference Room 16

RE: HB 2626

Position: Support

The Hawaii Food Industry Association is comprised of two hundred member companies representing retailers, suppliers, producers and distributors of food and beverage related products in the State of Hawaii.

The tax credit proposed in this bill would help grow and diversify our economy, keep more dollars in Hawaii, decrease our dependence on imports, and grow and strengthen the Made in Hawaii brand.

Research has shown that a diversified economy and a business friendly tax climate are both key factors in keeping unemployment low. This bill could allow current manufacturers in our state to grow their businesses and can open the door for even more production here in Hawaii. This means more jobs and a stronger economy for the entire state.

Increasing manufacturing will also mean we are less reliant on imported goods. We currently import over 90% of the products we use here in the state. This situation leaves us vulnerable to any supply chain interruptions, adds shipping cost to almost all goods, and sends millions of dollars a year out of the state. Importing less and making more can have wide reaching positive impacts for everyone from the manufacturers to the consumers.

This bill will also open the door for more products to earn the distinction of being Made in Hawaii. The products we currently make here in the state have a worldwide reputation for quality and excellence. There is strong demand both in and out of the state for more products of that high caliber, and this bill can help grow our manufacturing industry to meet that demand.
For these reasons we ask that you please vote yes on this measure.

Thank you for the opportunity to testify.

Meadow Gold Dairies

HB2626hd2, Relating to Taxation
Senate EGH Hearing
Monday, March 10, 2014
2:45 pm – Room 16

Written Testimony By: Glenn Muranaka

Position: Support

Chair Dela Cruz and Members of the Senate EGH Committee:

My name is Glenn Muranaka, President and General Manager of Meadow Gold Dairies. Our company has been in Hawaii since 1897—117 years, providing Hawaii consumers with a variety of milk products and juices. Meadow Gold's long history has not come without effort. We continually adapt to our customers' and consumers' ever-changing needs, and we constantly evolve along with our industry, our community and our market. Over the years, this has required that we struggle, tighten our belts, innovate and work extremely hard, making us a better company in the process. The foundation of this work rests with the 330 employees that are committed to providing superior quality products.

I support this bill as part of the Chamber of Commerce's economic development package. There are approximately 1000 active manufacturers in the state that employ almost 17,000 people at an average compensation rate of $42,896 or over $6,000 more than the average private non-farm employee. Manufacturers helped Hawaii's economy by contributing nearly $570 million in manufactured goods exported in 2012.

The bill gives a 20% tax credit, not to exceed $200,000, to companies on their expenditures for manufacturing equipment and the training of their employees. We believe that this credit will help fuel manufacturing in Hawaii to grow and provide more products for both local consumption and export. There is movement to begin to manufacture more back in the U.S. At the same time Hawaii still has some competitive disadvantages. This credit will help companies in Hawaii to start or grow their operations.

Your support of this measure is appreciated with amendments made in HD1, which allow for refundable tax credits. Thank you for the opportunity to submit testimony. I can be reached at 944-5911 if there are any questions.

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KYD, Inc. dba k. yamada distributors
An independent leader in packaging and wholesale distribution
P.O. BOX 29669, Honolulu, Hawaii 96820 Phone: (808) 836-3221 Fax: (808) 833-8995

HB2626hd2, Relating to Taxation
Senate EGH Committee – Monday, March 10, 2014
2:45 pm
Room 16
Written Testimony by: Dexter Yamada
Position: Support

Chair Dela Cruz and Members of the Senate EGH Committee:

I am Dexter Yamada, President of KYD, Inc. dba: K. Yamada Distributors. KYD, Inc. is a local family run business that originated in the 1940's as a florist and florist supply distributor, and in 1958, evolved into a packaging company. Today, KYD, Inc and its sister company, Hawaii Foam Products, LLC, employ about 100 employees and contribute to Hawaii's economy through taxes and payroll based on $35 million annual revenue. Our companies manufacture packaging materials such as food-grade EPS (Expanded Polystyrene) food containers, and distribute a variety of supplies, to include compostable containers, for food processors, food establishments, supermarkets, hotels hospitals and other institutions.

We appreciate this measure that supports Hawaii's manufacturing industry. Locally manufactured products contribute to import replacement, and help with local job creation. The temporary tax credit will encourage companies to invest in equipment purchases and train employees to manufacture locally made products. This in turn, lends to greater efficiency and reduction in the cost of products to customers. Your consideration of the HD1 draft which includes the refundable tax credit is appreciated.

Thank you for the opportunity to testify.