DAVID Y. IGE
GOVERNOR

SHAN TSUTSUI
LT. GOVERNOR

MARIA E. ZIELINSKI
DIRECTOR OF TAXATION

JOSEPH K. KIM
DEPUTY DIRECTOR

STATE OF HAWAII
DEPARTMENT OF TAXATION
P.O. BOX 259
HONOLULU, HAWAII 96809
PHONE NO: (808) 587-1540
FAX NO: (808) 587-1560

To: The Honorable Sylvia Luke, Chair
and Members of the House Committee on Finance

Date: March 2, 2016
Time: 11:00 A.M.
Place: Conference Room 308, State Capitol

From: Maria E. Zielinski, Director
Department of Taxation

Re: H.B. 1689, H.D. 1, Relating to Taxation.

The Department of Taxation (Department) appreciates the intent of H.B. 1689, H.D. 1, and provides the following comments for your consideration.

H.B. 1689, H.D. 1 amends the ethanol facility tax credit at section 235-110.3, Hawaii Revised Statutes, to apply to facilities that produce renewable fuels. The definition of renewable fuels include a variety of fuel products produced from "renewable feedstocks," which are defined. The amendments apply to taxable years beginning after December 31, 2015.

First, the Department notes that the suggested amendment to Paragraph (a)(4) is confusing. The paragraph reads "No taxpayer that claims the credit under this section shall use the investment upon which the claim under this section is made to claim any other tax credit under this chapter for the taxable year." The Department suggests clarification of this provision as the credit is limited by the "investment" amount, but the credit is not calculated on it.

Second, the Department notes that the definition provided for "qualified renewable fuels" requires additional certification for fuels produced from feedstocks transported more than five hundred miles using a fossil fuel. This addition is likely impermissible under the Commerce Clause of the United States Constitution, which typically does not allow differential tax treatment for products originating in different states. The Department defers to the Department of the Attorney General for an analysis of the constitutionality of this provision.

Third, the Department notes that this tax credit is certified by the Department of Business, Economic Development, and Tourism (DBEDT). The certification requirements are contained in subsection (d) of section 235-110.3, HRS, and is not edited by this measure. The Department defers to DBEDT regarding its ability to make the necessary certifications, but requests that the certification provisions in this tax credit remain, as the Department is unable to make the technical judgments necessary in administering this tax credit.

Finally, the Department notes that this tax credit is refundable. As a general matter, the Department recommends that tax credits be non-refundable because refundable credits are more prone to wrongful claims and abuse.

Thank you for the opportunity to provide comments.

DAVID Y. IGE
GOVERNOR

LUIS P. SALAVERIA
DIRECTOR

MARY ALICE EVANS
DEPUTY DIRECTOR

DEPARTMENT OF BUSINESS, ECONOMIC DEVELOPMENT & TOURISM

No. 1 Capitol District Building, 250 South Hotel Street, 5th Floor, Honolulu, Hawaii 96813
Mailing Address: P.O. Box 2359, Honolulu, Hawaii 96804
Web site: www.hawaii.gov/dbedt
Telephone: (808) 586-2355
Fax: (808) 586-2377

Statement of
LUIS P. SALAVERIA
Director
Department of Business, Economic Development, and Tourism
before the
HOUSE COMMITTEE ON FINANCE

Wednesday, March 2, 2016
11:00 a.m.
State Capitol, Conference Room 308

in consideration of
HB 1689, HD 1
RELATING TO TAXATION.

Chair Luke, Vice Chair Nishimoto, and Members of the Committee.

The Department of Business, Economic Development & Tourism (DBEDT) offers comments on HB 1689, HD1, which establishes a renewable fuels facility tax credit (TC) and repeals the ethanol facility tax credit. The HD1 added a definition of “qualifying renewable fuels.”

DBEDT recognizes the value of the State of Hawaii in becoming more self-sufficient in its energy supply.

With regards to the State’s policy of diversifying Hawaii’s energy portfolio, we are concerned that this bill does not provide a clear definition of how much renewable feedstock must originate from Hawaii and be used for renewable fuel production in order to qualify for the full tax credit, thus negating potential diversification of our energy portfolio with indigenous resources and leading to subsidization of non-indigenous resources. For example, a renewable fuel producer may use one percent Hawaii grown renewable feedstock and blend it with another 99 percent non-Hawaii sourced renewable feedstock and still qualify for the full tax credit under the present language of the bill. Therefore, this bill will require more clarity on the administration of the tax credit and how it will be computed, especially if a blend of renewable feedstock is allowed.

Regarding the State's policy to create an efficient market-place that benefits producers and consumers, the bill caps the available tax credit at an aggregate total of forty million gallons per year. However, the bill does not preclude a single taxpayer of a renewable fuels facility to capture the full allocation of the credit, thus concentrating the tax credit benefit with a single individual/entity and contradicting our policy of creating an efficient marketplace.

DBEDT is also concerned about its responsibilities under this bill as DBEDT lacks, and would require, funding and human resources beyond our current budget to execute our responsibilities under the bill. Responsibilities of concern to DBEDT under this bill include: the verification of actual production of the renewable fuel facilities, which would be required to revise the facilities' capacity (lines 13-20, page 9); analyzing the impact of renewable feedstock traveling over five hundred miles (reference definition of qualifying renewable fuels, pages 4-5); and the annual report to the Governor and Legislature.

DBEDT defers to the Department of Taxation on the administration of the renewable fuels production tax credit; to the Department of Budget and Finance on the fiscal impacts of this measure; and to the Department of Health on the contribution of greenhouse gas emissions requirement relative to fossil fuel transport of renewable feedstock traveling over five hundred miles.

Thank you for the opportunity to offer these comments regarding HB 1689, HD1.

TAX FOUNDATION OF HAWAII

126 Queen Street, Suite 304 Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: INCOME, Renewable Fuels Facility Tax Credit

BILL NUMBER: HB 1689, HD-1

INTRODUCED BY: House Committee on Energy & Environmental Protection.

EXECUTIVE SUMMARY: Replaces the ethanol fuels income tax credit with a renewable fuels production income tax credit to encourage the production of such fuels. A direct appropriation would be preferable as it would provide some accountability for the taxpayer funds being utilized to support this effort. Meaning, we as taxpayers know what we're getting and we know how much we're paying for it.

BRIEF SUMMARY: Amends to HRS section 235-110.3, which now defines the ethanol facility tax credit, to be retitled the renewable fuels facility tax credit. The credit shall be allowed to taxpayers producing qualifying renewable fuels for an eight-year period beginning on the date of first production.

The annual dollar amount of the credit shall be 30% of the annual nameplate capacity if it is greater than 500,000 but less than 15,000,000 gallons. The credit amount is not to exceed 100% of the total of all investments made by the taxpayer in the facility during the credit period; the facility must operate at 75% or more of its nameplate capacity on an annualized basis; and the facility must be in production on or before January 1, 2017.

No taxpayer that claims the credit shall use the investment upon which the claim for credit is made to claim any other Hawaii income tax credit for the same taxable year.

Defines "qualifying renewable fuel" as fuel created from renewable feedstocks; provided that for the purpose of the renewable fuels facility tax credit, any renewable feedstock transported more than five hundred miles using a fossil fuel can become a qualifying renewable feedstock only upon a showing to the state energy office of the department of business, economic development, and tourism that the renewable feedstock serves a legitimate public purpose for Hawaii. For the purpose of this showing, the state energy office of the department of business, economic development, and tourism shall consider the impact of such fossil fuel transportation on the State's energy security and contribution to greenhouse gas emissions.

Defines "qualifying renewable fuels production" as fuel produced or generated from renewable feedstocks. All qualifying production shall be fermented, distilled, transesterified, gasified, pyrolized, combusted, or produced by physical, chemical, biochemical, or thermochemical conversion methods at the facility.

Defines "qualifying renewable fuels production facility" as one located in Hawaii that produces or generates, directly from renewable feedstocks, fuel grade renewable fuels meeting the relevant ASTM International specifications for the particular fuel or other industry specifications for liquid or gaseous fuels, including but not limited to: (1) methanol, ethanol, or other alcohols; (2) hydrogen; (3) biodiesel or renewable diesel; (4) biogas; (5) other biofuels; or (6) renewable jet fuel or renewable gasoline.

Defines "renewable feedstocks" as (1) biomass crops; (2) agricultural residues; (3) oil crops, including but not limited to algae, canola, jatropha, palm, soybean, and sunflower; (4) sugar and starch crops, including but not limited to sugar cane and cassava; (5) other agricultural crops; (6) grease and waste cooking oil; (7) food wastes; (8) municipal solid wastes and industrial wastes; (9) water; and (10) animal residues and wastes, that can be used to generate energy.

EFFECTIVE DATE: Applies to taxable years beginning after December 31, 2015.

STAFF COMMENTS: Act 289, SLH 2000, established an investment tax credit to encourage the construction of an ethanol production facility in the state. Act 140, SLH 2004, changed the credit from an investment tax credit to a facility tax credit. This measure proposes to amend the ethanol facility tax credit to encompass facilities that produce other renewable fuels.

While the idea of providing a tax credit to encourage such activities may have been acceptable a few years ago when the economy was on a roll and advocates could point to credits like those to encourage construction and renovation activities, what lawmakers and administrators have learned in these past few years is that unbridled tax incentives, where there is no accountability or limits on how much in credits can be claimed, are irresponsible as the cost of these credits goes far beyond what was ever intended. Instead, lawmakers should consider repealing the ethanol facility credit and look for other types of alternate energy to encourage through the appropriation of a specific number of taxpayer dollars. At least lawmakers would have a better idea of what is being funded and hold the developers of these alternate forms of energy to a deliberate timetable or else lose the funds altogether. A direct appropriation would be preferable to the tax credit as it would: (1) provide some accountability for the taxpayers' funds being utilized to support this effort; and (2) not be a blank check.

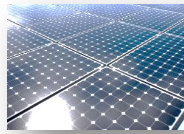
Ethanol was the panacea of yesterday; lawmakers have since learned that there are more minuses to the use of ethanol than there are pluses. Ethanol production demands more energy to produce than using a traditional petroleum product to produce the same amount of energy, and the demand for feedstock that is used to produce ethanol basically redirects that feedstock away from traditional uses, causing products derived from the feedstock to substantially increase in price. It may make sense to encourage development of other alternative fuels that will not have these issues, but doing it in open-ended fashion by way of a tax credit is an invitation to abuse.

An appropriation of taxpayer dollars for such untried and unproven technologies would be far more accountable than the tax credit as such technologies would have undergone the scrutiny of lawmakers. Providing a tax incentive is an indicator that lawmakers are unwilling to do the hard research and unwilling to impose strict discipline in the expenditure of hard-earned tax dollars. The tax incentive approach represents nothing more than a hope and a wish that some breakthrough will be made, no matter how inefficient it may be, that some alternative to fossil fuel will be found. In the meantime, those tax dollars will be wasted on some unproven folly. If this were an appropriation, taxpayers would then know who to hold accountable for the waste of those tax dollars.

This, along with numerous other proposals targeted at certain types of business activity, is truly an indictment of what everyone has known and acknowledged since before Hawaii became a state, that is, the climate imposed by government regulations and taxation makes it difficult to survive without some kind of subsidy such as tax credits from government. Once those subsidies disappear, so will the businesses. Instead of throwing out such breaks for special interests, lawmakers must endeavor to make Hawaii's business climate more welcoming and conducive to nurturing entrepreneurs.

Digested 2/29/2016

blue planet FOUNDATION



HOUSE COMMITTEE ON FINANCE
March 2, 2016, 11 A.M.
Room 308
(Testimony is 1 page long)

TESTIMONY IN SUPPORT OF HB 1689 HD1

Aloha Chair Luke, Vice Chair Nishimoto, and Committee members:

The Blue Planet Foundation supports HB 1689 HD1, expanding the eligibility for biofuel production facilities beyond ethanol. This policy—providing a biofuel facility tax credit to incentivize the needed development, construction, and operation of renewable fuel facilities—will provide greater support for Hawai'i's diverse biofuel production infrastructure.

Biofuels will likely play a major role in Hawai'i's clean energy future—particularly as a substitute for petroleum-based transportation fuels. While much of our work has been focused on renewable energy and reducing electricity use, transportation in Hawai'i (cars, trucks, ships, and planes) accounts for approximately two-thirds of the oil consumed. **In 2014, Hawai'i cars and trucks burned nearly 500 million gallons of gasoline and diesel fuel.** For a typical car, that's enough fuel to cover the distance equivalent to over 21,000 round trips to the moon. Currently, almost all of that travel burns imported fossil fuels. Transportation fuels in Hawai'i can be made from renewable resources, such as biomass in various forms, algae, and waste products. Just as importantly, these materials are available here. Hawai'i should set a clear course for a steady, incremental transition to renewable fuels including local and sustainable biofuels.

Tax incentives have proven to be an extraordinarily effective mechanism to develop a local renewable energy industry; the rooftop solar industry has grown to become an important part of the state's construction industry and is serving as a backstop in the electricity industry to ensure that consumers have options for clean energy. Tax incentive policies for renewable transportation fuels can serve the same purpose for transportation energy.

Blue Planet also asks legislators to also consider policy to require that a certain percentage (5% - 10%) of diesel fuel sold in Hawai'i be biodiesel. One of Hawai'i's entrepreneurial success stories is biodiesel, a fuel that is being locally created from recycled cooking grease and oils, and that can be substituted in place of fossil fuel-based diesel for transportation. Already, this local industry is creating enough fuel to displace 5% of transportation diesel fuel sold in the state. Blue Planet supports a mandate to blend biodiesel

info@blueplanetfoundation.org
55 Merchant Street 17th Floor • Honolulu, Hawai'i 96813 • 808-954-6142 • blueplanetfoundation.org

with all locally sold diesel fuel. This smart step will help to continue the momentum for a local industry to supply local clean energy for our transportation energy needs.

Thank you for the opportunity to testify.

TESTIMONY IN **SUPPORT**

WARREN BOLLMEIER ON BEHALF OF THE
HAWAII RENEWABLE ENERGY ALLIANCE BEFORE THE
HOUSE COMMITTEE ON FINANCE

HOUSE BILL 1689 HD1

WEDNESDAY, MARCH 2, 2016 11AM

Chair Luke, Vice Chair Nishimoto and Members of the Committee on Finance,

I am Warren Bollmeier, testifying on behalf of the Hawaii Renewable Energy Alliance (HREA). HREA is an industry-based, nonprofit corporation in Hawaii established in 1995. Our mission is to support, through education and advocacy, the use of renewables for a sustainable, energy-efficient, environmentally-friendly, economically-sound future for Hawaii. One of our goals is to support appropriate policy changes in state and local government, the Public Utilities Commission and the electric utilities to encourage increased use of renewables in Hawaii.

The purpose of this Act is to amend the existing ethanol facility income tax credit to include other renewable fuels.

HREA **strongly supports** this measure with the following comments:

1) Renewable fuels can diversify Hawaii's fuel mix, which can increase system reliability and reduce risk.
2) Intermittent Wind and Solar can be better managed with complementary firm power from renewable fuels.
3) Renewable fuels can displace oil.
4) Renewable fuels production is limited and is there are no Hawaii incentives to produce.

Recommendation: We recommend passing the measure out "as is."

Mahalo for this opportunity to testify.

46-040 Konane Place #3816, Kaneohe HI 96744 • www.http://hawaiirenewableenergy.org: 808.247.7753 •wsb@lava.net

REACH
RENEWABLE ENERGY ACTION COALITION OF HAWAII
1110 University Avenue, Suite 402
Honolulu, Hawaii 96826
Tel: (808) 371-1475
www.REACHawaii.org

Testimony of ERIK KVAM
Director of Renewable Energy Action Coalition of Hawaii
e-mail: Erik.Kvam@REACHawaii.org

In SUPPORT of HB 1689 HD 1 RELATING TO TAXATION

Before the
HOUSE COMMITTEE ON FINANCE

Wednesday, March 2, 2016 11:00 a.m.

Aloha, Chair Luke, Vice-Chair Nishimoto and members of the Committee.

My name is Erik Kvam. I am a Director of Renewable Energy Action Coalition of Hawaii (REACH). REACH is a trade association whose vision is a Hawaiian energy economy based 100% on renewable sources indigenous to Hawaii.

Hawaii is far behind in achieving its renewable goals for transportation. Transportation fuels account for about two-thirds of all the energy consumed in Hawaii. Virtually all of Hawaii's energy for transportation comes from imported fuels.

Without renewable fuel production from sources indigenous to Hawaii, Hawaii will have virtually no fuel available for critical transportation needs when imported fuels stop flowing to Hawaii.

REACH **SUPPORTS** HB 1689 HD 1 **–** creating a renewable fuels facility investment tax credit -- to encourage the development of facilities in Hawaii for the production of fuels from renewable sources indigenous to Hawaii. REACH **SUPPORTS** HB1689 HD 1, so that Hawaii has the transportation fuels it needs when imported fuels stop flowing to Hawaii.

Thank you for providing this opportunity to testify.