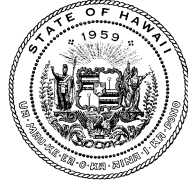


DAVID Y. IGE  
GOVERNOR

JOSH GREEN M.D.  
LT. GOVERNOR



STATE OF HAWAII  
**DEPARTMENT OF TAXATION**

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RONA M. SUZUKI  
DIRECTOR OF TAXATION

DAMIEN A. ELEFANTE  
DEPUTY DIRECTOR

To: The Honorable Ryan I. Yamane, Chair;  
The Honorable Chris Todd, Vice Chair;  
and Members of the House Committee on Water, Land, & Hawaiian Affairs

From: Rona M. Suzuki, Director  
Department of Taxation

Re: **H.B. 2716, Relating to Taxation**

Date: Wednesday, February 12, 2020

Time: 10:30 A.M.

Place: Conference Room 325, State Capitol

The Department of Taxation (Department) provides the following comments regarding H.B. 2716.

H.B. 2716 establishes the ocean sciences research tax credit up to an unstated amount. The measure is effective upon approval and applies to taxable years beginning after December 31, 2019, but not to taxable years beginning after December 31, 2025.

The Department first notes that proposed section (b) determines the credit based on the **investment** into an entity that does research that meets National American Industry Classification System (NAICS) code 541715. Substantial credit could thus be generated by simply investing in an entity, regardless of how much research is actually performed. The high technology business investment tax credit (QHTB credit) codified at section 235-110.9, Hawaii Revised Statutes (HRS), also allowed for a tax credit based on investment rather than the actual activity that the State intended to incentivize. The Department suggests amending the measure so that qualification for the credit is contingent on more than just an investment.

In addition, unlike the QHTB credit, H.B. 2716 does not require the investment to actually be at-risk. The Department suggests adding a provision to this measure specifying that the investment be at-risk. This will help to reduce any sham investments that do not effectuate the purpose of the credit.

The Department notes further that NAICS Code 541715 is very broad and therefore overlaps with several existing credits, including the ship repair industry tax credit under section 235-110.65, HRS, and the tax credit for research activities under section 235-110.91, HRS. To prevent double-dipping, the Department strongly suggests adding a new subsection to read:

(h) No other credit under this chapter shall be claimed for expenses or costs paid with an investment made into a qualified entity for which the credit was claimed under this section.

The Department also suggests clarification of the definition of “qualified entity.” As currently written, a “qualified entity” is a small business in the State of Hawaii. The term “small business” needs to be defined because the term is ambiguous and is not a defined term in chapter 235, HRS. In addition, “in the State of Hawaii” should be clarified because providing the new credit only for entities physically located in Hawaii is likely to violate the Commerce Clause of the U.S. Constitution.

Finally, the Department respectfully requests that this new credit be made available for taxable years beginning after December 31, 2020. This will prevent retroactive availability of the credit and allow sufficient time to make the necessary form and computer system modifications.

Thank you for the opportunity to provide comments.



Statement of  
**Hermann Kugeler**  
**Business Development Manager**  
**Makai Ocean Engineering, Inc.**  
before the  
**House Committee on Water, Land, & Hawaiian Affairs**  
Wednesday, February 12, 2020  
10:30am  
State Capitol, Conference Room 325  
In consideration of  
**HB2716**  
**RELATING TO TAXATION.**

Chair Yamane, Vice Chair Todd, and Members of the Committee.

Makai Ocean Engineering, Inc. **SUPPORTS HB2716, WITH AMENDMENT** that establishes the ocean sciences research tax credit. We respectfully request the following amended language:

**“BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF HAWAII:**

SECTION 1. The legislature finds that to keep our community vibrant and our economy expanding, Hawaii needs to focus on innovation sectors that will bring new dollars and high—demand jobs to Hawaii's economy. As an island state, research and development in ocean sciences is an intrinsic and essential part of our future sustainability. Supporting and encouraging more research and development in ocean and marine sciences will foster and fuel innovative ideas and promote entrepreneurship that will better position Hawaii for future economic growth and expansion. Innovation as a result of research and development contributes greatly to economic growth. It is oftentimes the catalyst for change, job creation, and a higher standard of living. Expanding Hawaii's research and development industry in ocean sciences will bring in new dollars to our State's economy and create a wide range of high—skilled, high-paying jobs for our young people so they may continue to live and work in Hawaii. Research and development in ocean sciences may be vital to Hawaii's future economic growth.

The purpose of this Act is to establish an ocean science research tax credit to foster research and development to expand and diversify Hawaii's economy.

SECTION 2. Chapter 235, Hawaii Revised Statutes, is amended by adding a new section to be appropriately designated and to read as follows:

"§235- Ocean sciences research; tax credit.

(a) There shall be allowed to each taxpayer subject to the taxes imposed by this chapter an ocean sciences research tax credit that shall be deductible from the taxpayer's net income liability, if any, imposed by this chapter.

(b) The amount of the tax credit shall be equal to per cent of the investment made into the qualified entity; Provided that:

(1) The taxpayer shall not claim any credit in any one taxable year that exceeds \$ ; provided that if the total amount of credits applied for in any particular year exceeds the aggregate amount of credits allowed for such year under this section the excess shall be treated as having been applied for in the subsequent year and shall be claimed in such year; provided further that no excess shall be allowed to be claimed after December 31, 2025; and

(2) In no event shall a taxpayer claim a credit under this section after December 31, 2025.

(c) The credit allowed under this section shall be claimed against the net income tax liability for the taxable year. If the tax credit under this section exceeds the taxpayer's income tax liability, the excess of the tax credit over liability may be used as a credit against the taxpayer's net income tax liability in subsequent years until exhausted. All claims, including amended claims, for a tax credit under this section shall be filed on or before the end of the twelfth month following the close of the taxable year for which the credit may be claimed. Failure to comply with the foregoing provision shall constitute a waiver of the right to claim the credit.

(d) The director of taxation shall prepare any forms that may be necessary to claim a credit under this section. The director may also require the taxpayer to furnish information to

ascertain the validity of the claim for credit made under this section. The director of taxation may adopt rules pursuant to chapter 91 to effectuate the purposes of this section.

(e) Any taxpayer claiming a tax credit under this section, within ninety days of the end of the calendar year in which the credit is properly claimable, shall submit the following information to the department of taxation:

(1) The amount of the eligible costs for which the tax credit may be claimed; and

(2) The qualified entity that incurred the costs. Failure to timely submit the information shall be subject to a penalty of \$5,000 per month or a fraction thereof, not to exceed \$25,000.

(f) This section shall not apply to taxable years beginning after December 31, 2025.

(g) For the purposes of this section: "Net income tax liability" means income tax liability reduced by all other credits allowed under this section.

"Qualified entity" means a small business, defined herein as fewer than 100 employees and fewer than \$50 million gross revenue per year, which has been doing business for at least five years, employing or maintaining an office in this State; provided that the activities are for the qualified purpose.

"Qualified purpose" means the principal purpose of research and development, as defined by the National American Industry Classification System code 541715, in the field of ocean sciences, and includes:

(1) The development and design of computer software for ultimate commercial sale, lease, license or to be otherwise marketed, for economic consideration. With respect to the software's development and design, the business shall have substantial control and retain substantial rights to the resulting intellectual property, including but not limited to those from SBIR data rights, Patent Rights, or Trademark rights..



(2) The development of subsea, maritime, or naval hardware for ultimate commercial sale, lease, license or to be otherwise marketed, for economic consideration. With respect to the hardware's development and design, the business shall have substantial control and retain substantial rights to the resulting intellectual property, including but not limited to those from SBIR data rights, Patent Rights, or Trademark rights.

(h) No other credit under this chapter shall be claimed for expenses or costs paid with an investment made into a qualified entity for which the credit was claimed under this section.

SECTION 3. New statutory material is underscored.

SECTION 4. This Act, upon its approval, shall apply to taxable years beginning after December 31, 2020.”

This tax credit would attract local investment in ocean science companies like Makai, and allow our business and the rest of the industry to grow. Like the tech giants in the Bay Area of California that grew from investment capital, this tax credit would assist Hawaii in meeting its potential and become the leader in ocean science research and development.

This is why we **SUPPORT HB2716** with the amendment included above, which would establish the ocean science research tax credit, and increase investment in Hawaii's ocean science industry. Not only would this tax credit increase investments in local companies by Hawaii residents, it would enable the ocean sciences industry in Hawaii to gain investment capital that will allow the companies to grow and provide more highly-skilled professional jobs for our keiki here at home.

Thank you for the opportunity to offer these comments.



# NATURAL ENERGY LABORATORY OF HAWAII AUTHORITY

An Authority of the State of Hawaii attached to the Department of Business, Economic Development & Tourism

Statement of  
**Gregory P. Barbour**  
Executive Director

**LATE**

Natural Energy Laboratory of Hawaii Authority  
before the

## HOUSE COMMITTEE ON WATER, LAND AND HAWAIIAN AFFAIRS

Wednesday, February 12, 2020  
10:30 am  
State Capitol, Conference Room 325

in consideration of  
**H.B. 2716**  
**RELATING TO TAXATION.**

The Natural Energy Laboratory of Hawaii Authority (NELHA) supports the intent and is pleased to comment on H.B. 2716 which would create an income tax credit for Hawaii businesses whose principal purpose is research and development in the field of ocean sciences for at least five years. This makes good business sense as Hawaii is a large ocean state and offers comparative advantages for businesses in this field.

NELHA administers the 900-acre Hawaii Ocean Science and Technology Park (HOST Park) in Kailua-Kona on the Island of Hawaii. Last year we created, with the Legislative support, an aquaculture accelerator operated by HATCH focused on global innovation for technologies in

ocean science. This accelerator has been very successful and recently completed its first cohort of 13 companies. We are in discussions regarding new leases at HOST Park with two of the companies from the HATCH accelerator and one company in a similar field which just completed the Elemental Accelerator. In this regard, providing tax credits for these types of businesses will assist us in our “investment attraction” mission for the State of Hawaii economic development programs and grow our economy.

The policy position is from NELHA which is from an economic development position and does not take into consideration the tax, fiscal and revenue policy, as it relates to the State of Hawaii, for that we defer to the Departments of Taxation and Budget and Finance.

Thank you for the opportunity to offer these comments.

**HB-2716**

Submitted on: 2/11/2020 10:12:28 PM

Testimony for WLH on 2/12/2020 10:30:00 AM



<b>Submitted By</b>	<b>Organization</b>	<b>Testifier Position</b>	<b>Present at Hearing</b>
Ann Chung	Individual	Support	Yes

Comments:

I strongly support HB2716. There are many companies in Hawaii doing great research and engineering , creating high-paying, high-skilled jobs, and bringing in significant amounts of federal funding. Research and engineering can be a vital part of diversifying and growing our economy. As an island state, it makes clear sense to support these companies working in the ocean sciences field. Ocean sciences are an intrinsic and meaningful part of the State. Innovation as a result of research and development contributes greatly to our economic growth and is a catalyst for job creation and higher standards of living for our young people. I urge you to pass this bill.