



Written Statement of
Len Higashi
Executive Director
Hawaii Technology Development Corporation
before the
Senate Committee On Energy, Economic Development & Tourism
Thursday, February 9, 2023
1:03 p.m.
Conference Room 229 & Videoconference

In consideration of
SB951
RELATING TO THE TAX CREDIT FOR RESEARCH ACTIVITIES.

Chair DeCoite, Vice Chair Wakai, and Members of the Committee.

The Hawai'i Technology Development Corporation (HTDC) **supports** SB951 that adds a cap for the amount of tax credits for research activities that an eligible taxpayer and the taxpayer's related entities may receive per taxable year; consolidates the survey and certification requirements for tax credits for research activities; amends the annual aggregate cap on tax credits for research activities that the Department of Business, Economic Development, and Tourism (DBEDT) may certify; and requires certification of the tax credits for research activities on a first-come, first-served basis to be based on the date that a complete application is received, subject to certain conditions; takes effect on 7/1/2023 and applies to taxable years beginning after 12/31/2022.

HTDC supports initiatives aimed at growing tech and innovation jobs. Last year, HTDC assisted DBEDT with the online applications for the certification. Last year, the entire \$5 million cap was claimed in the first **23 seconds** after the applications opened. HTDC suggests this bill be coordinated with the Administration's bill SB1288. SB951 includes language that increases the cap per entity and the total amount available.

HTDC supports this bill provided it does not supplant the priorities of the administration. Thank you for the opportunity to offer these comments

JOSH GREEN M.D.
GOVERNOR

SYLVIA LUKE
LT. GOVERNOR



STATE OF HAWAII
DEPARTMENT OF TAXATION

Ka 'Oihana 'Auhau
P.O. BOX 259

HONOLULU, HAWAII 96809
PHONE NO: (808) 587-1540
FAX NO: (808) 587-1560

GARY S. SUGANUMA
DIRECTOR

KRISTEN M.R. SAKAMOTO
DEPUTY DIRECTOR

**TESTIMONY OF
GARY S. SUGANUMA, DIRECTOR OF TAXATION**

TESTIMONY ON THE FOLLOWING MEASURE:

S.B. No. 951, Relating to the Tax Credit for Research Activities

BEFORE THE:

Senate Committee on Energy, Economic Development, and Tourism

DATE: Thursday, February 9, 2023

TIME: 1:03 p.m.

LOCATION: State Capitol, Room 229

Chair DeCoite, Vice-Chair Wakai, and Members of the Committee:

The Department of Taxation ("Department") offers the following comments regarding S.B. 951 for your consideration.

S.B. 951 seeks to amend section 235-110.91, Hawaii Revised Statutes (HRS) relating to the tax credit for research activities, by: (1) imposing a cap of \$2,500,000 that an eligible taxpayer and the taxpayer's related entities may receive per taxable year; (2) changing the deadline that the taxpayer must provide a certified statement to the Department of Business, Economic, Development, and Tourism (DBEDT) from March 31 of each year to the last day of the third month following the end of the taxable year; (3) expanding the required data that a qualified high technology business must submit to DBEDT; (4) clarifying that the certification is determined on a first-come, first-served basis and is based on the date that the complete application is received; and (5) amending the aggregate cap from \$5,000,000 per taxable year to \$15,000,000 per calendar year.

The measure is effective on July 1, 2023 and applies to taxable years beginning after December 31, 2022.

First, the Department notes that the measure changes the time for certification from March 31 after the end of the calendar year in which research was conducted to

the last day of the third month following the close of the taxable year in which research was conducted. Some taxpayers are fiscal year filers, with the end of the tax year varying. Because of the aggregate cap, this change could result in some taxpayers having a substantial advantage or disadvantage in obtaining the credit, depending on when their fiscal year ends. The Department suggests deleting this amendment.

Second, the Department notes that that the taxpayer submission deadline in subsection (d) may be read to conflict with subsection (f). Subsection (f) refers to the aggregate cap and certifications in terms of a calendar year. As such, subsection (d) should also be set in terms of a calendar year so that no taxpayer has an advantage based on their specific tax year end date. The Department strongly suggests that the term “taxable year” on page 3, line 13, be replaced with “calendar year.”

Third, to prevent the credit from being claimed on research that has been funded by tax-exempt receipts such as a grant, the Department suggests that subsection (b) be amended to read as follows:

(b) All references to Internal Revenue Code sections within sections 41 and 280C(c) of the Internal Revenue Code shall be operative for purposes of this section; provided that references to the base amount in section 41 of the Internal Revenue Code shall not apply, and credit for all qualified research expenses may be taken without regard to the amount of expenses for previous years. In determining the allowable credit, research funded by any grant, forgivable loan, or other amounts not included in gross income for purposes of this chapter shall not be eligible research.

Finally, the Department recommends amending the effective date of the bill to apply to qualified expenses incurred after December 31, 2023.

Thank you for the opportunity to provide comments on this measure.



Written Statement of
MR. MATTHEW SULLIVAN
DIRECTOR OF PRODUCT, OCEANIT

Before the
SENATE COMMITTEE ON ECONOMIC DEVELOPMENT AND TOURISM

Thursday, February 9, 2023, 1:03 p.m.
State Capitol, Conference Room 229 & Videoconference

In Support and Requested Changes to
SB951 RELATING TO TAX CREDIT FOR RESEARCH ACTIVITIES

To: Senator Lynn DeCoite, Chair, Senator Glenn Wakai, Vice Chair and Members of the Committee

From: Mr. Matthew Sullivan, Director of Product

Re: Testimony in Support and Requested Changes to SB951

Honorable Chair, Vice-Chair and Committee Members: Thank you for the opportunity to submit testimony in **Support and Requested Changes to SB951**.

Oceanit is one of the largest local science and technology companies in the State of Hawaii and has been around for over 35 years. We employ over 100 local scientists and engineers in specialized fields such as artificial intelligence and nanomaterials, addressing global problems such as climate change and energy transition.

The tech industry is globally competitive and Hawaii's R&D tax credit is one of the few effective public policies to support our local tech industry which creates good jobs for Hawaii's residents, stems the "Brain Drain" of our best and brightest leaving Hawaii, diversifies our economy, and benefits the public good.

We request the following changes to SB951:

1. Extend the sunset date to December 31, 2029
2. Tighten the qualifying criteria to focus on supporting local Hawaii companies by:
 - Requiring businesses to be registered to do business in Hawaii; and
 - Occupy a business location and address in the State where at least seventy-five percent of the business' employees are located

Thank you for your consideration of SB951.



Statement of
Hermann Kugeler
Vice President of Business Development
Makai Ocean Engineering, Inc.
before the
Senate Committee on Energy, Economic Development, and Tourism
Thursday, February 9, 2023
1:03 pm
Videoconference
State Capitol, Conference Room 229
In consideration of
SB951
RELATING TO THE TAX CREDIT FOR RESEARCH ACTIVITIES.

Chair DeCoite, Vice Chair Wakai, and Members of the Committee

Makai Ocean Engineering, Inc. **SUPPORTS SB951.**

Makai is a locally-owned and operated technology company based in Hawai'i for 50 years. We are currently performing R&D on a variety of exciting ocean technology projects, including autonomous underwater vehicles, ocean thermal energy conversion (OTEC) and seawater air conditioning (SWAC) systems, submarine and subsea cable systems, and several software and hardware development projects supporting our Navy and other federal customers.

Makai has been successful in bringing in tens of millions of dollars in R&D funds from federal and international sponsors to Hawai'i, helping to stem the tide of "brain drain" of talented kama'aina kids going to the mainland. Makai is not unique among Hawaii technology companies in this. There is a tech community here that has made a strong economic impact in terms of high paying jobs, and demonstrated success in commercializing R&D, which has increased taxable revenue for the state, and brought home kama'aina scientists and engineers.

This bill allows Hawaii companies like Makai to outshine mainland peers in competitive federal R&D projects, bring home R&D dollars that greatly exceed the initial investment, and create a critical mass and a truly vibrant industry of innovative R&D companies in Hawaii. It helps expand and diversify Hawaii's economy, and enable our tech industry to support high-paying, highly-skilled professional jobs for our keiki here at home.

This is why we **SUPPORT SB951**, which supports Hawaii's R&D companies enabling them to continue spending monies on wages, materials and subcontractors IN THE STATE OF HAWAII and recognizes the importance of Hawaii's innovation industries to our economy.

SB-951

Submitted on: 2/7/2023 11:44:06 PM

Testimony for EET on 2/9/2023 1:03:00 PM

Submitted By	Organization	Testifier Position	Testify
Ian Kitajima	Testifying for Pacific International Center High Tech Research	Support	Written Testimony Only

Comments:

Aloha Senators. PICHTR supports SB951 which will encourage more local companies to focus on the creation of an innovation economy and workforce in Hawaii. Hawaii doesn't lack smart creative people, but it does lack the funding to encourage more small businesses to focus on high-value research and development. The structure of the R&D credit means that companies must first invest in R&D in Hawaii, before they can claim the credit. So unless a company does qualified research based on federal government rules, they cannot claim the Hawaii R&D credit. **PICHTR SUPPORTS SB951.** Mahalo for the opportunity to testify, Ian Kitajima

TAX FOUNDATION OF HAWAII

126 Queen Street, Suite 305

Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: DBEDT; Tax Credit for Research Activities; Requirements; Survey; Certification; Caps

BILL NUMBER: SB 951

INTRODUCED BY: KEOHOKALO, CHANG, Keith-Agaran

EXECUTIVE SUMMARY: Adds a cap for the amount of tax credits for research activities that an eligible taxpayer and the taxpayer's related entities may receive per taxable year. Consolidates the survey and certification requirements for tax credits for research activities. Amends the annual aggregate cap on tax credits for research activities that the Department of Business, Economic Development, and Tourism may certify. Requires certification of the tax credits for research activities on a first-come, first-served basis to be based on the date that a complete application is received, subject to certain conditions.

SYNOPSIS: Amends section 235-110.91(c), HRS, to provide that each taxpayer, together with all of its related entities including subsidiaries or business entities with common ownership structures, shall not be eligible for more than \$2,500,000 in tax credits per taxable year.

Amends section 235-110.9(d), HRS, to require, as a condition of claiming the credit, a credit applicant to submit the following to DBEDT on or before the end of the third month following the end of the taxable year: (1) Qualified expenditures, if any, expended in the previous taxable year; (2) The amount of tax credits claimed pursuant to this section, if any, in the previous taxable year; (3) The industry sector or sectors in which the qualified high technology business conducts business, as set forth in paragraphs (2) to (8) of the definition of "qualified research" in section 235-7.3(c), HRS; (4) Revenue and expense data, including a breakdown of any licensing royalty or other forms of income generated from intellectual property; (5) Hawaii employment and wage data, including the numbers of full-time and part-time employees retained, new jobs, temporary positions, external services procured by the business, and payroll taxes; (6) The number of filed intellectual property, including invention disclosures, provisional patents, and patents issued or granted; (7) The number of new companies spun out or established in Hawaii to commercialize the intellectual property owned by the qualified high technology business; and (8) A written declaration signed by an officer of the qualified high technology business certifying that the information that is submitted is true and correct as to every material matter, which certification shall be subject to the penalties provided in section 231-36, HRS, including monetary fines or imprisonment.

DBEDT may request any additional information necessary to measure the effectiveness of the tax credit, such as additional information related to patents.

Clarifies that failure to meet the requirements of subsection (d) shall constitute a waiver of the right to claim the credit.

Amends section 235-110.91(f), HRS, to limit the amount of certified credits to \$15 million per calendar year. DBEDT shall certify credits on a first-come, first-served basis determined based on the date and time a complete application is received by DBEDT. If all \$15,000,000 is not expended within the first twenty-four hours that the applications are made available, DBEDT shall certify any remaining credits after that date to companies on a pro rata basis.

Removes the requirement of an annual survey contained in current subsections (i) and (j) of section 235-110.91, HRS.

EFFECTIVE DATE: July 1, 2023, applicable to taxable years beginning after December 31, 2022.

STAFF COMMENTS: The legislature by Act 270, SLH 2013, reestablished the income tax credit for qualified research activities that expired on 12/31/10. The prior version of that law, under Act 221, SLH 2001, offered a credit for qualified research activities that was a flat percentage of qualified research expenses in Hawaii without regard to the federal base amount (the federal credit is supposed to be an incentive to increase research activities, so the federal credit is based on incremental research expenses). When Act 270 brought the credit back, it did so as an incremental credit, like the federal credit.

Act 261, SLH 2019, amended the credit by reinserting the phrase “provided that references to the base amount shall not apply and credit for all qualified research expenses may be taken without regard to the amount of expenses for previous years.”

Substantively, over the last decade, Hawaii has adopted various tax incentives to encourage the development of high technology businesses in the state. The acts provided investment and research credits as well as income exclusions providing tax relief to high tech businesses and individuals associated with high tech businesses. 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 plow money into such activities is the fact that the credit provides a way to avoid paying state taxes.

At a minimum, lawmakers should carefully examine the results that have come out of this 20-year-old incentive to see if the State has gotten its money’s worth. If it hasn’t, how can an extension or increase in the credit be justified?

Digested: 2/6/2023

SB-951

Submitted on: 2/8/2023 1:01:17 PM

Testimony for EET on 2/9/2023 1:03:00 PM

Submitted By	Organization	Testifier Position	Testify
Ryan Bradley	Testifying for Hawaii Aerospace Corp	Support	Written Testimony Only

Comments:

I support SB951:

1. Each taxpayer, together with all of its related entities, shall not be eligible for any more than \$1.5M in tax credits provided by this section per taxable year;

Requested change: Page 3, Line 8. Replace “\$2,500,000” with “\$1,500,000.

1. Every qualified high technology business shall. Be registered to do business in the State; and Occupy a business location and address in the State where at least seventy-five percent of the business’ employees are located; and

Requested addition to be inserted on Page 3 after line 9.

1. Extend the sunset date to December 31, 2029.

Requested change: Page 12 line 18. Replaces December 31, 2024 with December 31, 2029.

LATE

SB-951

Submitted on: 2/8/2023 3:31:40 PM

Testimony for EET on 2/9/2023 1:03:00 PM

Submitted By	Organization	Testifier Position	Testify
Ann Chung	Individual	Support	Written Testimony Only

Comments:

I strongly support SB951 and humbly request 1 amendment. The sentence "Failure to meet the requirements of this subsection shall constitute a waiver of the right to claim the tax credit." may have unintended consequences - example if an applicant misses one question by mistake - it may disqualify them from the credit.

The Research Tax Credit is a critical initiative that allows Hawaii companies to effectively compete for federal R&D projects, bring home R&D dollars that greatly exceed the initial investment, and create a critical mass and a truly vibrant industry of innovative R&D companies in Hawaii. It helps expand and diversify Hawaii's economy, and enable our tech industry to support highpaying, highly-skilled professional jobs for our keiki here at home.

Mahalo for your consideration.