

JOSH GREEN M.D.  
GOVERNOR

SYLVIA LUKE  
LT. GOVERNOR



STATE OF HAWAII  
**DEPARTMENT OF TAXATION**  
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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, S.D.2, Relating to the Tax Credit for Research Activities

**BEFORE THE:**

House Committee on Economic Development

**DATE:** Wednesday, March 22, 2023  
**TIME:** 9:30 a.m.  
**LOCATION:** State Capitol, Room 423

Chair Holt, Vice-Chair Lamosao, and Members of the Committee:

The Department of Taxation ("Department") offers the following comments regarding S.B. 951, S.D.2, for your consideration.

S.B. 951, S.D.2, 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 \$1,500,000 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; (5) amending the aggregate cap from \$5,000,000 per taxable year to \$15,000,000 per calendar year; (6) requiring every qualified high technology business be registered to do business in the State; and (7) adding a definition of "small business." The measure further extends the sunset date for the credit from December 31, 2024 to December 31, 2029.

The measure is effective on July 1, 2050 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 (e) may be read to conflict with subsection (g). Subsection (g) refers to the aggregate cap and certifications in terms of a calendar year. As such, subsection (e) 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 15, 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  
**Len Higashi**  
Executive Director  
Hawaii Technology Development Corporation  
before the  
**House Committee On Economic Development**  
Wednesday, March 22, 2023  
9:30 a.m.  
Conference Room 423 & Videoconference

In consideration of  
**SB951, SD2**  
**RELATING TO THE TAX CREDIT FOR RESEARCH ACTIVITIES.**

Chair Holt, Vice Chair Lamosao, and Members of the Committee.

The Hawai'i Technology Development Corporation (HTDC) **supports** SB951, SD2 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; extends the sunset date for tax credits for research activities from December 31, 2024 to December 31, 2029.

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. This bill will resolve the issue by allowing same-day applicants to split a pro-rata share of the credit and increases the total amount available for all filers.

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



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

Before the  
**HOUSE COMMITTEE ON ECONOMIC DEVELOPMENT**

Wednesday, March 22, 2023  
9:30 a.m.  
State Capitol, Conference Room 423 & Videoconference

In Support and Requested Changes to  
**SB951 SD2 RELATING TO TAX CREDIT FOR RESEARCH ACTIVITIES**

To: Representative Daniel Holt, Chair, Representative Rachele F. Lamosao, Vice Chair and Members of the Committee

From: Mr. Matthew Sullivan, Director of Product

Re: Testimony in Support and Requested Changes to SB951 S.D.2.

Honorable Chair, Vice-Chair and Committee Members: Thank you for the opportunity to submit testimony in **Support and Requested Changes to SB951 S.D.2.**

Oceanit is one of the largest local science and engineering 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 transformation.

Hawaii's R&D tax credit is one of the few state policies to support the local tech industry. We support SB951 S.D.2. and request the following changes:

- HRS Sec. 235-110.91 (d) - Add to the end of last sentence to the qualifying requirements as follows - "...and shall be a "Small Business" as defined in section (n) herein."
  - o We recommend this change because the definition of a "Small Business" was added to SB951 S.D.2., in response to testimony from the AG. However, the definition was not inserted in a way that tied it to an actual qualification.
  
- HRS Sec. 235-110.91 (g) - Delete the last sentence of the first paragraph of this section which reads as follows - "Complete applications received on the same date shall be certified on a pro rata basis."
  - o We believe that the addition of "pro rata" language will make it impractical to calculate and issue tax credits to companies in a timely manner and furthermore will penalize companies that prioritize the preparation and timely submission of their application. The industry already spends a significant amount of time and money to qualify, categorize, and substantiate expenses for the R&D tax credit. For various reasons, DOTAX has been slow to review tax returns including R&D tax credits to companies that qualify. It is not uncommon for companies to wait a significant amount of time to receive the tax credit. Further, returns remain open

to audit beyond the date after which the tax return is processed. Adding “pro rata” will add confusion and slow down this process which will make it difficult for small businesses to use the tax credit to hire employees and purchase equipment – the intent of the bill.

**The Hawaii R&D tax credit is a good investment for the State.**

According to a 2021 UHERO report titled *The Hawaii Research Activity Tax Credit: Is It Effective and How Can It Be Improved?*, every \$1 in tax credits claimed generates an additional \$1-2 in additional spending in the State by private firms.

**The tech industry supports a living wage for locals, empowering locals to compete for housing in Hawaii and remain in the State vs move to the mainland.**

According to the *Report on Hawaii Tax Credit for Research Activities for Tax Year 2021* prepared by DBEDT, the average annual wage was \$93,634 for the 34 Qualified High Technology Businesses that applied for the Hawaii tax credit for research activities for the tax year 2021.

**The R&D tax credit enables Hawaii companies to compete with other states for talent.**

37 of the 50 states in the U.S. offer an R&D tax credit. Hawaii’s R&D tax credit enables Hawaii companies to compete with other states to recruit and retain more local talent and stem Hawaii’s “Brain Drain”.

**To grow our local tech industry, the annual \$5 million cap should be increased.**

In 2021, 34 companies applied for the Hawaii tax credit but only 9 received it due to the \$5 million annual cap. In aggregate, the 34 QHTBs generated a total of \$223 million revenue from all goods and services produced in Hawaii, \$195 million as operating cost, and paid a total of \$80 million as payroll.

Mahalo for your consideration,

Matthew Sullivan



Statement of  
**Hermann Kugeler**  
**Vice President of Business Development**  
**Makai Ocean Engineering, Inc.**

before the  
**House Committee on Economic Development**

Wednesday, March 22, 2023

9:30 am

State Capitol, Conference Room 423

In consideration of

**SB951**

**RELATING TO THE TAX CREDIT FOR RESEARCH ACTIVITIES.**

Chair Holt, Vice Chair Lamosao, 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.

# TAX FOUNDATION OF HAWAII

126 Queen Street, Suite 305

Honolulu, Hawaii 96813 Tel. 536-4587

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

BILL NUMBER: SB 951 SD 2

INTRODUCED BY: Senate Committee on Ways and Means

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. Extends from December 31, 2024 to December 31, 2029, the sunset date for tax credits for research activities.

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 \$1,500,000 in tax credits per taxable year.

Adds a new subsection (d) that requires that every qualified high technology business (1) be registered to do business in the State.

Amends section 235-110.9(d), HRS, and redesignates it as subsection (e), 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 (e) 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.

Extends the sunset date of the credit by five years, to December 31, 2029.

EFFECTIVE DATE: July 1, 2050, provided that section 1 is 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?



Re: SB 951 SD2  
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Digested: 3/21/2023



**LATE**

**LATE**

March 21, 2023

**Committee:** House Committee on Economic Development  
**Bill Number:** SB 801 SD2, Relating to Qualified Internships Tax Credit  
**Hearing Date and Time:** March 22, 2023, 9:30am  
**Re:** Testimony of HPM Building Supply in support

Dear Chair Holt, Vice Chair Lamasao, and members of the Committee,

I am writing to express my strong support for SB 801 SD2 which establishes a qualified internship income tax credit for employers of qualified interns.

HPM Building Supply is a 100% employee-owned company serving Hawaii's home improvement market and building industry for over 100 years since 1921. With 17 locations across Hawaii and Washington State, HPM offers various services and products, including retail stores, building supply and lumber yards, home design centers, drafting and design services, and manufacturing facilities. HPM is dedicated to enhancing homes, improving lives, and transforming communities. The company is guided by its core values of Heart, Character, and Growth, striving to provide top-quality products and build exceptional customer loyalty. HPM has earned recognition as a leader in the industry for its products, services, and commitment to its community.

This bill aligns with two of HPM's core values: Heart and Growth. With Heart, we care deeply about the future of our children and our community. With Growth, we are committed to transforming the next generation of workers and building a better economy for Hawaii.

Work-based learning opportunities such as internships give students the chance to learn on-the-job and gain experience that will make them stand out in high-paying job opportunities in the future. This bill will encourage and enable more employers to offer paid internships for students, which will directly address the issue of high youth unemployment rates in Hawaii.

HPM recognizes the benefits of internships in promoting experiential learning and building confidence in entering the workforce or attaining post-secondary education. By offering qualified internships, we can provide students with valuable experience in high-demand industries such as healthcare, technology, construction and engineering.

Furthermore, the tax credits suggested in this bill will incentivize more small and medium-sized businesses in Hawaii to provide paid internships, resulting in a more extensive and diverse range of opportunities that align with student interest. Through a skilled workforce, Hawaii's economy will continue to grow and thrive.

We respectfully request your favorable consideration of SB 801 SD2 and support for this critical measure.

Sincerely,

Jason Fujimoto  
President & CEO

