
A BILL FOR AN ACT

RELATING TO TAXATION.

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

1 **PART I**

2 SECTION 1. The purpose of this part is to improve the
3 organizational framework of the statutes relating to tax
4 provisions concerning motion pictures, digital media, and film
5 production. This part is intended to simplify the statutory
6 structure through recodification and the renaming of certain
7 provisions, where necessary, and not to effect any substantive
8 changes to the current tax provisions, except for the amount of
9 the motion picture, digital media, and film production tax
10 credit allowed. In particular, the sunset provisions for the
11 performing arts investment tax credit and the tax credit for
12 performing arts research activities remain the same as in
13 current law - December 31, 2010.

14 It is time for Hawaii to take full advantage of its natural
15 constituency with the countries of the Pacific rim and the
16 rising tide of global popular culture in all its forms



1 (including video games, animation, and indigenous films)
2 leveraging Hawaii's inherent strengths.

3 Digital entertainment, in the form of computer animated
4 films and video games, not only dominates the entertainment
5 business today (e.g., top box office hits like *Finding Nemo* and
6 *Happy Feet*), but it is a globally-distributed economy.
7 Technology means that companies can grow where people want to
8 live, not where they have to work. Today's biggest hits come
9 from outside Hollywood – from Emeryville (Pixar), Australia and
10 New Zealand (*Happy Feet* and *Lord of the Rings*), and upstate New
11 York (*Ice Age*). The \$25 billion video game industry is based
12 wherever the talent is; not where the historic infrastructure
13 is. In the competition for artistic talent, Hawaii offers the
14 perfect place to raise a family and the perfect lifestyle for
15 the artists in the creative digital field.

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

19 **"PART . MOTION PICTURE, DIGITAL MEDIA, AND FILM PRODUCTION**

20 **§235-A Performing arts royalties derived from patents,**
21 **copyrights, or trade secrets excluded from gross income. (a)**

22 In addition to the exclusions in section 235-7, there shall be



1 excluded from gross income, adjusted gross income, and taxable
2 income, amounts received by an individual or a qualified
3 business as royalties and other income derived from any patents,
4 copyrights, and trade secrets:

5 (1) Owned by the individual or qualified business; and

6 (2) Developed and arising out of a qualified business.

7 (b) This exclusion shall extend to:

8 (1) The authors of performing arts products, or any parts
9 thereof, without regard to the application of the
10 work-for-hire doctrine under United States copyright
11 law;

12 (2) The authors of performing arts products, or any parts
13 thereof, under the work-for-hire doctrine under United
14 States copyright law; and

15 (3) The assignors, licensors, and licensees of any
16 copyright rights in performing arts products, or any
17 parts thereof.

18 (c) For the purposes of this section:

19 "Performing arts products" means:

20 (1) Audio files, video files, audiovideo files, computer
21 animation, and other entertainment products perceived
22 by or through the operation of a computer; and



1 (2) Commercial television and film products for sale or
2 license, and reuse or residual fee payments from these
3 products.

4 "Qualified business" means a business engaged in producing
5 performing arts products that conducts more than fifty per cent
6 of its activities in qualified research.

7 "Qualified research" means:

8 (1) The same as in section 41(d) of the Internal Revenue
9 Code; and

10 (2) Performing arts products.

11 **§235-B Performing arts investment tax credit.** (a) There
12 shall be allowed to each taxpayer subject to the taxes imposed
13 by this chapter a performing arts investment tax credit that
14 shall be deductible from the taxpayer's net income tax
15 liability, if any, imposed by this chapter for the taxable year
16 in which the investment was made and the following four years
17 provided the credit is properly claimed. The tax credit shall
18 be as follows:

19 (1) In the year the investment was made, thirty-five per
20 cent;

21 (2) In the first year following the year in which the
22 investment was made, twenty-five per cent;



1 (3) In the second year following the investment, twenty
2 per cent;

3 (4) In the third year following the investment, ten per
4 cent; and

5 (5) In the fourth year following the investment, ten per
6 cent;

7 of the investment made by the taxpayer in each qualified
8 business, up to a maximum allowed credit in the year the
9 investment was made, \$700,000; in the first year following the
10 year in which the investment was made, \$500,000; in the second
11 year following the year in which the investment was made,
12 \$400,000; in the third year following the year in which the
13 investment was made, \$200,000; and in the fourth year following
14 the year in which the investment was made, \$200,000.

15 (b) The credit allowed under this section shall be claimed
16 against the net income tax liability for the taxable year. For
17 the purpose of this section, "net income tax liability" means
18 net income tax liability reduced by all other credits allowed
19 under this chapter.

20 (c) If the tax credit under this section exceeds the
21 taxpayer's income tax liability for any of the five years that
22 the credit is taken, the excess of the tax credit over liability



1 may be used as a credit against the taxpayer's income tax
2 liability in subsequent years until exhausted. Every claim,
3 including amended claims, for a tax credit under this section
4 shall be filed on or before the end of the twelfth month
5 following the close of the taxable year for which the credit may
6 be claimed. Failure to comply with the foregoing provision
7 shall constitute a waiver of the right to claim the credit.

8 (d) If at the close of any taxable year in the five year
9 period in subsection (a):

10 (1) The business no longer qualifies as a qualified
11 business;

12 (2) The business or an interest in the business has been
13 sold by the taxpayer investing in the qualified
14 business; or

15 (3) The taxpayer has withdrawn the taxpayer's investment
16 wholly or partially from the qualified business;

17 the credit claimed under this section shall be recaptured. The
18 recapture shall be equal to ten per cent of the amount of the
19 total tax credit claimed under this section in the preceding two
20 taxable years. The amount of the credit recaptured shall apply
21 only to the investment in the particular qualified business that
22 meets the requirements of paragraph (1), (2), or (3). The



1 recapture provisions of this subsection shall not apply to a tax
2 credit claimed for a qualified business that does not fall
3 within the provisions of paragraph (1), (2), or (3). The amount
4 of the recaptured tax credit determined under this subsection
5 shall be added to the taxpayer's tax liability for the taxable
6 year in which the recapture occurs under this subsection.

7 (e) Every taxpayer, before April 1 of each year in which
8 an investment in a qualified business was made in the previous
9 taxable year, shall submit a written, certified statement to the
10 director of taxation identifying:

- 11 (1) Qualified investments, if any, expended in the
12 previous taxable year;
- 13 (2) The amount of tax credits claimed pursuant to this
14 section, if any, in the previous taxable year; and
- 15 (3) The number of total hires versus the number of local
16 hires by category (i.e., department) and by country.

17 The department of taxation shall use the information from the
18 statements submitted each year under this subsection to prepare
19 a report published by May 1 of each year presenting the
20 information received under this subsection. The information
21 shall be presented in the aggregate and shall be available to
22 the public.



- 1 (f) The department shall:
- 2 (1) Maintain records of the names and addresses of the
- 3 taxpayers claiming the credits under this section and
- 4 the total amount of the qualified investment costs
- 5 upon which the tax credit is based;
- 6 (2) Verify the nature and amount of the qualifying
- 7 investments;
- 8 (3) Total all qualifying and cumulative investments that
- 9 the department certifies; and
- 10 (4) Certify the amount of the tax credit for each taxable
- 11 year and cumulative amount of the tax credit.

12 Upon each determination made under this subsection, the

13 department shall issue a certificate to the taxpayer verifying

14 information submitted to the department, including qualifying

15 investment amounts, the credit amount certified for each taxable

16 year, and the cumulative amount of the tax credit during the

17 credit period. The taxpayer shall file the certificate with the

18 taxpayer's tax return with the department.

19 The director of taxation may assess and collect a fee to

20 offset the costs of certifying tax credits claims under this

21 section. All fees collected under this section shall be



1 deposited into the tax administration special fund established
2 under section 235-20.5.

3 (g) As used in this section:

4 "Investment tax credit allocation ratio" means, with
5 respect to a taxpayer that has made an investment in a qualified
6 business, the ratio of:

7 (1) The amount of the credit under this section that is,
8 or is to be, received by or allocated to the taxpayer
9 over the life of the investment, as a result of the
10 investment; to

11 (2) The amount of the investment in the qualified
12 business.

13 "Qualified business" means a business engaged in producing
14 performing arts products, employing or owning capital or
15 property, or maintaining an office, in this State; provided
16 that:

17 (1) More than fifty per cent of its total business
18 activities are qualified research; and provided
19 further that the business conducts more than seventy-
20 five per cent of its qualified research in this State;
21 or



1 (2) More than seventy-five per cent of its gross income is
2 derived from qualified research; and provided further
3 that this income is received from:

4 (A) Products sold from, manufactured in, or produced
5 in this State; or

6 (B) Services performed in this State.

7 "Qualified research" means the same as defined in section
8 235-A.

9 "Performing arts products" means the same as defined in
10 section 235-A.

11 (h) Common law principles, including the doctrine of
12 economic substance and business purpose, shall apply to any
13 investment. There exists a presumption that a transaction
14 satisfies the doctrine of economic substance and business
15 purpose to the extent that the special allocation of the
16 performing arts tax credit has an investment tax credit ratio of
17 1.5 or less of credit for every dollar invested.

18 Transactions for which an investment tax credit allocation
19 ratio greater than 1.5 but not more than 2.0 of credit for every
20 dollar invested and claimed may be reviewed by the department
21 for applicable doctrines of economic substance and business
22 purpose.



1 Businesses claiming a tax credit for transactions with
2 investment tax credit allocation ratios greater than 2.0 of
3 credit for every dollar invested shall substantiate economic
4 merit and business purpose consistent with this section.

5 (i) Persons eligible for a tax credit under section 235-D
6 may claim a tax credit under this section but not under section
7 235-110.9. Persons not eligible for a tax credit under 235-D
8 shall not claim any tax credit under this section. Any person
9 that has:

10 (1) Claimed the tax credit under section 235-110.9; and

11 (2) Not exhausted the right to claim the tax credit for
12 the five-year period provided thereunder,

13 shall be eligible to continue to claim the tax credit, without
14 reduction or requalification, for the remainder of the five-year
15 period pursuant to this section if the taxpayer qualifies for a
16 credit under section 235-D.

17 (j) This section shall not apply to taxable years
18 beginning after December 31, 2010.

19 **§235-C Tax credit for performing arts research activities.**

20 (a) Section 41 (with respect to the credit for increasing
21 research activities) and section 280C(c) (with respect to
22 certain expenses for which the credit for increasing research



1 activities are allowable) of the Internal Revenue Code shall be
2 operative for the purposes of this chapter as provided in this
3 section; except that references to the base amount shall not
4 apply and credit for all qualified research expenses may be
5 taken without regard to the amount of expenses for previous
6 years. If section 41 of the Internal Revenue Code is repealed
7 or terminated prior to January 1, 2011, its provisions shall
8 remain in effect for purposes of the income tax law of the State
9 as modified by this section, as provided for in subsection (j).

10 (b) All references to Internal Revenue Code sections
11 within sections 41 and 280C(c) of the Internal Revenue Code
12 shall be operative for purposes of this section.

13 (c) There shall be allowed to each qualified business
14 subject to the tax imposed by this chapter an income tax credit
15 for qualified research activities equal to the credit for
16 research activities provided by section 41 of the Internal
17 Revenue Code and as modified by this section. The credit shall
18 be deductible from the taxpayer's net income tax liability, if
19 any, imposed by this chapter for the taxable year in which the
20 credit is properly claimed.

21 (d) Every qualified business, before April 1 of each year
22 in which qualified research and development activity was



1 conducted in the previous taxable year, shall submit a written,
2 certified statement to the director of taxation identifying:

- 3 (1) Qualified expenditures, if any, expended in the
4 previous taxable year; and
5 (2) The amount of tax credits claimed pursuant to this
6 section, if any, in the previous taxable year.

7 The department of taxation shall use the information from the
8 statements submitted each year under this subsection to prepare
9 a report published by May 1 of each year presenting the
10 information received under this subsection. The information
11 shall be presented in the aggregate and shall be available to
12 the public.

13 (e) The department shall:

- 14 (1) Maintain records of the names and addresses of the
15 taxpayers claiming the credits under this section and
16 the total amount of the qualified research and
17 development activity costs upon which the tax credit
18 is based;
19 (2) Verify the nature and amount of the qualifying costs
20 or expenditures;
21 (3) Total all qualifying and cumulative costs or
22 expenditures that the department certifies; and



1 (4) Certify the amount of the tax credit for each taxable
2 year and cumulative amount of the tax credit.

3 Upon each determination made under this subsection, the
4 department shall issue a certificate to the taxpayer verifying
5 information submitted to the department, including the
6 qualifying costs or expenditure amounts, the credit amount
7 certified for each taxable year, and the cumulative amount of
8 the tax credit during the credit period. The taxpayer shall
9 file the certificate with the taxpayer's tax return with the
10 department.

11 The director of taxation may assess and collect a fee to
12 offset the costs of certifying tax credit claims under this
13 section. All fees collected under this section shall be
14 deposited into the tax administration special fund established
15 under section 235-20.5.

16 (f) As used in this section:

17 "Basic research" under section 41(e) of the Internal
18 Revenue Code shall not include research conducted outside of the
19 State.

20 "Qualified business" means the same as in section 235-B.



1 "Qualified research" under section 41(d)(1) of the Internal
2 Revenue Code shall not include research conducted outside of the
3 State.

4 (g) If the tax credit for qualified performing arts
5 research activities claimed by a taxpayer exceeds the amount of
6 income tax payment due from the taxpayer, the excess of the tax
7 credit over payments due shall be refunded to the taxpayer;
8 provided that no refund on account of the tax credit allowed by
9 this section shall be made for amounts less than \$1.

10 (h) All claims for a tax credit under this section shall
11 be filed on or before the end of the twelfth month following the
12 close of the taxable year for which the credit may be claimed.
13 Failure to properly claim the credit shall constitute a waiver
14 of the right to claim the credit.

15 (i) The director of taxation may adopt any rules under
16 chapter 91 and forms necessary to carry out this section.

17 (j) Persons eligible to claim a tax credit under section
18 235-D may claim a tax credit under this section but not under
19 section 235-110.91. Persons not eligible for a tax credit under
20 section 235-D shall not claim a tax credit under this section.
21 Any person that has:

22 (1) Claimed the tax credit under section 235-110.91; and



1 (2) Not exhausted the right to claim the tax credit
2 provided thereunder,
3 shall be eligible to continue to claim the tax credit, without
4 reduction or requalification, pursuant to this section, if the
5 taxpayer is eligible to claim a credit under section 235-D.

6 (k) This section shall not apply to taxable years
7 beginning after December 31, 2010."

8 SECTION 3. Section 235-7.3, Hawaii Revised Statutes, is
9 amended to read as follows:

10 **"§235-7.3 Royalties derived from patents, copyrights, or**
11 **trade secrets excluded from gross income.** (a) In addition to
12 the exclusions in section 235-7, there shall be excluded from
13 gross income, adjusted gross income, and taxable income, amounts
14 received by an individual or a qualified high technology
15 business as royalties and other income derived from any patents,
16 copyrights, and trade secrets:

17 (1) Owned by the individual or qualified high technology
18 business; and

19 (2) Developed and arising out of a qualified high
20 technology business.

21 ~~[(b) With respect to performing arts products, this~~
22 ~~exclusion shall extend to:~~



1 ~~(1) The authors of performing arts products, or any parts~~
2 ~~thereof, without regard to the application of the~~
3 ~~work for hire doctrine under United States copyright~~
4 ~~law;~~

5 ~~(2) The authors of performing arts products, or any parts~~
6 ~~thereof, under the work for hire doctrine under United~~
7 ~~States copyright law; and~~

8 ~~(3) The assignors, licensors, and licensees of any~~
9 ~~copyright rights in performing arts products, or any~~
10 ~~parts thereof.~~

11 ~~(e)]~~ (b) For the purposes of this section:

12 ~~["Performing arts products" means:~~

13 ~~(1) Audio files, video files, audiovideo files, computer~~
14 ~~animation, and other entertainment products perceived~~
15 ~~by or through the operation of a computer; and~~

16 ~~(2) Commercial television and film products for sale or~~
17 ~~license, and reuse or residual fee payments from these~~
18 ~~products.]~~

19 "Qualified high technology business" means a business that
20 conducts more than fifty per cent of its activities in qualified
21 research.

22 "Qualified research" means:



- 1 (1) The same as in section 41(d) of the Internal Revenue
2 Code;
- 3 (2) The development and design of computer software for
4 ultimate commercial sale, lease, license or to be
5 otherwise marketed, for economic consideration. With
6 respect to the software's development and design, the
7 business shall have substantial control and retain
8 substantial rights to the resulting intellectual
9 property;
- 10 (3) Biotechnology;
- 11 [~~(4)~~ ~~Performing arts products;~~
- 12 ~~(5)] (4) Sensor and optic technologies;~~
- 13 [~~(6)] (5) Ocean sciences;~~
- 14 [~~(7)] (6) Astronomy; or~~
- 15 [~~(8)] (7) Nonfossil fuel energy-related technology."~~

16 SECTION 4. Section 235-17, Hawaii Revised Statutes, is
17 amended as follows:

18 1. By renumbering the section, inserting it into the new
19 part of chapter 235, Hawaii Revised Statutes, established under
20 section 2 of this Act, and amending subsection (a) to read:

21 "~~§235-17] §235-D Motion picture, digital media, and film~~

22 production income tax credit. (a) Any law to the contrary



1 notwithstanding, there shall be allowed to each taxpayer subject
2 to the taxes imposed by this chapter, an income tax credit which
3 shall be deductible from the taxpayer's net income tax
4 liability, if any, imposed by this chapter for the taxable year
5 in which the credit is properly claimed. The amount of the
6 credit shall be:

- 7 (1) [~~Fifteen~~] Twenty per cent of the qualified production
8 costs incurred by a qualified production in any county
9 of the State with a population of over seven hundred
10 thousand; or
- 11 (2) [~~Twenty~~] Twenty-five per cent of the qualified
12 production costs incurred by a qualified production in
13 any county of the State with a population of seven
14 hundred thousand or less.

15 A qualified production occurring in more than one county may
16 prorate its expenditures based upon the amounts spent in each
17 county, if the population bases differ enough to change the
18 percentage of tax credit.

19 In the case of a partnership, S corporation, estate, or
20 trust, the tax credit allowable is for qualified production
21 costs incurred by the entity for the taxable year. The cost
22 upon which the tax credit is computed shall be determined at the



1 entity level. Distribution and share of credit shall be
2 determined by rule.

3 If a deduction is taken under section 179 (with respect to
4 election to expense depreciable business assets) of the Internal
5 Revenue Code of 1986, as amended, no tax credit shall be allowed
6 for those costs for which the deduction is taken.

7 The basis for eligible property for depreciation of
8 accelerated cost recovery system purposes for state income taxes
9 shall be reduced by the amount of credit allowable and claimed."

10 2. By amending subsection (h) to read:

11 "(h) Every taxpayer claiming a tax credit under this
12 section for a qualified production shall, no later than ninety
13 days following the end of each taxable year in which qualified
14 production costs were expended, submit a written, sworn
15 statement to the department of business, economic development,
16 and tourism, identifying:

17 (1) All qualified production costs as provided by
18 subsection (a), if any, incurred in the previous
19 taxable year;

20 (2) The amount of tax credits claimed pursuant to this
21 section, if any, in the previous taxable year; [and]



1 (3) The number of total hires versus the number of
2 qualified local hires by category (i.e., department)
3 and by county[-]; and

4 (4) Evidence of educational or workforce development
5 efforts, including but not limited to:

6 (A) Teacher training, mentorship, and internship
7 opportunities by industry professionals and
8 Hawaii-based productions for "below-the-line"
9 local technical crews; and

10 (B) Participation in a statewide advisory council to
11 develop the training, mentorship, and internship
12 opportunity programs to produce qualified workers
13 entering film and television production and
14 creative media industries.

15 The department of business, economic development, and tourism
16 shall use the information from the statements submitted under
17 this section to prepare a report, published biannually, no later
18 than June 30 and December 31, presenting information identifying
19 tax credit recipients and the aggregate total value of the
20 credits received under this subsection. The information shall
21 be available to the public in both print and electronic form."

22 3. By amending subsection (j) to read:



1 Applications for grants shall [~~be made to the board~~
2 ~~and shall~~] contain such information as [~~the board~~
3 ~~shall require~~] required by rules adopted pursuant to
4 chapter 91. At a minimum, the applicant shall agree
5 to the following conditions:

- 6 (A) The grant shall be used exclusively for eligible
7 Hawaii projects;
- 8 (B) The applicant shall have applied for or received
9 all applicable licenses and permits;
- 10 (C) The applicant shall comply with applicable
11 federal and state laws prohibiting discrimination
12 against any person on the basis of race, color,
13 national origin, religion, creed, sex, age, or
14 physical handicap;
- 15 (D) The applicant shall comply with other
16 requirements as the [~~board~~] department may
17 prescribe;
- 18 (E) All activities undertaken with funds received
19 shall comply with all applicable federal, state,
20 and county statutes and ordinances;
- 21 (F) The applicant shall indemnify and save harmless
22 the State of Hawaii and its officers, agents, and



1 employees from and against any and all claims
2 arising out of or resulting from activities
3 carried out or projects undertaken with funds
4 provided hereunder, and procure sufficient
5 insurance to provide this indemnification if
6 requested to do so by the department;

7 (G) The applicant shall make available [~~to the board~~]
8 all records the applicant may have relating to
9 the project, to allow the [~~board~~] department to
10 monitor the applicant's compliance with the
11 purpose of this chapter; and

12 (H) The applicant [~~, to the satisfaction of the~~
13 ~~board,~~] shall establish that sufficient funds are
14 available for the completion of the project for
15 the purpose for which the grant is awarded; and

16 (2) A venture capital program. [~~The board shall adopt~~
17 ~~rules~~] Rules adopted pursuant to chapter 91 [~~to~~] shall
18 provide conditions and qualifications for venture
19 capital investments in eligible Hawaii projects. The
20 program may include a written agreement between the
21 borrower and the [~~board,~~] department, as the
22 representative of the State, that as consideration for



1 the venture capital investment made under this part,
2 the borrower shall share any royalties, licenses,
3 titles, rights, or any other monetary benefits that
4 may accrue to the borrower pursuant to terms and
5 conditions established [~~by the board~~] by rule pursuant
6 to chapter 91. Venture capital investments may be
7 made on such terms and conditions as the [~~board~~]
8 department shall determine to be reasonable,
9 appropriate, and consistent with the purposes and
10 objectives of this part."

11 SECTION 8. Section 201-114, Hawaii Revised Statutes, is
12 amended to read as follows:

13 "[~~§~~201-114~~§~~] **Inspection of premises and records.** The
14 [~~board~~] department shall have the right to inspect, at
15 reasonable hours, the plant, physical facilities, equipment,
16 premises, books, and records of any applicant in connection with
17 the processing of a grant to the applicant."

18 SECTION 9. Section 201-112, Hawaii Revised Statutes, is
19 repealed.

20 [~~§201-112~~] ~~Hawaii television and film development board.~~
21 ~~(a) There is established the Hawaii television and film~~
22 ~~development board. The board shall be attached to the~~



1 ~~department of business, economic development, and tourism for~~
2 ~~administrative purposes only. The board shall administer the~~
3 ~~grant and venture capital investment programs and the Hawaii~~
4 ~~television and film development special fund established under~~
5 ~~this part. The board shall also assess and consider the overall~~
6 ~~viability and development of the television and film industries~~
7 ~~and make recommendations to appropriate state or county~~
8 ~~agencies.~~

9 ~~(b) The board shall be composed of nine members, four of~~
10 ~~whom shall be appointed by the governor pursuant to section 26-~~
11 ~~34, and all of whom shall serve four year staggered terms. One~~
12 ~~of the governor's appointments shall be made from a list of~~
13 ~~nominees submitted by the president of the senate and another~~
14 ~~appointment shall be made from a list of nominees submitted by~~
15 ~~the speaker of the house of representatives. The four appointed~~
16 ~~members shall possess a current working knowledge of the film,~~
17 ~~television, or entertainment industry. The director of~~
18 ~~business, economic development, and tourism, and the chairs of~~
19 ~~the four county film commissions or its equivalent, shall serve~~
20 ~~as ex officio voting members, who may be represented on the~~
21 ~~board by designees.~~



Report Title:

Taxation; Motion Picture, Digital Media, Film Production

Description:

Recodifies and renames existing motion picture, digital media, and film production tax provisions; increases the tax credits from fifteen and twenty per cent to twenty and twenty-five per cent; increases reporting requirements; repeals the Hawaii television and film development board; deletes references to the board from the Hawaii television and film development special fund and elsewhere. (SD1)

