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# A BILL FOR AN ACT

RELATING TO TAX CREDITS.

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

1           SECTION 1. Research and development is the core of  
2 innovation. Without innovation, there is no technology industry  
3 and the subsequent growth of our economy is stunted with no new  
4 products, services, or processes. Research and development is  
5 the critical first step in the product development cycle.  
6 During the research and development stage, ideas and theories  
7 are tested to determine feasibility. Due to the increasingly  
8 interconnected and competitive global economy, fostering and  
9 encouraging innovation is essential to a comprehensive economic  
10 strategy for the State. The key to developing more jobs and  
11 more prosperity will be to create and deploy new products,  
12 services, and processes.

13           Innovation is essential for creating new jobs in high  
14 technology and traditional sectors. In recent years, innovation  
15 has led to new jobs in many different sectors as diverse as  
16 defense or dual-use, software and information technology, life  
17 sciences and biotechnology, and clean energy. At the same time,  
18 innovations ripple through the economy, creating jobs for



1 workers building advanced infrastructure (clean energy  
2 solutions), installing broadband networks, and utilizing new  
3 devices and products in the service industries, such as health  
4 care and tourism.

5 Innovation is also critical for sustaining the vitality and  
6 resilience of our economy. Future challenges (natural or man-  
7 made) are impossible to predict. However, it is certain that an  
8 economy better able to respond to such events by adopting  
9 innovative solutions and re-deploying old activities, jobs, and  
10 industries will be less susceptible to adversity.

11 Innovation is the key to remaining competitive globally,  
12 new and better jobs, and a resilient economy. The legislature  
13 recognizes this and supports research and development as the  
14 stimulant to our innovation economy.

15 The current law parallels, with enhancements tailored to  
16 Hawaii's unique position, the Internal Revenue Code, providing  
17 support for scientific experimentation through a tax credit at  
18 twenty per cent of the cost of the qualified research. The  
19 program cost to the State has averaged about \$11,000,000 per  
20 year over the last nine years, and in 2006, provided funding to  
21 over four hundred companies. This tax credit has been a great  
22 source of support for local companies, especially to the



1 research and development companies that are still in the start-  
 2 up or early growth stage, and is seen as helping to level the  
 3 playing field of our high-cost State, as Hawaii companies  
 4 compete with national and international competition. It has  
 5 also been useful in providing support for research and  
 6 development companies that are in the early growth stage and not  
 7 yet profitable, and have few sources of funding. Further, the  
 8 refundable element of the tax credit is helping to attract new  
 9 technology companies to Hawaii.

10 The purpose of this Act is to extend the income tax credit  
 11 for qualified research activities for an additional five years  
 12 and to add extensive reporting requirements related to the tax  
 13 credit.

14 SECTION 2. Section 235-110.91, Hawaii Revised Statutes, is  
 15 amended to read as follows:

16 **"§235-110.91 Tax credit for research activities.** (a)  
 17 Section 41 (with respect to the credit for increasing research  
 18 activities) and section 280C(c) (with respect to certain  
 19 expenses for which the credit for increasing research activities  
 20 are allowable) of the Internal Revenue Code shall be operative  
 21 for the purposes of this chapter as provided in this section;  
 22 except that references to the base amount shall not apply and



1 credit for all qualified research expenses may be taken without  
2 regard to the amount of expenses for previous years. If section  
3 41 of the Internal Revenue Code is repealed or terminated prior  
4 to January 1, [~~2011,~~] 2017, its provisions shall remain in  
5 effect for purposes of the income tax law of the State as  
6 modified by this section, as provided for in subsection [~~(j)~~]  
7 (n).

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

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

19 (d) Every qualified high technology business, before  
20 March 31 of each year in which qualified research and  
21 development activity was conducted in the previous taxable year,



1 shall submit a written, certified statement to the director of  
2 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 (e) The department shall:
  - 8 (1) Maintain records of the names and addresses of the  
9 taxpayers claiming the credits under this section and  
10 the total amount of the qualified research and  
11 development activity costs upon which the tax credit  
12 is based;
  - 13 (2) Verify the nature and amount of the qualifying costs  
14 or expenditures;
  - 15 (3) Total all qualifying and cumulative costs or  
16 expenditures that the department certifies; and
  - 17 (4) Certify the amount of the tax credit for each taxable  
18 year and cumulative amount of the tax credit.

19 Upon each determination made under this subsection, the  
20 department shall issue a certificate to the taxpayer verifying  
21 information submitted to the department, including the  
22 qualifying costs or expenditure amounts, the credit amount



1 certified for each taxable year, and the cumulative amount of  
2 the tax credit during the credit period. The taxpayer shall  
3 file the certificate with the taxpayer's tax return with the  
4 department.

5 The director of taxation may assess and collect a fee to  
6 offset the costs of certifying tax credit claims under this  
7 section. All fees collected under this section shall be  
8 deposited into the tax administration special fund established  
9 under section 235-20.5.

10 (f) As used in this section:

11 [~~"Basic research" under section 41(e) of the Internal~~  
12 ~~Revenue Code shall not include research conducted outside of the~~  
13 ~~State.]~~

14 "Qualified high technology business" means [~~the same as in~~  
15 ~~section 235-110.9.] a business employing or owning capital or  
16 property, or maintaining an office, in this State; provided that  
17 more than fifty per cent of its total business activities are  
18 qualified research and more than fifty per cent of its qualified  
19 research is in this State.~~

20 "Qualified research" [~~under~~] means the same as in section  
21 41(d)(1) of the Internal Revenue Code [~~shall not include~~  
22 ~~research conducted outside of the State].~~



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

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

12 (i) A qualified high technology business that claims a tax  
13 credit under this section shall complete and file with the  
14 director of taxation through the department website, an annual  
15 survey on electronic forms prepared and prescribed by the  
16 department. The annual survey shall be filed before June 30 of  
17 each calendar year following the calendar year in which the  
18 credit may be claimed under this section. The department may  
19 adjust the due date of the annual survey by rule.

20 A qualified high technology business that claims a tax  
21 credit under this section and wilfully fails to file the survey



1 by the due date shall be assessed a fine of not more than \$1,000  
2 for each month of failure to file.

3 (j) The annual survey shall include the following  
4 information for the time period or periods specified by the  
5 department:

6 (1) Identification of the industry sector or sectors in  
7 which the qualified high technology business conducts  
8 business, as set forth in paragraphs (2) to (8) of the  
9 definition of "qualified research" in section  
10 235-7.3(c);

11 (2) Qualified expenditures, if any, expended in the  
12 previous taxable year;

13 (3) Revenue and expense data;

14 (4) Hawaii employment and wage data, including the numbers  
15 of full- and part-time employees retained, new jobs,  
16 temporary positions, external services procured by the  
17 business, and payroll taxes;

18 (5) Filed intellectual property, including invention  
19 disclosures, provisional patents, and patents issued  
20 or granted; and





1       (6) Federal and state income tax returns and documents  
2           related to deductions for tax credits for research  
3           activities.

4       The department shall request information in each of these  
5       categories sufficient to measure the effectiveness of the tax  
6       credit. The department may request any additional information  
7       necessary to measure the effectiveness of the tax credit, such  
8       as information related to patents. In preparing the survey and  
9       requesting any additional information, the department shall  
10       ensure that qualified high technology businesses are not subject  
11       to duplicative reporting requirements.

12       (k) The department shall use information collected under  
13       this section and through other reporting requirements of the  
14       department to prepare summary descriptive statistics by  
15       category. The information shall be reported at the aggregate  
16       level to prevent compromising identities of qualified high  
17       technology business investors or other confidential information.  
18       The department shall also identify each qualified high  
19       technology business that is the beneficiary of tax credits  
20       claimed under this section. The department shall report the  
21       information required under this subsection to the legislature by  
22       September 1 of each year.



1        (1) The department shall use the information collected to  
2 study the effectiveness of the tax credit under this section.  
3 The department shall report on the amount of tax credits claimed  
4 and total taxes paid by qualified high technology businesses,  
5 the number of qualified high technology businesses in each  
6 industry sector, jobs created, external services and materials  
7 procured by the businesses, compensation levels, qualified  
8 research activities, and other factors as the department  
9 determines. The department shall report the results of its  
10 study to the legislature by December 1 of each year.

11        [~~i~~] (m) The director of taxation may adopt any rules  
12 under chapter 91 and forms necessary to carry out this section.

13        [~~j~~] (n) This section shall not apply to taxable years  
14 beginning after December 31, [~~2010-~~] 2016."

15        SECTION 3. Statutory material to be repealed is bracketed  
16 and stricken. New statutory material is underscored.

17        SECTION 4. This Act shall take effect on July 1, 2012, and  
18 apply to taxable years beginning after December 31, 2011.



**Report Title:**

Taxation; Technology; Tax Credit for Research Activities

**Description:**

Defines "qualified high technology business" to mean a business employing or owning capital or property, or maintaining an office, in this State; provided that more than fifty per cent of its total business activities are qualified research and more than fifty per cent of its qualified research is in this State; adds reporting requirements to measure the effectiveness of the tax credit for research activities; establishes a fine for failure to file the survey information in the reporting requirements; includes federal and state income tax returns and documents related to deductions for tax credits for research activities to be filed as part of the survey; extends the tax credit through 2016; applies to tax years beginning after 12/31/2011. (SD1)

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