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December 13, 2010

LETTER RULING NO. 2010-33
[REDACTED TEXT]
[REDACTED TEXT]
[REDACTED TEXT]
[REDACTED TEXT]

RE: APPLICATION OF CERTAIN TAX INCENTIVES TO [REDACTED TEXT]

Dear [REDACTED TEXT]:

This letter responds to your request of November 17, 2010 for a comfort ruling confirming that certain tax incentives are available if [REDACTED TEXT] (the "Company") meets the definition of a qualified high technology business ("QHTB").

In general, Hawaii offers the following tax incentives to qualifying businesses:

1. The high technology business investment tax credit under § 235-110.9, Hawaii Revised Statutes ("HRS");

2. The income tax exclusion for royalties and other income derived from patents and copyrights received by an individual or a QHTB and developed and arising out of a QHTB under § 235-7.3, HRS;

3. The income tax exclusion for stock options, dividends from stock, the receipt of the options, the exercise of the options, and income from the sale of the options under § 235-9.5, HRS; and

4. The tax credit for research activities under § 235-110.91, HRS.

In addition, other tax provisions may provide tax incentives to a QHTB that do not depend on whether the business meets the definition of a qualified high technology business.

SHORT ANSWER

Based on the information in your request for a high tech comfort ruling, the questionnaire, "Does a Company Qualify for Hawaii Tax Incentives?" ("Questionnaire"), and the representations made by the Company as stated below in this letter (the "Representations"), the Company will meet the definition of a qualified high technology business as defined in both

§ 235-7.3, HRS and § 235-110.9, HRS; provided the amount of cash invested in the Company does not exceed $2,400,000.

Based solely on the Representations, the Company qualifies as a QHTB for purposes of the tax benefits identified above in Paragraph 1.

Based solely on the Representations, the patents, copyrights, or trade secrets developed and arising out of the Company will qualify for the tax benefits identified above in Paragraph 2.

Based solely on the Representations, the Company's members will qualify for the tax benefits identified above in Paragraph 3, as further discussed in Part III of this letter.

Based solely on the Representations, the Company's research activities are eligible for the tax benefits identified above in Paragraph 4, as further discussed in Part IV of this letter.

FACTS REPRESENTED BY THE COMPANY

The Company makes the following representations:

The Company represents that it is involved in software development incorporating all phases of software development activity.

The Company will develop and design computer software using fourth generation or higher software development tools or native programming languages to design and construct unique and specific code to [REDACTED TEXT].

Specifically, the Company will develop software that will [REDACTED TEXT]. The software will also be specifically designed for [REDACTED TEXT].

The Company has [REDACTED TEXT].

The Company's software is for ultimate commercial sale, lease, franchise and/or license, and is not merely adaptations of existing business components. The Company will not be engaged in the customization of the software for individual customers as part of its qualified research activities.

The Company has made additional representations, in Exhibit A, regarding jobs, Hawaii costs, tax incentives that may be claimed by the Company or its investors, long term business plans, and investments.

LAW AND ANALYSIS

The requirements for these tax incentives and their application to the Company are discussed below.

I. High technology business investment tax credit

For investments made in taxable years beginning after December 31, 2000, but before taxable years beginning after December 31, 2010, a nonrefundable high technology business investment tax credit of up to $2,000,000 per taxpayer is available.[1] The credit is graduated over five years (35% to 10%) from the date of the "investment"[2] in a QHTB. The credit is capped at varying amounts ($700,000 in the year the investment is made to $200,000 in the last year). Some of the credit claimed will be recaptured in certain circumstances. If the tax credit exceeds the taxpayer's income tax liability for any of the five years that the credit is taken, the excess of the tax credit over liability may be used as a credit against the taxpayer's income tax liability in subsequent years until exhausted.

Act 178 SLH 2009 added additional restrictions for investments received on or after May 1, 2009, including:

- Not more than 80% of a taxpayer's tax liability may be offset by utilizing such credits for tax years ending on or before December 31, 2010;
- No carryover of any unused credits from investments made on or after May 1, 2009 for tax years ending on or before December 31, 2010;
- The credit must be taken ratably over the five year period in accordance with §235-110.9(a), HRS and may not exceed an Investment Tax Credit Allocation ratio of 1:1; and
- IRC § 704(b)(2) is operative for partnership allocations of the High Technology Business Investment Tax ("HTBIT") credits received from investments made by the partnership into a QHTB.

The purpose of the amendment to HRS § 235-2.45(d) made by Act 178 SLH 2009 was to require partnerships to allocate HTBIT credits in proportion to the amounts of partners' investments in the partnership attributable to the QHTB investments made by the partnership for

[1] Taxpayers may continue to claim the credit in taxable years beginning after December 31, 2010 if the five-year period to claim the credit commences in taxable years beginning before January 1, 2011.

[2] "Investment" is defined as "a nonrefundable investment, at risk, as that term is used in section 465 (with respect to deductions limited to amount at risk) of the Internal Revenue Code, in a qualified high technology business, of cash that is transferred to the qualified high technology business, the transfer of which is in connection with a transaction in exchange for stock, interests in partnerships, joint ventures, or other entities, licenses (exclusive or nonexclusive), rights to use technology, marketing rights, warrants, options, or any items similar to those included in this definition, including but not limited to options or rights to acquire any of the items included in this definition. The nonrefundable investment is entirely at risk of loss where repayment depends upon the success of the qualified high technology business. If the money invested is to be repaid to the taxpayer, no repayment except for dividends or interest shall be made for at least one year from the date the investment is made. The annual amount of any dividend and interest payment to the taxpayer shall not exceed twelve per cent of the amount of the investment." *See* § 235-1, HRS.

investments made on or after May 1, 2009. This is consistent with the underlying purpose of IRC § 704(b), which is to have tax consequences follow economics. *See McKee, Nelson & Whitmire*, *Federal Taxation of Partnership and Partners*, Paragraph 11.02[2] (4th ed. 2007).

HTBIT credits are generated at the time of investment and not at the point of expenditure which may be in a later tax year and is generated without respect to the day of the year. Therefore, a calendar year investor who makes a QHTB investment on December 31st of a year would be entitled to the full credit of 35% of their investment in the year of investment, even though the investment was made on the last day of the tax year of the investor.

Some of the credits claimed will be recaptured from the investor if at the close of any taxable year in the five-year period: (1) the Company no longer qualifies as a QHTB, (2) the Company or an interest in the Company is sold by the taxpayer investing in the QHTB, or (3) the taxpayer withdraws the taxpayer's investment wholly or partially from the QHTB.

The recapture will be equal to ten percent of the amount of the total tax credit claimed for the investment in the two taxable years prior to the year in which any of the aforementioned events occurs. The recaptured amount must be added to the investor's tax liability for the taxable year in which the recapture occurs.

If a QHTB accepts any investments after June 30, 2007, the QHTB is required to file an annual survey as described in Act 206 (Session Laws of Hawaii, 2007). Failure to file the survey when due may result in a penalty of $1,000 per month for each month the annual survey is not filed, not to exceed a total of $6,000 for any annual survey not filed. Furthermore, by accepting an investment for which an investment credit allowed under section 235-110.9, HRS may be claimed, the QHTB is deemed by statute to have consented to the public disclosure of the Company's name and status as a beneficiary of the investment credit.

To be considered a QHTB for purposes of this tax credit, in each of the years for which the credit will be claimed, the Company must employ or own capital or property, or maintain an office, in Hawaii and:

(1) More than 50% of its total business activities must be qualified research and more than 75% of its qualified research must be conducted in Hawaii (the "Activity Test"); or

(2) More than 75% of its gross income must be derived from qualified research and the income from this qualified research must be received from:

(a) Products sold from, manufactured in, or produced in Hawaii; or

(b) Services performed in Hawaii (the "Gross Income Test").[3]

[3] This definition of a QHTB for purposes of § 235-110.9 differs from the definition of a QHTB in § 235-7.3, HRS, which is discussed in Part II of this letter.

If the Company contracts with another person to perform qualified research, the research will qualify as research performed by the Company for the purpose of determining the Company's status as a QHTB only if the contract meets the following requirements:

(1) The contract must be entered into before the performance of the qualified research activity;

(2) The contract requires the Company to bear the expense of the research even if the project is unsuccessful;

(3) The contract provides that the research is to be performed on behalf of the Company and the Company will have substantial rights to the research results[4]; and

(4) The contract provides that the company performing the research will not claim the Hawaii qualified high technology business investment credit under HRS §235-110.9 or the Hawaii tax credit for research activities under HRS §235-110.91 for the activities performed on behalf of the Company.

If another person contracts with the Company to have the Company perform qualified research, the research will not qualify as research performed by the Company for the purpose of determining the Company's status as a QHTB if the above requirements have been met in favor of the other person, even if the other person is not a QHTB.

The Department has also released Tax Information Release ("TIR") 2008-04 (Certain Prototype Costs that may be Eligible for the Hawaii Tax Credit for Research Activities under HRS § 235-110.91) and Announcement 2008-07 (High Tech Comfort Rulings Relying on the Gross Income Test), which are incorporated by reference herein.

A. The Company's presence in Hawaii

The Company, a [REDACTED TEXT] organized under the laws of [REDACTED TEXT], represents that it maintains an office at [REDACTED TEXT] Hawaii. Therefore, for purposes of § 235-110.9, HRS, the Company meets the requirement that it employ or own capital or property or maintain an office in Hawaii.

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[4] If the Company receives a license, the term of the license must be for the useful life of product(s) or research.

B. The Company's qualified research activities

The term "qualified research" means:[5]

(1) The same as in § 41(d), Internal Revenue Code ("IRC");

(2) The development and design of certain computer software;

(3) Biotechnology;

(4) Performing arts products;

(5) Sensor and optic technologies;

(6) Ocean sciences;

(7) Astronomy; or

(8) Nonfossil fuel energy-related technology.

(1) The same as in §41(d), IRC

Item (1) of the definition of qualified research above is drawn from IRC §41(d), where it is defined as research undertaken to discover information technological in nature, which constitutes a process of experimentation relating to a new or improved function, performance, reliability, or quality.

"Qualified research" activities must satisfy the following tests under Treasury Regulation §1.41-4:

(a) The expenditures must qualify as research and experimental expenditures under IRC §174;

(b) The expenditures must relate to research undertaken to discover information that is both technological in nature and the application of which is intended to be useful in developing a new or improved business component of the taxpayer;[6] and

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[5] Section 235-110.9, HRS, incorporates the definition of "qualified research" in § 235-7.3, HRS.

[6] Treasury Regulation §1.41-4(3)(i), provides that "[r]esearch is undertaken for the purpose of discovering information if it is intended to eliminate uncertainty concerning the development or improvement of a business component. Uncertainty exists if the information available to the taxpayer does not establish the capability or method for developing or improving the business component, or the appropriate design of the business component. "

(c) Substantially all of the activities of the research must constitute elements of a process of experimentation.[7]

§41(d), IRC, further clarifies that qualified research does not include any research:

(a) Conducted after the beginning of commercial production of the business component;

(b) Related to the adaptation of existing business components;

(c) Related to the reproduction of existing business components;

(d) Surveys, studies, market research, etc.;

(e) Conducted outside of the United States;

(f) In the social sciences, arts, or humanities; or

(g) To the extent funded by any grant, contract, or otherwise by another person (or governmental entity).

Hawaii's law conforms to the federal definition of "qualified research" as set forth in §41(d), IRC, and the accompanying Treasury Regulations. Thus, the Company's activities must meet the federal standards of "qualified research" to be classified as such under Hawaii law.

If some of the work is funded by grant, contract, or otherwise by another person or governmental entity, to the extent the work is funded, the requirements of item (1) of qualified research are not met unless the Company retains substantial rights to their research, as defined in

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[7] Treasury Regulations further define a *process of experimentation* as "a process designed to evaluate one or more alternatives to achieve a result where the capability or the method of achieving that result, or the appropriate design of that result, is uncertain as of the beginning of the taxpayer's research activities. A process of experimentation must fundamentally rely on the principles of the physical or biological sciences, engineering, or computer science and involves the identification of uncertainty concerning the development or improvement of a business component, the identification of one or more alternatives intended to eliminate that uncertainty, and the identification and the conduct of a process of evaluating the alternatives (through, for example, modeling, simulation, or a systematic trial and error methodology). A process of experimentation must be an evaluative process and generally should be capable of evaluating more than one alternative. A taxpayer may undertake a process of experimentation if there is no uncertainty concerning the taxpayers capability or method of achieving the desired result so long as the appropriate design of the desired result is uncertain as of the beginning of the taxpayers research activities. Uncertainty concerning the development or improvement of the business component (e.g., its appropriate design) does not establish that all activities undertaken to achieve that new or improved business component constitute a process of experimentation."

The *substantially all* requirement is satisfied only if 80% or more of the research activities measured in cost or other consistently applied reasonable basis constitutes elements in a process of experimentation.

§1.41-4A(d)(2), Treasury Regs., and the funding is contingent upon the success of the research. §1.41-4A(d)(1), Treasury Regs.

Where a taxpayer bears the risk of loss with respect to a research project, the project will not otherwise be deemed to be funded and, thus, non-qualifying under §41(d), IRC. *See Fairchild Indus., Inc. v. U.S.*, 71 F.3d 868, 873-74 (Fed. Cir. 1995) ("The statute is designed so that those who bear the risk of financial loss can include the tax credit in their calculation of investment risk.") The Company must also retain "substantial rights to its research." *See* §1.41-4A(d)(2), Regs. *See Lockheed Martin Corp. v. U.S.,* 85 A.F.T.R.2d 2000-1495, 1502 (Fed. Cir. 2000).

The Company has represented that more than 80% of its qualified research activities in this category will constitute elements in a process of experimentation as that term is defined in § 41(d), IRC. The Company represents that there is uncertainty as to capability and design, including as to the development and implementation of the Company's applications having the capability to meet the proposed specifications and functional requirements of the product.

In Part I of the Questionnaire, the Company checked the box indicating that it performs research as defined in § 41(d), IRC. By checking this box, the Company represents that it performs research as defined in § 41(d), IRC, and specifically represents the following:

- The Company is developing or improving a business component;
- The Company is employing an evaluative process designed to eliminate uncertainty concerning a new or improved function, the performance, reliability, or the quality of that business component;
- The Company's research activities regarding that business component fundamentally rely on principles of the physical or biological sciences, engineering, or computer science;
- The Company is not in commercial production; is not adapting or reproducing existing business components; and is not performing surveys or market research;
- The Company's work is not in the social sciences, arts, or humanities;
- The Company's research activities are not funded by or through any grant, contract, or otherwise by another person or governmental entity; and
- The Company's research activities do not include any activities specifically excluded from the definition of "qualified research" by § 41(d)(4), IRC.

Based solely on the Representations, the Company performs qualified research as defined in § 41(d), IRC.

(2) The development and design of certain computer software

"Qualified Research" includes 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 must have substantial control and retain substantial rights to the resulting intellectual property.

The Company represents that its software is for ultimate commercial sale, lease, and/or license, and that it will own or have substantial control over all rights to the resulting intellectual property. The Company will develop and design computer software that will conduct site assessment, interface with computer aided design, and manage the development and integration of renewable energy systems.

In Part I of the Questionnaire, the Company checked the box indicating that it develops and designs computer software. By checking this box, the Company represents that it meets the requirements of Item (2) of qualified research.

C. Activity Test and Gross Income Test

Under § 235-110.9, HRS, in order for a company performing qualified research to meet the definition of a QHTB, it must be a business employing or owning capital or property, or maintaining an office, in the State of Hawaii. In addition, the company must meet the requirements of either the Activity Test or the Gross Income Test. Under the Activity Test, a company is a QHTB if more than 50% of its total business activities are qualified research and more than 75% of such qualified research is conducted in Hawaii. Under the Gross Income Test, a company is a QHTB if more than 75% of its gross income is derived from qualified research in the form of either (i) products sold from, manufactured in, or produced in Hawaii, or (ii) services performed in Hawaii.

Due to the highly fact intensive nature of qualifying as a QHTB under the Gross Income Test, including the uncertainty and ambiguity of: 1) revenue streams associated with qualified research; 2) determining the source of product sales; 3) manufacturing or production quantification; as well as 4) the extent services are performed in the State within the meaning of HRS § 235-110.9(g), the Department will not issue rulings determining whether a business satisfies the Gross Income Test for purposes of qualifying as a QHTB.

The Company represents in Part A, above, that it maintains an office in Hawaii.

The Company represents that it will meet the Activity Test because more than 50% of its activities will be in qualified research and more than 75% of those qualified research activities will be conducted in Hawaii. In making this determination, the Company used a numerator that contained the costs of activities in direct support of qualified research and a denominator that included all costs for all activities.[8] Furthermore, as to the requirement that 75% of the qualified research activities be conducted in Hawaii, the Company used a numerator that contained all costs incurred in direct support of qualified research activities conducted in Hawaii and a denominator that contained all costs incurred for all qualified research activities. In making these representations about the Activity Test, the Company understands that the following activities do not count as qualified research activities for purposes of this test:

- Activities associated with research that is funded by grants and in which the Company has no substantial risks and rights;
- Activities associated with research being performed by the Company pursuant to a contract in which the contract requirements discussed in Part I, above, have been met in favor of another party to the contract; and
- Activities performed by another business on behalf of the Company where the contract requirements discussed in Part I, above, have not been met in favor of the Company.

Based on the Representations, the Company is a QHTB for purposes of the high technology business investment tax credit because it meets the requirements of Items (1) and (2) in the definition of "qualified research," the Company will maintain an office in Hawaii, and the Company satisfies the Activity Test. Solely based on the Representations, investments (as defined in HRS § 235-1) in the Company will qualify for the high technology business investment tax credit.

Pursuant to Announcement 2008-07, the Department makes no determination as to whether the Company qualifies under the Gross Income Test.

D. Credit Recapture

Section 235-110.9(d), HRS, provides for recapture of credits that have been claimed by a taxpayer where one of the following three events occurs (recapture event):

(1) The business no longer qualifies as a QHTB;
(2) The business or an interest in the business has been sold by the taxpayer investing in the QHTB;
(3) The taxpayer has withdrawn the taxpayer’s investment wholly or partially from the QHTB.

Where recapture is triggered, 10% of the amount of the total tax credit claimed by the selling or withdrawing investor in each of the two taxable years prior to the year in which recapture occurs must be added to such investors’ tax liability for the taxable year in which the recapture occurs.

[8] "Business activities" may be measured by the cost of these activities, the time spent on these activities, or another consistently applied reasonable basis. This statement is based upon general principles in the income tax and general excise tax law. Whatever the measure adopted by the taxpayer, the measure must reasonably reflect business realities.

The credit cannot be claimed in the year of a recapture event because investors do not have an investment in a QHTB. If a recapture event occurs, the Company should notify the investors that they are not eligible to claim the credit and that some of the credit claimed in prior years shall be recaptured.

E. Credit Allocation

For investments made on or after May 1, 2009, allocations, special or otherwise, of credits may not exceed the amount of the investment made by the taxpayer ultimately claiming this credit; and investment tax credit allocation ratios greater than one dollar of credit for every dollar invested shall not be allowed.

II. Income tax exclusion for royalties and other income from QHTB

Pursuant to § 235-7.3, HRS, an income tax exclusion is available for income received by an individual or a QHTB[9] as royalties and other income derived from any patents, copyrights, and trade secrets developed and arising out of a QHTB.[10] The exclusion may be claimed by the individual or QHTB that owns the patents, copyrights, or trade secrets. For purposes of the royalty income exclusion, a QHTB is defined as "a business conducting more than 50% of its activities in qualified research."[11]

As discussed in Part I, relating to the high technology business investment tax credit, the Company's representations meet the requirements of Items (1) and (2) in the definition of "qualified research." The Company also represents that more than 50% of the Company's activities are in qualified research, again using a numerator that contained the costs of qualified research activities and a denominator that included all costs for all activities. Based on the Representations, royalties and other income derived from any patents, copyrights, and trade secrets developed and arising out of the Company received by an individual[12] or a QHTB may be excluded from income tax.

[9] If the QHTB receiving the income is treated as a partnership for income tax purposes, then the partners or members of the QHTB may exclude the allocated portion of such income, even if the partner or member excluding the income is not an individual or QHTB.

[10] Expenses for royalties and other income derived from any patents, copyrights, and trade secrets by an individual or a QHTB as defined in § 235-7.3, HRS, are deductible. *See* § 235-2.4(g), HRS.

[11] This definition differs from the definition of a QHTB in § 235-110.9, HRS, which is discussed in Part I of this letter.

[12] The performing arts product exclusion in § 235-7.3, HRS, is applicable to the author and assignors, licensors, and licensees.

III. Income tax exclusion for stock options from qualified high technology business

Section 235-9.5, HRS, provides an exclusion for "all income earned and proceeds derived from stock options or stock," including stock issued through the exercise of stock options or warrants, from a QHTB or from a holding company of a QHTB[13] by an employee, officer, or director of the QHTB, or investor who qualifies for the high technology business investment tax credit in §235-110.9, HRS, effective for taxable years beginning after December 31, 2000. This exclusion is applicable to dividends from stock or stock received through the exercise of stock options or warrants, the receipt or the exercise of stock options or warrants, and income from the sale of stock, including stock issued through the exercise of stock options or warrants.[14]

For purposes of this income tax exclusion, a QHTB means the same as defined in §235-7.3, HRS, relating to the income tax exclusion for royalties.

The Company meets the requirements of Items (1) and (2) in the definition of "qualified research" based upon the discussion in Part I relating to the high technology business investment tax credit.

Based on the Company's representations, more than 50% of the Company's activities will be in qualified research.

Based on these facts, dividends from stock or stock received through the exercise of stock options or warrants, the receipt or the exercise of stock options or warrants, and income from the sale of stock, including stock issued through the exercise of stock options or warrants, issued by the Company or a holding company of the Company received by an employee, officer, director, or investor (who qualifies for the high technology business investment tax credit) are excluded from income tax.

IV. Tax credit for research activities

The tax credit for research activities in Hawaii provided under § 235-110.91, HRS, is similar to the federal credit for increasing research activities under §41, IRC. The Hawaii credit is available for tax years 2000-2010 for research done in the State. Unlike the federal credit, the Hawaii credit may be claimed without increasing research expenses for tax years 2001 to 2010 and the 20% Hawaii credit is refundable (the federal credit is nonrefundable).

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[13] A holding company of a QHTB means any business entity that possesses:

(1) At least eighty per cent of the total voting power of the stock or other interest; and

(2) At least eighty per cent of the total value of the stock or other interest in the qualified high technology business.

[14] §165, IRC, is operative for Hawaii income tax purposes and applies to losses sustained from the sale of stock issued through stock options or warrants granted by a QHTB. *See* §235-2.4(d), HRS.

As discussed in Part I of this letter, Hawaii tax law conforms to the federal definition of "qualified research" as set forth in §41(d), IRC, and accompanying Treasury Regulations. Based solely on the Representations, as discussed in Part I of this letter, the Company is eligible to claim the Hawaii tax credit for its research activities conducted in Hawaii; provided that it has "qualified research expenses," as that term is defined in § 41(b), IRC. Because the determination of whether any expense of the Company is a "qualified research expense" is particularly fact intensive and outside the scope of this ruling, this ruling does not express an opinion on whether any of the expenses of the Company will be "qualified research expenses." Furthermore, if the Internal Revenue Service determines that the Company's activities fail to satisfy the definition of "qualified research" in IRC § 41(d), then those activities will also be ineligible for the Hawaii tax credit in HRS § 235-110.91.

V. Miscellaneous provisions

Act 221, SLH 2001, provides additional tax incentives, which are not dependent on the Company qualifying as a QHTB.

- **Technology infrastructure renovation tax credit.** A nonrefundable income tax credit of 4% of the "renovation costs" for each commercial building located in Hawaii is available for tax years 2001 through 2010. "Renovation costs" means costs incurred after December 31, 2000, to plan, design, install, construct, and purchase technology-enabled infrastructure equipment to provide a commercial building with technology-enabled infrastructure. Act 178, Session Laws of Hawaii 2009, also limits this credit to 80% of the taxpayer's tax liability for renovation costs incurred on or after May 1, 2009 and on or before December 31, 2010.

- **Expanded related entities exemption**. The related entities exemption which exempts from the general excise tax (GET) amounts received, charged, or attributable for "services" or interest between one "related entity" and another "related entity" is expanded. The use of computer software and hardware, information technology services, and database management between related entities is exempt from the GET. These changes are applicable to gross income or gross proceeds received beginning July 1, 2001.

VI. Conclusion

Based solely on the information and representations submitted, the Company qualifies for:

1. The high technology business investment tax credit under §235-110.9, HRS;

2. The income tax exclusion for royalties and other income derived from patents and copyrights received by an individual or a QHTB and developed and arising out of a QHTB under §235-7.3, HRS;

3. The income tax exclusion for income earned and proceeds derived from stock options or stock, including income from dividends from stock or stock received through the exercise of stock options or warrants, the receipt or exercise of stock options or warrants, and the sale of stock options or stock, including stock issued through the exercise of stock options or warrants, under §235-9.5, HRS;

4. The tax credit for research activities under §235-110.91, HRS; and

5. Other miscellaneous tax provisions.

This ruling is applicable only to the Company, and shall not be applied retroactively. It may not be used or cited as precedent by any other taxpayer, and is based on our understanding of the facts that you have represented, and only applies if the amount of cash investments received by the Company does not exceed $2,400,000. In the event that the Company finds it necessary to increase the amount of investment monies to be obtained which qualifies for the high technology business investment tax credit, the Company shall submit a supplemental ruling request to the Department. No user fee shall be assessed on such supplemental ruling request.

HRS § 235-110.9(k) provides that the high technology business investment tax credit does not apply to taxable years beginning after December 31, 2010. All investments must conform to this provision to be eligible for the investment credit.

If it is later determined that our understanding of these facts is not correct, the facts are incomplete, or the facts later change in any material respect, the conclusion in this letter will be modified accordingly. This ruling also may be subject to change due to future amendments to laws, rules, or official Department positions.

The Company has reviewed and agreed that the redacted version of this ruling attached as Exhibit B will be available for public inspection and copying.

If you have any further questions regarding this matter, please call me at 808-587-1569. Additional information on Hawaii's taxes is available at the Department's website at www.state.hi.us/tax.

Very truly yours,

JOSEPH B. TICHY
Administrative Rules Specialist

APPROVED BY:

JOHNNEL NAKAMURA
Rules Officer [REDACTED TEXT]