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GOVERNOR

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STATE OF HAWAII
DEPARTMENT OF TAXATION
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FREDERICK D. PABLO
DIRECTOR OF TAXATION

RANDOLF L. M. BALDEMOR
DEPUTY DIRECTOR

January 6, 2012

Letter Ruling No. 2012-02

[redacted text]

Re: Exemption of Certain Scientific Contracts with the United States

Dear [redacted text]:

By letter dated September 16, 2011, [redacted text] ("Taxpayer"), requested the State of Hawaii Department of Taxation (the "Department") rule on the proper treatment of gross proceeds derived from the performance of scientific work under a contract entered into with the United States under section 237-26 of the Hawaii Revised Statutes ("HRS").

SHORT ANSWER

Based on Taxpayer's representations, Taxpayer is performing scientific work under the contract and therefore Taxpayer's gross proceeds derived from the performance of that portion of the contract which constitutes scientific work are exempt from general excise tax under HRS § 237-26.

FACTS REPRESENTED BY TAXPAYER

1. Taxpayer Information

[redacted text]

2. Description of Taxpayer's Business Operations

Taxpayer leases office space to the National Oceanic and Atmospheric Administration (NOAA).

3. Facts Relating to the Transaction

On [redacted text], a lease agreement was entered into between Taxpayer, as owner and lessor, and the General Services Administration (GSA), as lessee, to provide a space [redacted text] (the "Facility"). As part of the agreement, Taxpayer is to provide design, installation, supervision, and construction for the leased space based on

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specific requirement set by the lessee. To complete this work Taxpayer solicited bids for goods and services from numerous contractors and subcontractors. The leased space will be occupied and used as a scientific facility by NOAA and National Marine Fisheries Service Pacific Island Regional Office (NMFS). The primary purpose and use of this leased facility are documented in a memo from [redacted text], attached as **Exhibit A** and incorporated by reference herein.

Exhibit A states that NOAA/NMFS will use the facility to conduct [redacted text] science. Specifically, NOAA/NMFS will use the facility to [redacted text].

LAW AND ANALYSIS

HRS § 237-26 states:

- (a) Any provision of law to the contrary notwithstanding, there shall be exempted from the measure of the taxes imposed by chapter 237, all of the gross proceeds derived by a contractor or subcontractor arising from the performance of any scientific work as defined in subsection (b), under a contract or subcontract entered into with the United States (including any agency or instrumentality thereof but not including national banks), and all of the gross proceeds derived from the sale of tangible personal property by a seller of such tangible personal property which is to be affixed to, or to become a physical, integral part of the scientific facility, or which is to be entirely consumed during the performance of the service required by the contract or subcontract.
- (b) For purposes of this section, "scientific work" is work involving primarily the research and development for, or the design, manufacture, instrumentation, installation, maintenance, or operation of aerospace, agricultural, astronomical, biomedical, electronic, geophysical, oceanographic, test range, or other scientific facilities. Maintenance or operation, for purposes of this section, shall include housekeeping functions in providing certain nonscientific logistic and support services.

Taxpayer's gross proceeds from the design, manufacture, instrumentation, installation, maintenance and operation of the Facility are exempt from general excise tax under HRS § 237-26.

First, the work is being performed under a contract with the United States. Based on Taxpayer's representations, it has entered into a contract with NOAA and NMFS via the GSA.

Second, Taxpayer is performing scientific work. HRS § 237-26(b) defines scientific work as including "design, manufacture, instrumentation, installation, maintenance, or operation of ... agricultural, ... oceanographic, ... or other scientific facilities." Based on Taxpayer's representations, the Facility will be a scientific facility, and under its agreement with NOAA/NMFS Taxpayer will be required to design, construct (manufacture), install, and

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supervise (operate) the Facility. Therefore, Taxpayer will be performing scientific work under HRS § 237-26.

Thus, Taxpayer will be performing scientific work, and doing so under a contract with the United States. Any gross proceeds from the scientific work of designing, manufacturing, instrumenting, installing, maintaining or operating the Facility pursuant to the contract with NOAA/NMFS are exempt from general excise tax. However, any gross proceeds that constitute mere rental income are not exempt, as leasing of scientific facilities is not scientific work. Gross income under the contract is exempt only to the extent it is received for design, manufacture, instrumentation, installation, maintenance or operation of the Facility, and not merely for the leasing of the Facility.

Additionally, any subcontractors Taxpayer may enter into contract with in order to help it meet its contractual obligations to design, manufacture, instrument, install, maintain or operate the Facility may also potentially qualify for this exemption, so long as those subcontractors are also performing scientific work. However, the Department does not rule on the taxability of any of Taxpayer's subcontractors at this time.

The conclusion reached in this letter is based on our understanding of the facts that you have represented. 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 Taxpayer has reviewed the redacted version of this ruling and agreed that it will be available for public inspection and copying.

If you have any further questions regarding this matter, please call me at 808-587-5334.

Sincerely,

JACOB L. HERLITZ
Administrative Rules Specialist