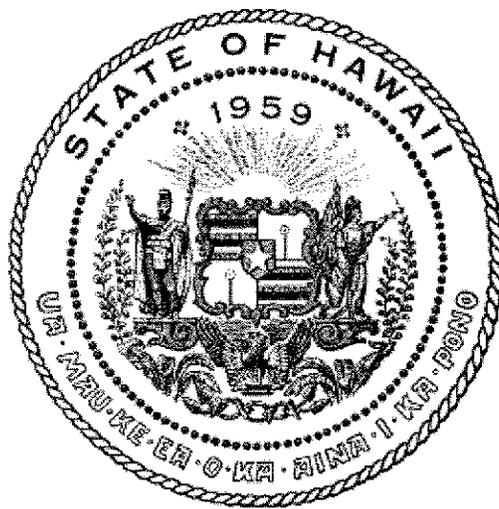


**Report on the Operations of
Qualified High Technology Businesses
From 2002 Through 2006**



**Department of Taxation
State of Hawaii
October 2007**

STATE OF HAWAII
Linda Lingle, Governor

DEPARTMENT OF TAXATION
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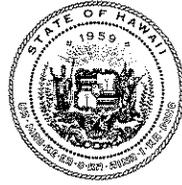
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Web Site: <http://www.hawaii.gov/tax>

LINDA LINGLE
GOVERNOR

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October 19, 2007

The Honorable Linda Lingle
Governor
State of Hawaii

Dear Governor Lingle:

I am pleased to present you with this **Report on the Operations of Qualified High Technology Businesses From 2002 Through 2006** as required by Act 206, SLH 2007.

On June 21, 2007, House Bill 1631 HD2, SD2, CD 1, was signed into law as Act 206. The purpose of Act 206 is to measure the effectiveness of the Act 178/221/215 business investment tax credit. The act requires any qualified high technology business (QHTB) that accepts an investment for which a credit may be claimed under Section 235-110.9, Hawaii Revised Statutes (HRS), to complete a survey that must be provided to the Department of Taxation by June 30 of each year for each of the five years following the year of investment.

The survey is to be filed electronically through the Department's website. The Department is required to report the information by providing summary statistical information. The report is due by September 1 of each year. The Department is currently finalizing the survey form, which should be ready for implementation early in 2008. This on-line survey will be used to gather information for the 2007 and later calendar years.

Act 206, SLH 2007 also requires that the Department prepare a report by October 31, 2007 summarizing the data submitted by QHTBs on Form N-317 prior to Act 206, SLH 2007. The report is to include summary statistics of the information provided, to date. The present report was compiled in order to satisfy this requirement.

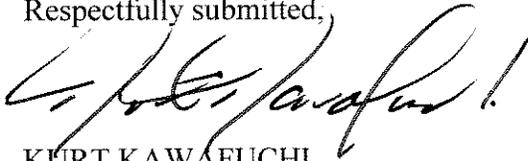
Some highlights:

- A total of 287 separate QHTBs filed Form N-317 at one time or another over the period from 2002 through 2006.
- Total expenses incurred in Hawaii by the QHTBs totaled \$1.043 billion over the period from 2002 through 2006.
- Investments received by the QHTBs totaled \$821.6 million over the same period.
- QHTBs that reported operations solely in the Performing Arts sector received about 35 percent of the investments received by all QHTBs (\$284.7 million) over the same period.
- Computer Software is the most frequently listed activity of the QHTBs.

- In 2006, the 157 QHTBs that filed Form N-317 reported paying 2,322 employees that year; the average of the employee salaries was \$56,262.
- In 2006, the 157 QHTBs that filed Form N-317 reported that they created 5,383 jobs since their inceptions.
- Total High Technology Business Investment Tax Credit claimed by Hawaii residents totaled \$195.6 million over the period from 1999 through 2005.

This report was prepared under the direction of Dr. Tu Duc Pham, Tax Research and Planning Officer, with the assistance of the Tax Research and Planning Office's staff: Glenn Ifuku, High Technology Study Technical Coordinator; Yvonne Chow, Economist; Lynn Ma, Research Statistician; the Rules Office's staff: Johnnel Nakamura, Rules Officer; Jason Healey, Rules Specialist – who compiled the summary and history of the High Technology Business Investment Tax Credit and Tax Credit for Research Activities; Betty Lam, Rules Specialist; Donald Rousslang, Tax Specialist – who compiled the tables and drafted the initial report; and Titin Sakata, Special Assistant to the Director.

Respectfully submitted,



KURT KAWAFUCHI
Director of Taxation

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REPORT ON THE OPERATIONS OF QUALIFIED HIGH TECHNOLOGY BUSINESSES FROM 2002 THROUGH 2006

I. Introduction

This report was prepared pursuant to Act 206, Session Laws of Hawaii (SLH) 2007. The Act directs the Department of Taxation (DOTax) to summarize data that were provided by qualified high technology businesses (QHTB's) on Form N-317 ("Statement by a Qualified High Technology Business") and to make a report to the Legislature by October 31, 2007. The report is to cover all tax years for which data are available and is to include descriptive statistics on the qualified research activities of the high technology businesses, on the jobs they created and on the salaries they paid. Accordingly, this report presents data taken from Form N-317 filed for calendar years 2002 through 2006. The data are aggregated to prevent disclosing confidential taxpayer information. The report also presents data extracted from the tax forms that investors use to claim the high technology business investment tax credit, in order to provide information on the revenue cost of the tax credit.

The remainder of the report is organized as follows. Section II describes the data that were extracted from Form N-317 on the operations of the QHTB's. Section III presents some important caveats that will help the reader avoid drawing erroneous conclusions from the data on Form N-317. Section IV describes the data that were extracted from the tax forms that investors use to claim the high technology business investment tax credit. Section V presents highlights from the data on QHTB operations and on the high technology business investment tax credits that have been claimed. Appendix I presents tables summarizing the data, Appendix II provides figures that

depict selected statistics, Appendix III provides a history of the high technology business investment tax credit and the tax credit for research activities, and Appendix IV contains copies of the tax forms from which DOTax extracted the data for this report.

II. The Data on QHTB Operations

Data on operations of the QHTB's are from Form N-317. For the present study, DOTax extracted the following items from the Form:

- (A) The year the QHTB began doing business in Hawaii,
- (B) The qualified research activities the QHTB performed during the calendar year,¹
- (C) The number of jobs the QHTB created since its inception,
- (D) The number of jobs the QHTB created during the calendar year,
- (E) The total salaries the QHTB paid,
- (F) The number of employees the QHTB paid in the calendar year,
- (G) Whether part of the salary paid by the QHTB was paid in the form of stock options or other property,
- (H) The costs the QHTB incurred in Hawaii during the calendar year,
- (I) The total amount of investments the QHTB received in the calendar year,
- (J) The number of investors that invested in the QHTB, and
- (K) Whether the QHTB claimed, or expected to claim the tax credit for research activities provided by section 235-110.91 of the Hawaii Revised Statutes.

Form N-317 was introduced in 2002 to collect data on the operations of the QHTB's in each calendar year. While the Form was essentially unchanged from 2003 through 2006, there were certain differences. For example, the Form for 2002 did not ask for the number of employees paid, so the item could not be tabulated for 2002; however, such data was added to the Form for 2003-2006. Also, the Form for 2002 asked the respondent to provide information on the QHTB's actual operations in calendar year 2002

¹ The respondent was asked to classify the activities of the QHTB into one or more of the following categories: (1) The same as in section 41(d) of the Internal Revenue Code; (2) Biotechnology, as defined in section 235-1, Hawaii Revised Statutes (HRS); (3) Performing arts products, as defined in section 235-7.3(c), HRS; (4) Sensor and optic technologies; (5) Ocean sciences; (6) Astronomy; (7) Nonfossil fuel energy related technology; and (8) the development and design of computer software, as defined in section 235-1, HRS. (The 2004 Legislature amended the definition of computer software.)

or its proposed activities for calendar year 2003. From 2003-2006, the Form modified the question by only asking for the QHTB's *actual* operations in the calendar year.² Tables 1 through 7 summarize the data that were extracted from Form N-317. The data are aggregated by activity of the QHTB in order to prevent disclosing confidential taxpayer information. The aggregation scheme is as follows: QHTB's that listed only one activity were classified in the activity. QHTB's that listed IRC Section 41(d) and one other activity were classified in the other activity. Otherwise, QHTB's that listed two or more activities were classified in "Multiple Activities." If presenting the aggregate data for an activity risked disclosing operations of any single QHTB, then the activity was merged with "Multiple Activities" to create the classification "Multiple Activities and Others." Table 1 shows only the data on actual operations of the QHTB's in 2002; the data on their prospective operations for 2003 are not included. In addition to the items described in (A) through (K) above, the tables also show average and median salaries for each activity in each year except 2002.

III. Caveats on the Data on QHTB Operations

The data from Form N-317 tend to understate the activities of the QHTB's. First, the data are available only for QHTB operations in calendar year 2002 and later, whereas the tax credit has been available for investments made since July 1, 1999. Secondly, the data tend to understate the number of QHTB's and the amount of their activities after 2002. There was a steep drop in the number of filings between 2002 and 2003, from 138 to 87. There also appears to be no uniformity or consistency in the filing of the Form

² The 2002, 2003, 2004, 2005 and 2006 versions of the Form N-317 are attached in the appendix.

N-317. For example, it appears that certain QHTBs did not file Form N-317 for a particular year unless they received new investments during the calendar year. Also, certain QHTBs did not appear to have filed the Form N-317, because it is an information return not directly related to calculating tax liabilities.

The category "the same as section 41(d) of the Internal revenue Code" is listed as an activity that the QHTB may select on Form N-317. However, the category is not a single activity; instead, it includes all activities that are eligible for the federal research credit. A QHTB that selected only this category might belong in one or more of the actual activities listed on the Form, or its activity might not have been listed.

The data for the jobs created since the inception of the QHTB, for the new jobs created in the calendar year, for the salaries paid, and for the number of employees paid, might include a portion of the operations of the QHTB outside of Hawaii. Respondents might have wondered why Hawaii would be interested in jobs created or salaries paid outside of the State, but Form N-317 did not ask them to exclude the out-of-State jobs or salaries, so it is possible that certain QHTBs might have included the out-of-state jobs in their responses. Indeed, in about 7 percent of the responses, the salaries paid exceeded the costs incurred in Hawaii, even though these costs include employee salaries. On the other hand, some respondents specifically stated that their figures for jobs and salaries were for Hawaii only.

When answering the questions on jobs created, respondents interpreted 'jobs' in different ways. Some of them measured jobs as full-time equivalent jobs, whereas others did not. Also, some respondents included jobs created outside of their own operations, such as jobs in companies that provided services to the QHTB. Finally, jobs that were

created in one year may be lost in another, so the figures for jobs created do not provide reliable information about the number of jobs now present in the QHTB's.

When answering the question on employees paid in the calendar year, most respondents counted each worker as a unit, whether full time, part time or temporary. However, some respondents converted to full-time equivalent workers when counting their employees.

When answering the question on the investors in the QHTB, some respondents listed all investors since the inception of the QHTB, whereas others listed only those who made investments during the calendar year. In some cases, it was not possible to determine which type of response was given.³ In any event, the number of investors reported on the Form is not very informative: In some cases, the investor is a partnership or other business organization that invests in the QHTB on behalf of many different individuals or entities.⁴

Form N-317 asks the respondent to list tax incentives, including the tax credit for research activities. However, the responses to this question were often so vague that it could not be determined whether the QHTB had claimed, or intended to claim the research credit.

Finally, it should be noted that the investments reported on Form N-317 tend to substantially overstate the high technology business investment tax credits that will be applied against Hawaii tax liabilities, for a variety of reasons. For example, the

³ Respondents may have answered the question differently, because the question on the investors in the QHTB does not say that respondents should only list investments provided in that particular calendar year (opposed to "since inceptions"), but it follows immediately after the question on the amount of investments received by the QHTB in the calendar year.

⁴ The QHTB's reported 483 investors on Form N-317 in 2002, 264 investors in 2003, 380 investors in 2004, 367 investors in 2005, and 444 investors in 2006. In tax year 2004, the high technology business investment tax credit was claimed on 1,040 tax returns.

investment amount on the Form includes non-cash investments of real and personal property, whereas the tax credit is available only for cash investments. Furthermore, even cash investments in QHTB's do not always result in tax credits being used because certain taxpayers failed to timely claim the credit, certain taxpayers lacked sufficient Hawaii tax liabilities to utilize the credit, or certain taxpayers will not utilize the full credit for other reasons. Therefore, the revenue cost of the tax credit should be gauged using the data from the forms used to claim the tax credit, rather than inferred from the data on the investment amounts reported on Form N-317.

IV. The Data on High Technology Business Investment Tax Credits Claimed

Form N-318 ("High Technology Business Investment Tax Credit") is filed by the investor in order to claim the high technology business investment tax credit. The tax credit is used (applied against Hawaii tax liability) on a variety of forms. Individuals and non-financial corporations apply the tax credit by filing Schedule CR ("Schedule of Tax Credits") with their net income tax return. Financial corporations, fiduciaries and tax-exempt organizations apply the tax credit using lines or schedules embedded in their net income tax returns, for example, tax-exempt organizations may claim the credit against Hawaii income taxes in certain circumstances.⁵

Insurance companies apply the high technology business investment tax credit against the tax on insurance premiums using Form 314 (the "Annual Premium Tax Statement") or Form 323 (the "Quarterly Premium Tax Statements"). The insurance

⁵ Financial corporations apply the tax credit on Schedule H of Form F-1 ("Franchise Tax Return"), fiduciaries use Schedule E of Form N-40 ("Fiduciary Income Tax Return"), and exempt organizations use the appropriate line on Form N-70NP ("Exempt Organization Business Income Tax Return i.e., unrelated business income tax (UBIT) return").

companies use calendar year accounting periods. The tax on insurance premiums is administered by the Insurance Division in the Department of Commerce and Consumer Affairs. The Insurance Division calculates the amounts of the tax credit that were applied against the tax on insurance premiums and provides the results to DOTax.

The net income tax returns are filed for the taxpayer's fiscal year and DOTax tabulates the data by tax year. The tax year includes returns filed for taxpayer fiscal years ending in the calendar year. For example, for a taxpayer with a fiscal year ending June 30, the return for tax year 2006 would include data for the period from July 1, 2005 through June 30, 2006. Taxpayers may extend the filing deadline for their net income tax return by as much as six months and there are additional processing lags before data from the returns are available for tabulation. Consequently, at time of writing, 2005 was the latest tax year that could be closed.⁶

Table 8 summarizes the data on the high technology business investment tax credits claimed for tax years 1999 through 2005. Act 178, SLH 1999, established the tax credit and set it at 10 percent of the investment amount for investments made on or after July 1, 1999. Act 221, SLH 2001, increased the tax credit to 100 percent of the investment amount (to be claimed over five years) for investments made on or after July 1, 2001.⁷ Thus, the data reported for tax years 1999 and 2000 reflect tax credits taken under the original modest program, the data for tax years 2001 and 2002 reflect tax credits taken under either the original program or the expanded program, and the data for tax years 2003 through 2005 reflect tax credits taken under the expanded program.

⁶ The investment credit claims for the 2006 tax year will have to be filed by December 31, 2007.

⁷ Act 221 was amended by Act 215, SLH 2004, which took effect July 1, 2004. Among other things, Act 215 required DOTax to certify qualified investments and to maintain records of taxpayers claiming the tax credit. Appendix III provides more detail on the tax credit and its history.

V. Some Highlights of the Data on QHTB Operations and on High Technology Business Investment Tax Credits Claimed

A total of 287 separate QHTB's filed Form N-317 at one time or another over the period from 2002 through 2006⁸. A total of 157 QHTBs filed the Form for 2006. Despite the annual filing requirement, it is possible that many QHTBs did not file Form N-317 for 2006 because they did not receive new investments for that year.⁹

As shown in Table 6, Computer Software is the most frequently listed activity, but in general little can be said with accuracy about the operations in specific activities. This is true because many QHTB's listed multiple activities and in such cases it is not possible to obtain data on operations in the individual activities. For example, 28 of the total 157 QHTB's that filed for 2006 reported having multiple activities: 11 listed Biotechnology as an activity, 8 listed Performing Arts, 5 listed Ocean Sciences, 4 listed Nonfossil Fuels, 17 listed Computer Software, 13 listed Sensors & Optics, and 3 listed Astronomy. Also, some QHTB's that listed only section 41(d) of the IRC as their activity might properly have been classified in one of the other activities listed on the Form.

As shown in Table 5, the QHTB's that filed for 2006 reported creating 5,383 jobs since their inception. They reported paying 2,322 employees during the calendar year. The bulk of the difference lies in the Performing Arts category, where for 2006 the QHTBs reported creating 2,856 jobs since their inception. They paid only 307 employees during the year. The jobs created may include workers that were not

⁸ This tabulation is not shown in the tables.

⁹ See the discussion in section III above. Also, some QHTB's might have changed their Federal Employer Identification Number, because they changed their business activities, and some might have merged with another QHTB.

considered employees, such as workers hired under contract or principals of the QHTB.¹⁰ Some of the jobs created also may have been temporary or subsequently lost. On the other hand, some QHTB's reported paying more employees during the calendar year than the number of jobs they claimed to have created since their inception. This might have occurred because the respondents measured jobs created in terms of full-time equivalents or permanent positions, whereas they counted each employee paid, including part time and temporary workers. Also, some QHTB's might have taken employees from existing operations elsewhere in the parent company.

As shown in Table 6, total expenses incurred in Hawaii by the QHTB's ranged from \$118.8 million in 2002 to \$290.6 million in 2006: over all the years, the total expenditures incurred in Hawaii amounted to \$1.043 billion. Investments received by the QHTBs ranged from a low of \$74.1 million in 2003 to a high of \$222.4 million in 2004 and totaled \$821.6 million for this four year period. The ratio of expenses incurred in Hawaii to investments received averaged 127 percent. Total salaries paid by the QHTB's ranged from \$47.0 million in 2003 to \$155.6 million in 2006. For this four year period the total salaries paid by the QHTB's was \$505.8 million. The ratio of salaries paid to investments received averaged 62 percent and the ratio of salaries paid to expenses incurred in Hawaii averaged 48 percent. The latter figure may overstate or understate labor's share of the total expenses incurred in Hawaii, however. The understatement can occur, because some QHTB's hired workers on contract rather than as employees; the overstatement can occur, because some of the salaries were paid to employees outside of

¹⁰ This could also explain why some QHTBs claimed to have created more jobs in the calendar year than the number of employees they paid during the year.

Hawaii. The Performing Arts had the lowest and the highest average salary per employee (2003 through 2006). The low was \$19,520 in 2003 and the high was \$173,386 in 2006.

The median of the average salaries paid by the QHTB's (that is, the average salary of the median QHTB when the QHTB's are ranked according to their average salary) climbed steadily from \$34,786 in 2003 to \$46,105 in 2006. The number of employees paid during the year includes some part time and temporary workers, so the average salaries, and the medians of these averages, tend to understate the corresponding measures for full time employees in the QHTB's.

More than half of the QHTB's stated clearly that they had taken, or planned to take the tax credit for research activities provided by Section 235-110.91, HRS. The percentage cannot be determined accurately, because (as already noted) in many cases the respondent was vague when describing the tax credits to be claimed by the QHTB. Twelve percent of the QHTB's indicated that salary amounts involved property, such as stock options. However, a number of respondents failed to answer the question on whether the salary amounts involved property.

As shown in Table 8, high technology business investment tax credits applied against Hawaii tax liabilities grew from \$0.6 million for tax years 1999 and 2000 combined to \$69.8 million for tax year 2005. As of the end of tax year 2005, the cumulative tax credits used totaled \$195.6 million. The number of claims for the tax credit also increased; from 23 claims in tax year 1999 to 1,216 claims in tax year 2005.

APPENDIX I
TABLES

Table 1-- Summary of Statistics from Forms N-317 Filed for 2002
(Includes Operations of the QHTBs in Calendar Year 2002 Only)

<i>Activity</i>	<i>Number of Forms</i>	<i>Jobs Created Since the QHTB's Inception 1/</i>	<i>New Jobs Created by the QHTB in the Calendar Year 2/</i>	<i>Salaries Paid by the QHTB in the Calendar Year (\$) 3/</i>	<i>Expenses Incurred by the QHTB in Hawaii in the Calendar Year (\$)</i>	<i>Investments Received by the QHTB in the Calendar Year (\$)</i>
IRC Section 41(d) 4/	7	57	8	1,588,748	1,923,521	508,351
Biotechnology	14	120	53	11,137,025	7,692,126	11,211,303
Performing Arts	20	723	723	4,008,435	8,230,697	23,126,499
Computer Software	64	520	193	19,684,685	36,387,016	37,982,782
Multiple Activities and Others 5/	33	429	128	24,116,164	64,526,187	44,865,767
Totals	138	1,849	1,105	60,535,057	118,759,547	117,694,702

Source: Hawaii State Department of Taxation, Tax Research and Planning Office

Notes:

1/ Includes jobs created outside the State of Hawaii and some jobs that subsequently ended.

2/ Includes jobs created outside the State of Hawaii.

3/ Includes salaries paid to employees outside of the State of Hawaii.

4/ Section 41(d) of the Internal Revenue Code defines activities that are eligible for the federal qualified research credit, which may be applied against the taxpayer's federal income tax liability. Companies are classified under this heading only if they did not specify another activity on Form N-317.

5/ Includes Sensors and Optics, Nonfossil Fuels, and Ocean Sciences. There were no QHTBs solely in Astronomy.

Table 2-- Summary of Statistics from Forms N-317 Filed for 2003

<i>Activity</i>	<i>Number of Forms</i>	<i>Jobs Created Since the QHTB's Inception 1/</i>	<i>New Jobs Created by the QHTB in the Calendar Year 2/</i>	<i>Salaries Paid by the QHTB in the Calendar Year (\$) 3/</i>	<i>Number of Employees Paid by the QHTB in the Calendar Year 4/</i>	<i>Expenses Incurred by the QHTB in Hawaii in the Calendar Year (\$) 5/</i>	<i>Investments Received by the QHTB in the Calendar Year (\$) 6/</i>	<i>Average of Salaries Paid by the QHTBs 5/</i>	<i>Median of Salaries Paid by the QHTBs 6/</i>
Biotechnology	10	190	18	6,464,184	170	10,287,195	9,005,457	38,025	37,250
Performing Arts	13	783	73	1,854,404	95	7,474,340	5,534,286	19,520	21,676
Computer Software	42	390	93	13,248,849	362	33,410,717	20,345,132	36,599	29,972
Multiple Activities and Others 7/	22	686	143	25,419,491	492	67,928,427	39,255,487	51,666	51,436
Totals	87	2,052	327	46,986,928	1,119	119,100,679	74,140,362	41,990	34,786

Source: Hawaii State Department of Taxation, Tax Research and Planning Office

Notes:

1/ Includes jobs created outside the State of Hawaii and some jobs that subsequently ended.

2/ Includes jobs created outside the State of Hawaii.

3/ Includes salaries paid to employees outside of the State of Hawaii.

4/ Includes people employed outside of the State of Hawaii.

5/ Equal to salaries paid divided by the number of employees paid.

6/ Equal to the median of the QHTB salary averages.

7/ Includes IRC Section 41(d), Sensors and Optics, Ocean Sciences, and Nonfossil Fuels. There were no QHTBs solely in Astronomy.

Table 3-- Summary of Statistics from Forms N-317 Filed for 2004

Activity	Number of Forms	Jobs Created Since the QHTB's Inception 1/	New Jobs Created by the QHTB in the Calendar Year 2/	Salaries Paid by the QHTB in the Calendar Year (\$) 3/	Number of Employees Paid by the QHTB in the Calendar Year 4/	Expenses Incurred by the QHTB in Hawaii in the Calendar Year (\$)	Investments Received by the QHTB in the Calendar Year (\$)	Average of Salaries Paid by the QHTBs 5/	Median of Salaries Paid by the QHTBs 6/
IRC Section 41(d) 7/	8	122	27	5,757,277	112	16,534,807	12,625,000	51,404	51,688
Biotechnology	10	198	31	7,739,206	196	13,636,101	13,742,711	39,486	28,253
Performing Arts	21	2,193	771	53,629,390	708	109,401,021	108,718,392	75,748	18,911
Computer Software	41	728	241	20,291,994	560	39,126,298	18,091,620	36,236	35,668
Multiple Activities and Others 8/	32	996	273	31,679,677	710	79,890,143	69,238,362	44,619	41,158
Totals	112	4,237	1,343	119,097,544	2,286	258,588,370	222,416,085	52,099	35,745

Source: Hawaii State Department of Taxation, Tax Research and Planning Office

Notes:

1/ Includes jobs created outside the State of Hawaii and some jobs that subsequently ended.

2/ Includes jobs created outside the State of Hawaii.

3/ Includes salaries paid to employees outside of the State of Hawaii.

4/ Includes people employed outside of the State of Hawaii.

5/ Equal to salaries paid divided by the number of employees paid.

6/ Equal to the median of the QHTB salary averages.

7/ Section 41(d) of the Internal Revenue Code defines activities that are eligible for the federal qualified research credit, which may be applied against the taxpayer's federal income tax liability. Companies are classified under this heading only if they did not specify another activity on Form N-317.

8/ Includes Ocean Sciences, Nonfossil Fuels, and Sensors and Optics. There were no QHTBs solely in Astronomy.

Table 4-- Summary of Statistics from Forms N-317 Filed for 2005

<i>Activity</i>	<i>Number of Forms</i>	<i>Jobs Created Since the QHTB's Inception 1/</i>	<i>New Jobs Created by the QHTB in the Calendar Year 2/</i>	<i>Salaries Paid by the QHTB in the Calendar Year (\$) 3/</i>	<i>Number of Employees Paid by the QHTB in the Calendar Year 4/</i>	<i>Expenses Incurred by the QHTB in Hawaii in the Calendar Year (\$) 5/</i>	<i>Investments Received by the QHTB in the Calendar Year (\$) 6/</i>	<i>Average of Salaries Paid by the QHTBs 7/</i>	<i>Median of Salaries Paid by the QHTBs 8/</i>
IRC Section 41D 7/	7	170	19	9,479,850	147	22,060,996	2,989,350	64,489	66,572
Biotechnology	13	157	26	10,643,939	206	18,704,207	13,013,401	51,670	24,153
Performing Arts	26	2,626	521	42,540,051	916	78,125,197	86,286,149	46,441	14,544
Computer Software	46	862	102	26,653,297	581	54,723,770	24,297,508	45,875	40,784
Multiple Activities and Others 8/	34	1,391	157	34,276,822	715	82,598,487	62,093,432	47,940	46,633
Totals	126	5,206	825	123,593,959	2,565	256,212,657	188,679,840	48,185	39,595

Source: Hawaii State Department of Taxation, Tax Research and Planning Office

Notes:

1/ Includes jobs created outside the State of Hawaii and some jobs that subsequently ended.

2/ Includes jobs created outside the State of Hawaii.

3/ Includes salaries paid to employees outside of the State of Hawaii.

4/ Includes people employed outside of the State of Hawaii.

5/ Equal to salaries paid divided by the number of employees paid.

6/ Equal to the median of the QHTB salary averages.

7/ Section 41(d) of the Internal Revenue Code defines activities that are eligible for the federal qualified research credit, which may be applied against the taxpayer's federal income tax liability. Companies are classified under this heading only if they did not specify another activity on Form N-317.

8/ Includes QHTBs with unknown activities, Ocean Sciences, Sensors and Optics, and Nonfossil Fuels. There were no QHTBs solely in Astronomy.

Table 5-- Summary of Statistics from Forms N-317 Filed for 2006

<i>Activity</i>	<i>Number of Forms</i>	<i>Jobs Created Since the QHTB's Inception 1/</i>	<i>New Jobs Created by the QHTB in the Calendar Year 2/</i>	<i>Salaries Paid by the QHTB in the Calendar Year (\$) 3/</i>	<i>Number of Employees Paid by the QHTB in the Calendar Year 4/</i>	<i>Expenses Incurred by the QHTB in Hawaii in the Calendar Year</i>	<i>Investments Received by the QHTB in the Calendar Year (\$)</i>	<i>Average of Salaries Paid by the QHTBs 5/</i>	<i>Median of Salaries Paid by the QHTBs 6/</i>
IRC Section 41D 7/	9	107	20	5,694,318	105	8,985,413	2,780,160	54,232	61,967
Biotechnology	19	217	68	13,451,074	254	30,452,054	27,500,488	52,957	39,107
Performing Arts	29	2,856	314	53,229,462	307	80,083,484	61,029,392	173,386	14,518
Nonfossil Fuels	13	37	8	1,756,091	50	7,924,927	7,213,697	35,122	26,138
Computer Software	50	921	174	37,493,304	824	68,478,671	46,638,812	45,502	48,315
Multiple Activities and Others 8/	37	1,245	167	43,997,243	782	94,712,773	73,491,373	56,262	51,915
Totals 9/	157	5,383	751	155,621,492	2,322	290,637,322	218,653,922	67,020	46,105

Source: Hawaii State Department of Taxation, Tax Research and Planning Office

Notes:

1/ Includes jobs created outside the State of Hawaii and some jobs that subsequently ended.

2/ Includes jobs created outside the State of Hawaii.

3/ Includes salaries paid to employees outside of the State of Hawaii.

4/ Includes people employed outside of the State of Hawaii.

5/ Equal to salaries paid divided by the number of employees paid.

6/ Equal to the median of the QHTB salary averages.

7/ Section 41(d) of the Internal Revenue Code defines activities that are eligible for the federal qualified research credit, which may be applied against the taxpayer's federal income tax liability. Companies are classified under this heading only if they did not specify another activity on Form N-317.

8/ Includes QHTBs with unknown activities, Sensors and Optics, and Ocean Sciences. There were no QHTBs solely in Astronomy.

9/ Totals for 2006 may increase, because they do not include some QHTBs that are expected to file late.

**Table 6-- Summary of Statistics from Forms N-317 Filed for 2002 through 2006:
Totals by Activity and by Calendar Year**

Year	Activity	Number of Forms	Jobs Created Since the QHTBs' Inceptions 2/	New Jobs Created by the QHTBs in the Calendar Year 3/	Salaries Paid by the QHTBs in the Calendar Year (\$) 4/	Number of Employees Paid by the QHTBs in the Calendar Year 5/	Expenses Incurred by the QHTBs in Hawaii in the Calendar Year (\$)	Investments Received by the QHTBs in the Calendar Year (\$)	Average of Salaries Paid by the QHTBs 6/	Median of Salaries Paid by the QHTBs 7/
2002	Biotechnology	14	120	53	11,137,025	NA	7,692,126	11,211,303	NA	NA
2003		10	190	18	6,464,184	170	10,287,195	9,005,457	38,025	37,250
2004		10	198	31	7,739,206	196	13,636,101	13,742,711	39,486	28,253
2005		13	157	26	10,643,939	206	18,704,207	13,013,401	51,670	24,153
2006		19	217	68	13,451,074	254	30,452,054	27,500,488	52,957	39,107
2002	Performing Arts	20	723	723	4,008,435	NA	8,230,697	23,126,499	NA	NA
2003		13	783	73	1,854,404	95	7,474,340	5,534,286	19,520	21,676
2004		21	2,193	771	53,629,390	708	109,401,021	108,718,392	75,748	18,911
2005		26	2,626	521	42,540,051	916	78,125,197	86,286,149	46,441	14,544
2006		29	2,856	314	53,229,462	307	80,083,484	61,029,392	173,386	14,518
2002	Computer Software	64	520	193	19,684,685	NA	36,387,016	37,982,782	NA	NA
2003		42	390	93	13,248,849	362	33,410,717	20,345,132	36,599	29,972
2004		41	728	241	20,291,994	560	39,126,298	18,091,620	36,236	35,668
2005		46	862	102	26,653,297	581	54,723,770	24,297,508	45,875	40,784
2006		50	921	174	37,493,304	824	68,478,671	46,638,812	45,502	48,315
2002	Multiple Activities and Others 1/	40	486	136	25,704,912	NA	66,449,708	45,374,118	NA	NA
2003		22	689	143	25,419,491	492	67,928,427	39,255,487	51,666	51,436
2004		40	1,118	300	37,436,954	822	96,424,950	81,863,362	45,544	41,904
2005		41	1,561	176	43,756,672	862	104,659,483	65,082,782	50,762	54,046
2006		59	1,389	195	51,447,652	937	111,623,113	83,485,230	54,907	51,915
2002	All Activities Combined	138	1,849	1,105	60,535,057	NA	118,759,547	117,694,702	NA	NA
2003		87	2,052	327	46,986,928	1,119	119,100,679	74,140,362	41,990	34,786
2004		112	4,237	1,343	119,097,544	2,286	258,588,370	222,416,085	52,099	35,745
2005		126	5,206	825	123,593,959	2,565	256,212,657	188,679,840	48,185	39,595
2006		157	5,383	751	155,621,492	2,322	290,637,322	218,653,922	67,020	46,105
Total, All Years	All Activities Combined	NA	NA	NA	505,834,980	NA	1,043,298,575	821,584,911	NA	NA

Source: Hawaii State Department of Taxation, Tax Research and Planning Office

Notes: NA denotes that the figure is either not available or not applicable.

1/ Includes QHTBs with unknown activities, IRC Section 41(d), Sensors and Optics, Ocean Sciences, and Nonfossil Fuels. There were no QHTBs solely in Astronomy.

2/ Includes jobs created outside the State of Hawaii and some jobs that subsequently ended.

3/ Includes jobs created outside the State of Hawaii.

4/ Includes salaries paid to employees outside of the State of Hawaii.

5/ Includes people employed outside of the State of Hawaii.

6/ Equal to salaries paid divided by number of employees paid.

7/ Equal to the median of the QHTB salary averages.

**Table 7-- Summary of Statistics from Forms N-317 Filed for 2002 through 2006:
Totals by Activity**

<i>Activity</i>	<i>Sum of Salaries Paid by the QHTBs in Calendar Years 2002 Through 2006 (\$) 2/</i>	<i>Sum of Expenses Incurred by the QHTBs in Hawaii in Calendar Years 2002 Through 2006 (\$)</i>	<i>Sum of Investments Received by the QHTBs in Calendar Years 2002 Through 2006 (\$)</i>
Biotechnology	49,435,428	80,771,683	74,473,360
Performing Arts	155,261,742	283,314,739	284,694,718
Computer Software	117,372,129	232,126,472	147,315,854
Multiple Activities and Others 1/	183,765,681	447,085,681	315,100,979
All Activities Combined	505,834,980	1,043,298,575	821,584,911

Source: Hawaii State Department of Taxation, Tax Research and Planning Office

Notes:

1/ Includes QHTBs with unknown activities, IRC Section 41(d), Sensors and Optics, Ocean Sciences, and Nonfossil Fuels. There were no QHTBs solely in Astronomy.

2/ Includes salaries paid to employees outside of the State of Hawaii.

**Table 8-- High Technology Business Investment Tax Credits for 1999 through 2005
Claims by Type of Taxpayer**

Year	Total Number of Claims	Total (\$)	Individuals (\$) 1/	Corporations (\$) 1/	Financial Corporations (\$) 2/	Insurance Underwriters (\$) 3/	Fiduciaries (\$) 4/	Exempt Organizations (\$) 1/
1999	23	162,208	NA	NA	NA	NA	NA	NA
2000	103	393,633	NA	NA	NA	NA	NA	NA
2001	268	9,579,923	3,334,260	225,205	4,209	6,013,757	2,492	NA
2002	493	26,185,181	11,191,036	1,710,041	0	13,057,896	226,208	NA
2003	652	38,870,301	13,360,232	3,855,197	2,100,658	19,391,764	162,450	NA
2004	1,040	50,543,285	26,858,573	994,571	1,599,658	20,714,206	376,277	NA
2005	1,216	69,827,709	38,111,997	3,428,405	2,286,892	25,293,046	700,845	6,524
Totals	3,795	195,562,240	92,856,098	10,213,419	5,991,417	84,470,669	1,468,272	6,524

Source: Hawaii State Department of Taxation, Tax Research and Planning Office

Notes:

1/ Data compiled from Schedule of Tax Credits (Sch. CR).

2/ Data compiled from Schedule H of Form F-1.

3/ Data provided by Hawaii State Department of Commerce and Consumer Affairs (DCCA).

4/ Data compiled from Schedule E of Form N-40.

APPENDIX II
FIGURES

Figure 1-- Number of Forms N-317 Filed by QHTBs

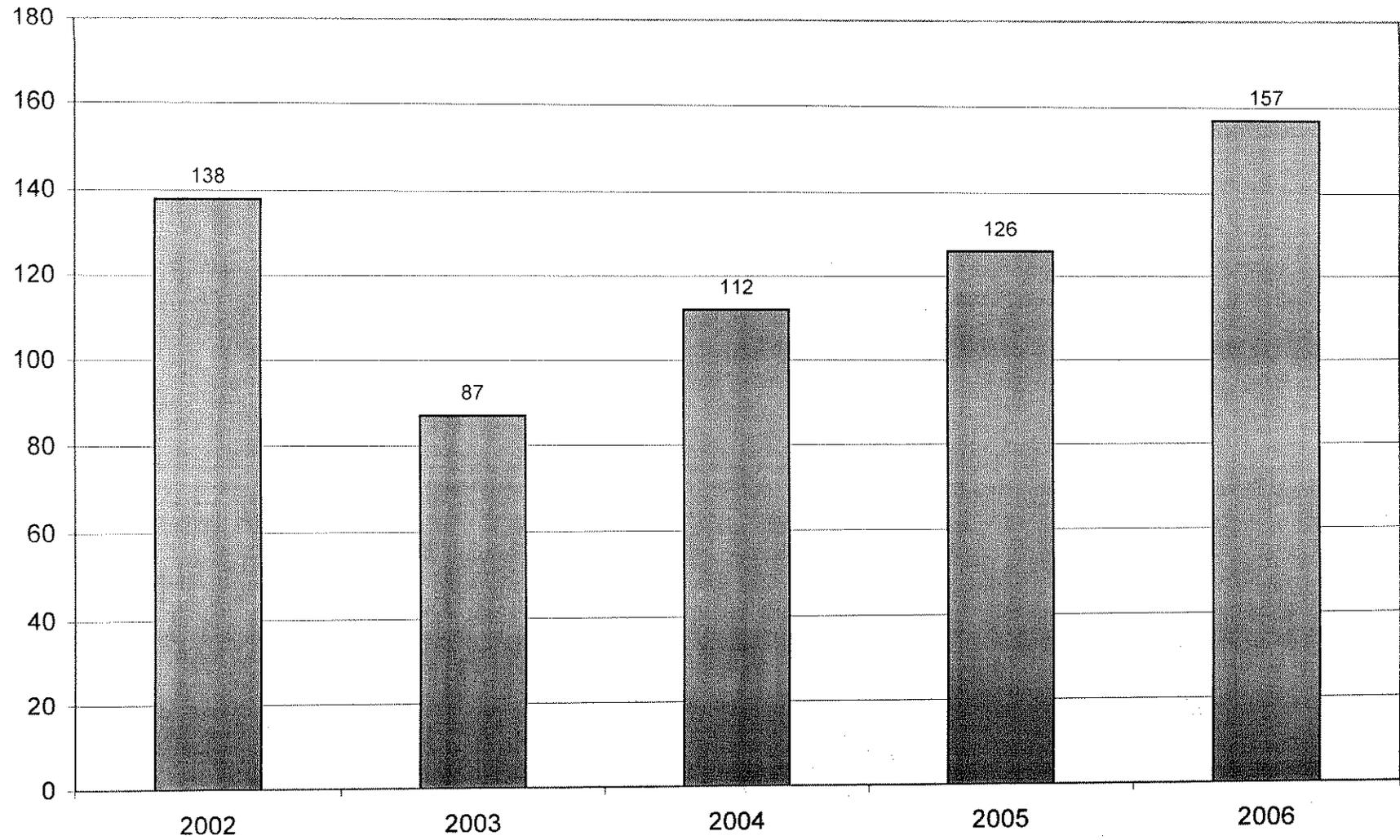


Figure 2-- Annual Investments Received by QHTBs

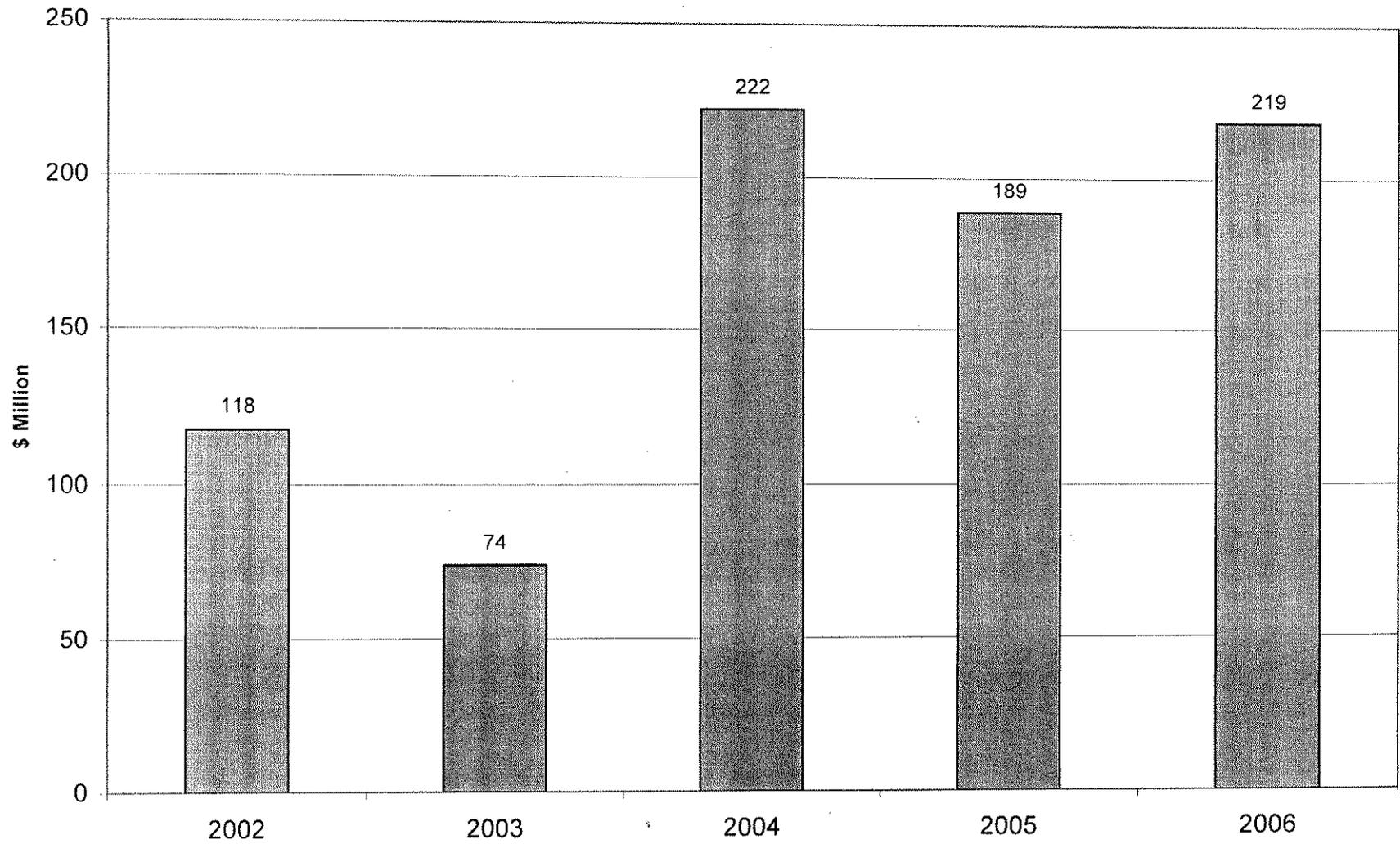


Figure 3-- Cumulative Investments Received by QHTBs

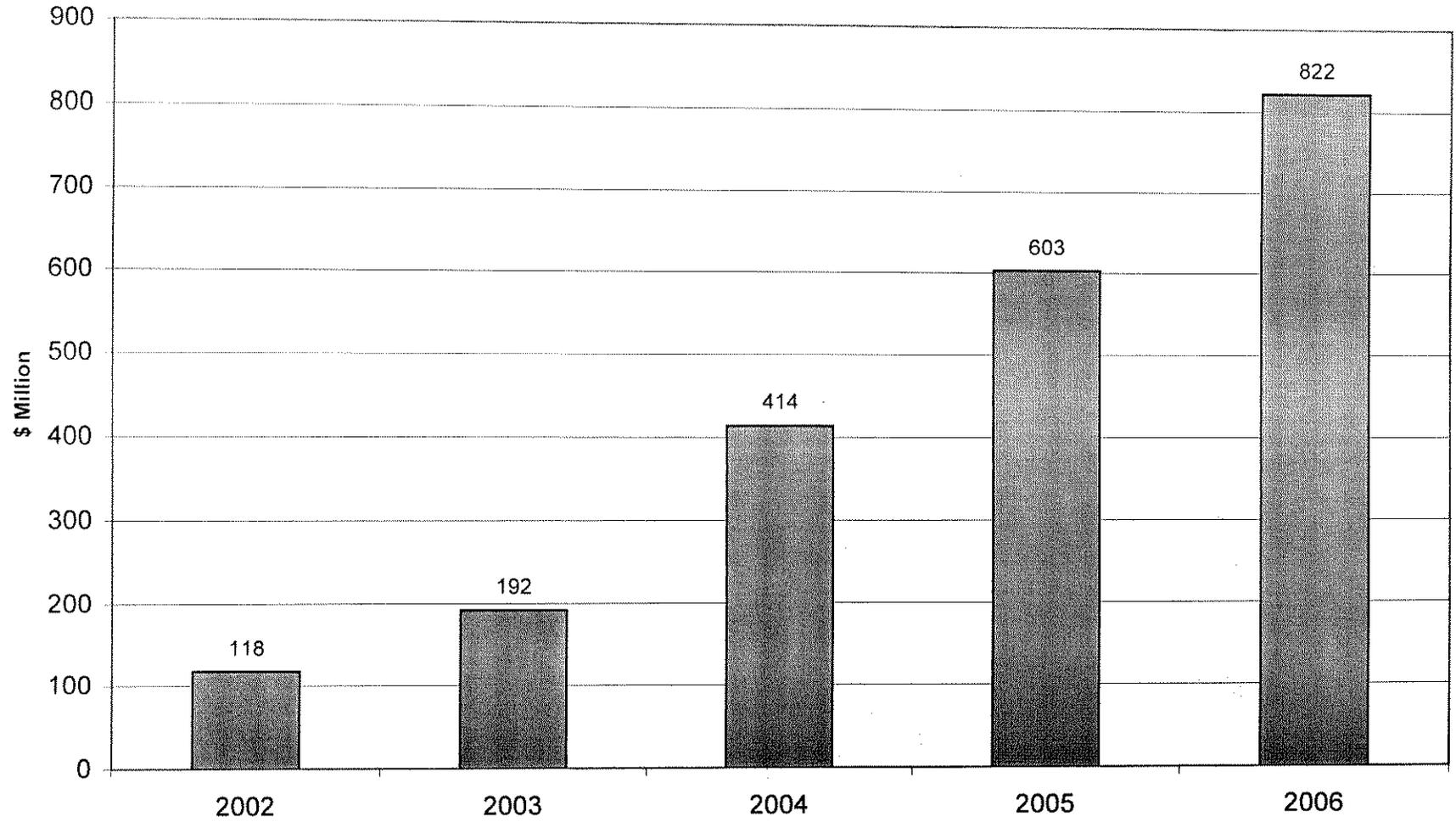
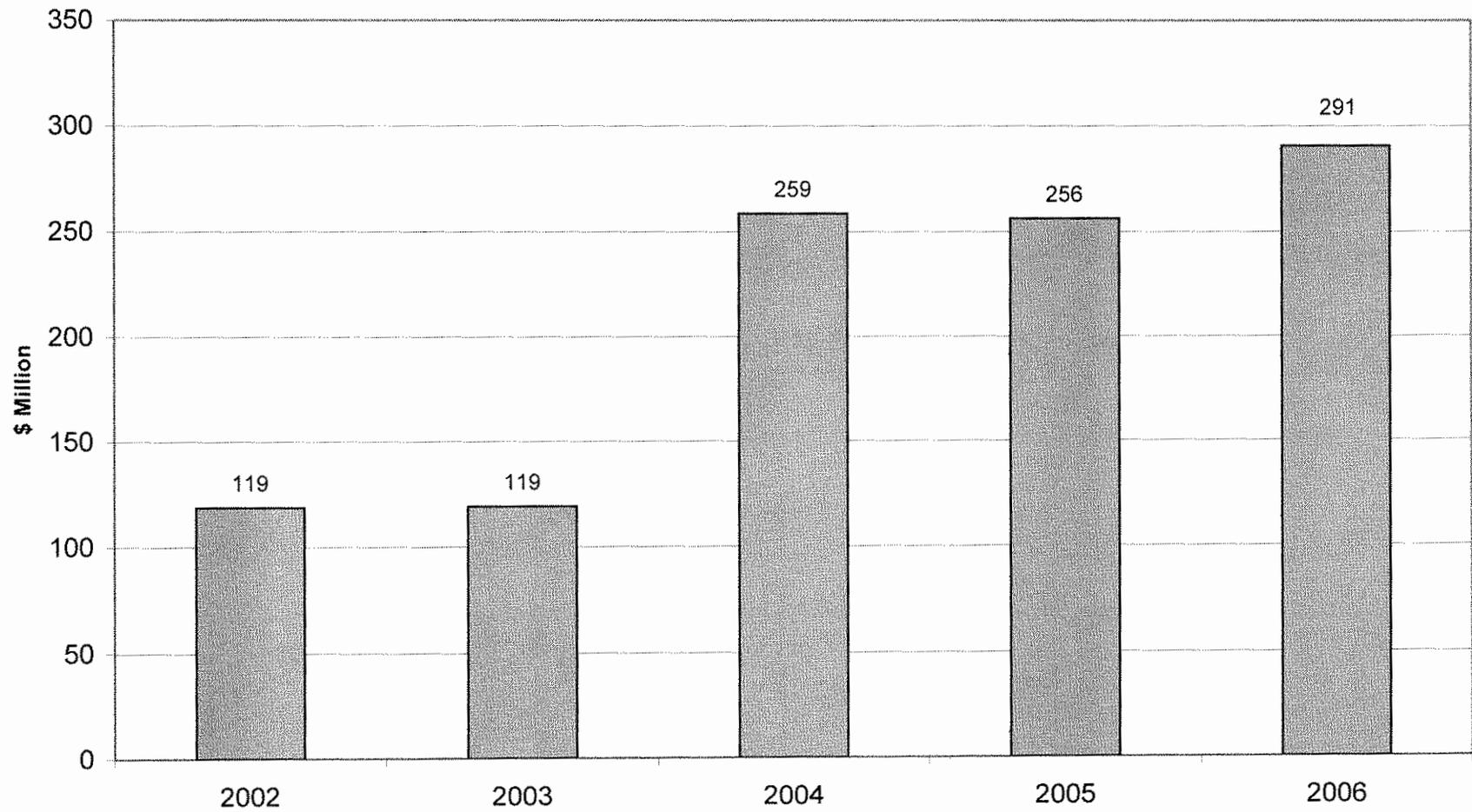


Figure 4-- Annual Expenditures Incurred in Hawaii by QHTBs
(i.e., Annual Expenditures by Hawaii QHTB)



**Figure 5-- Cumulative Expenditures Incurred In Hawaii
by QHTBs**
(i.e., Cumulative Expenditures by Hawaii QHTB)

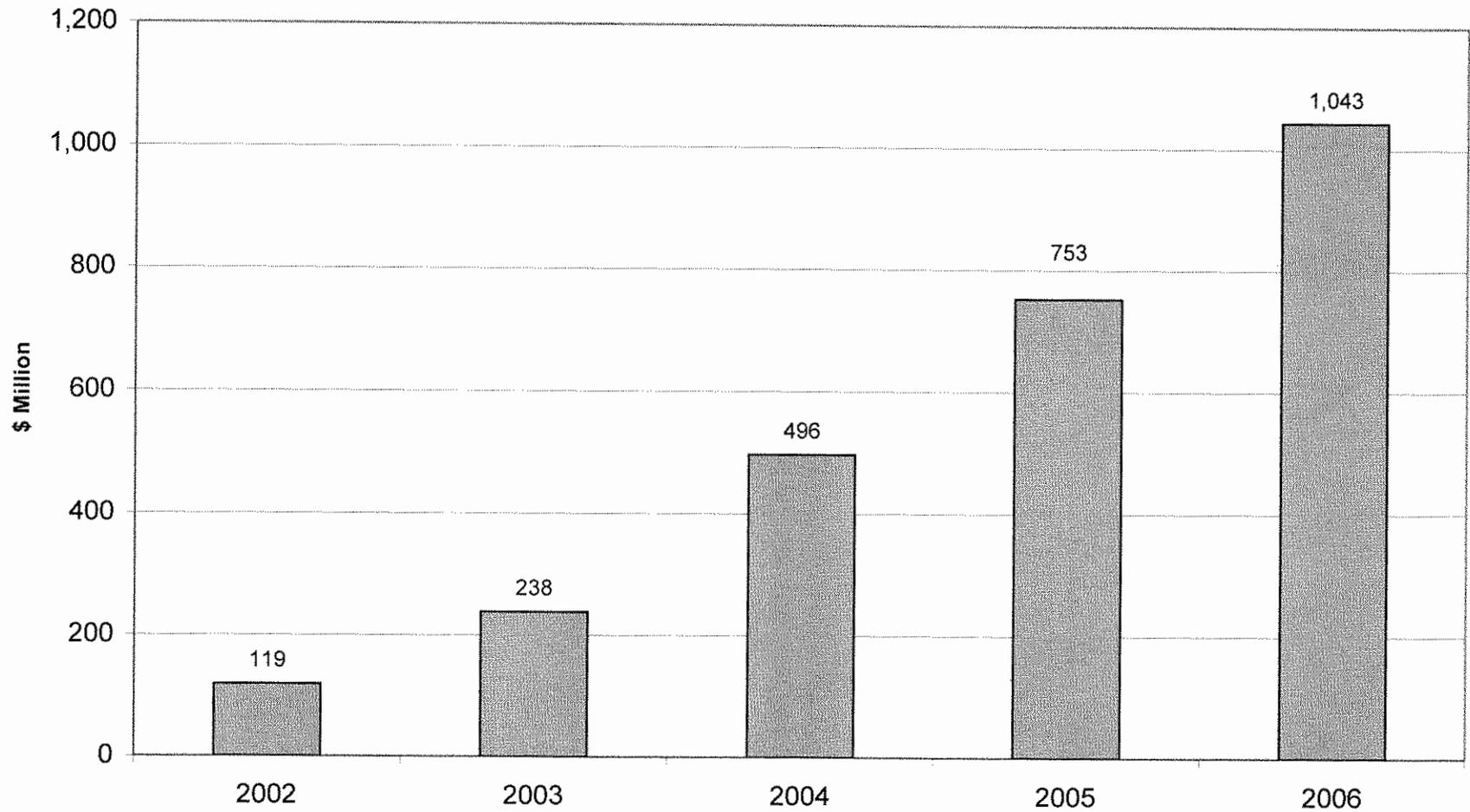
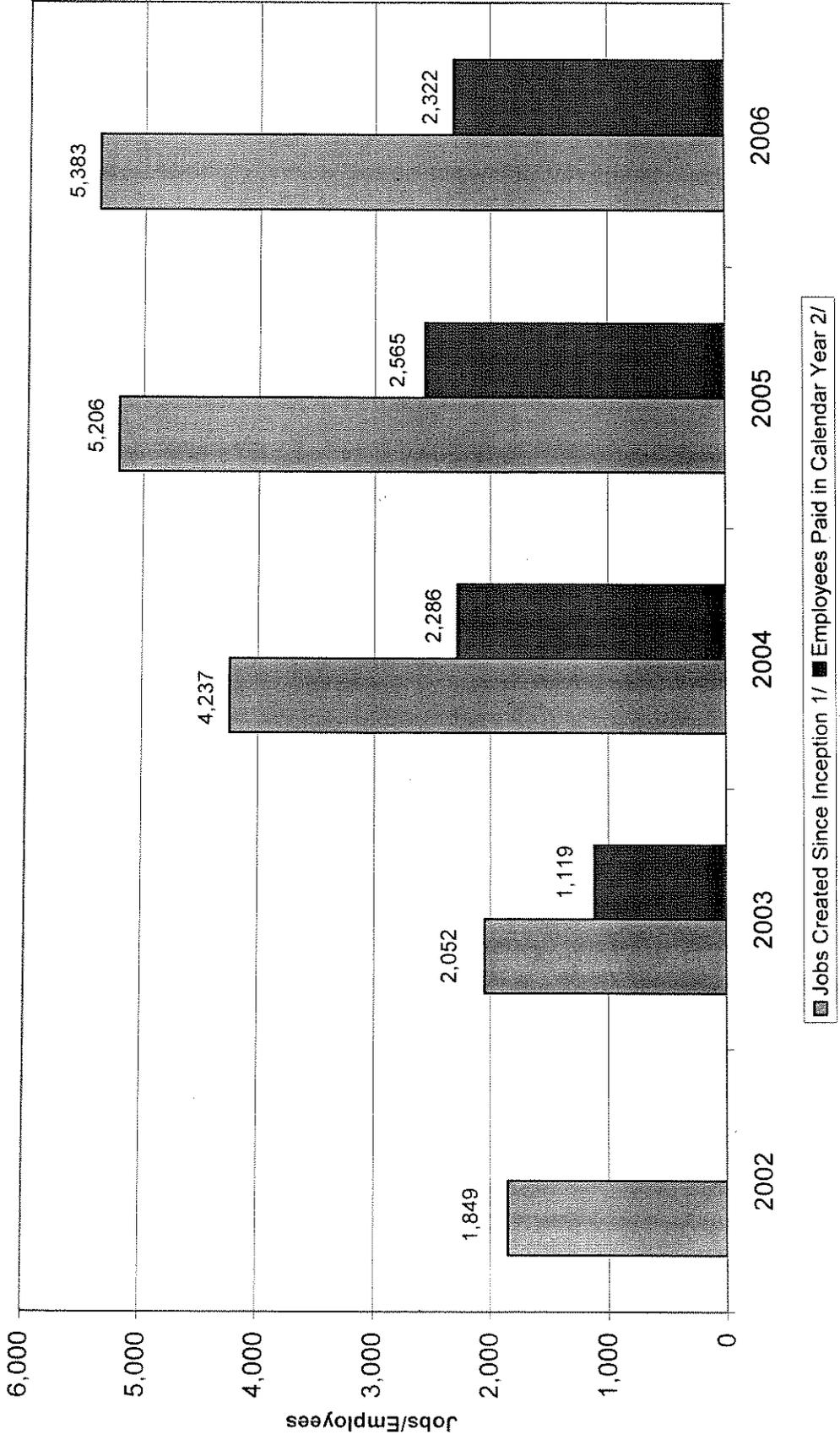


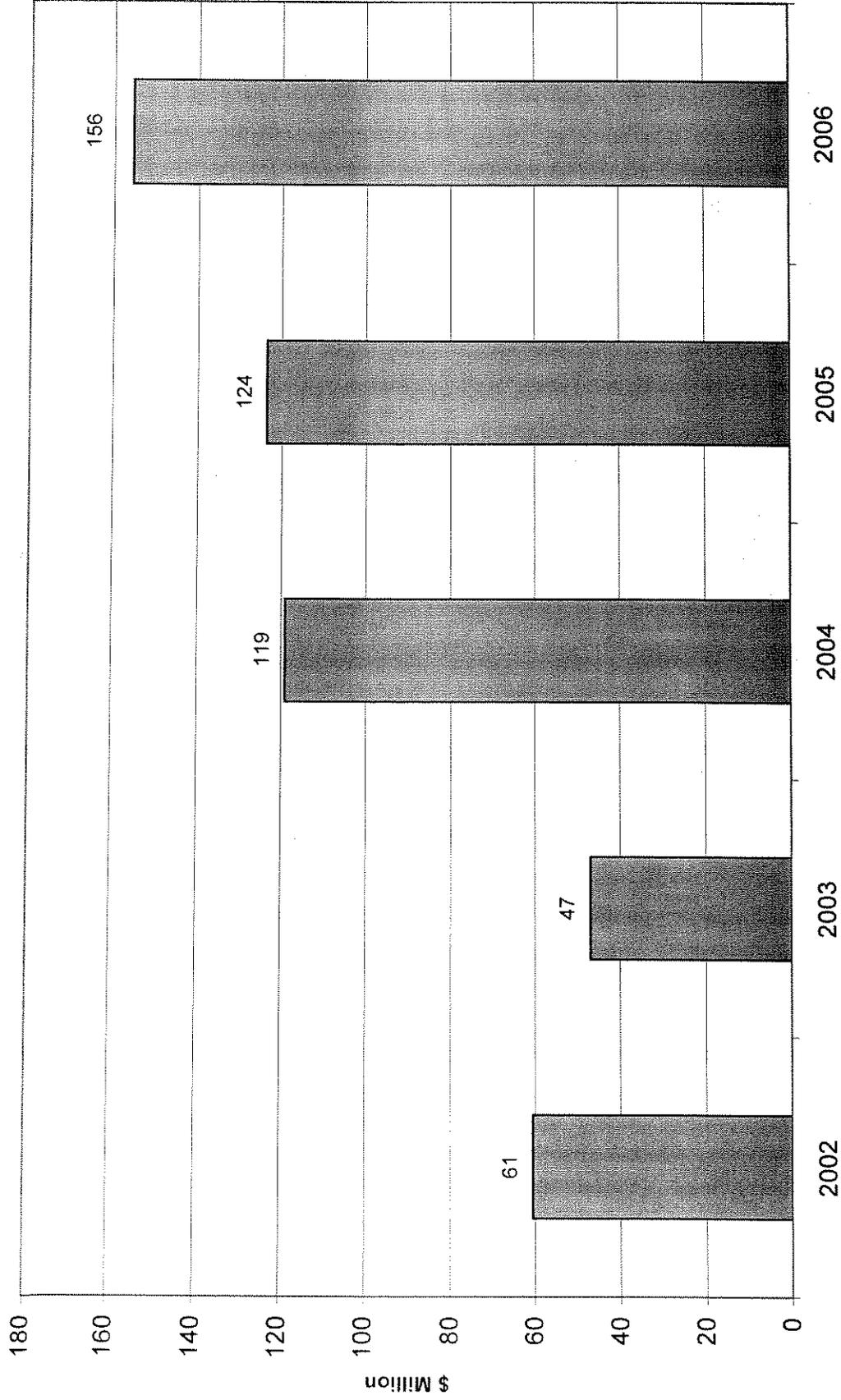
Figure 6-- Jobs Created Since Inception and Employees Paid by QHTBs



1/ Includes jobs created outside the State of Hawaii and some jobs that were subsequently lost.

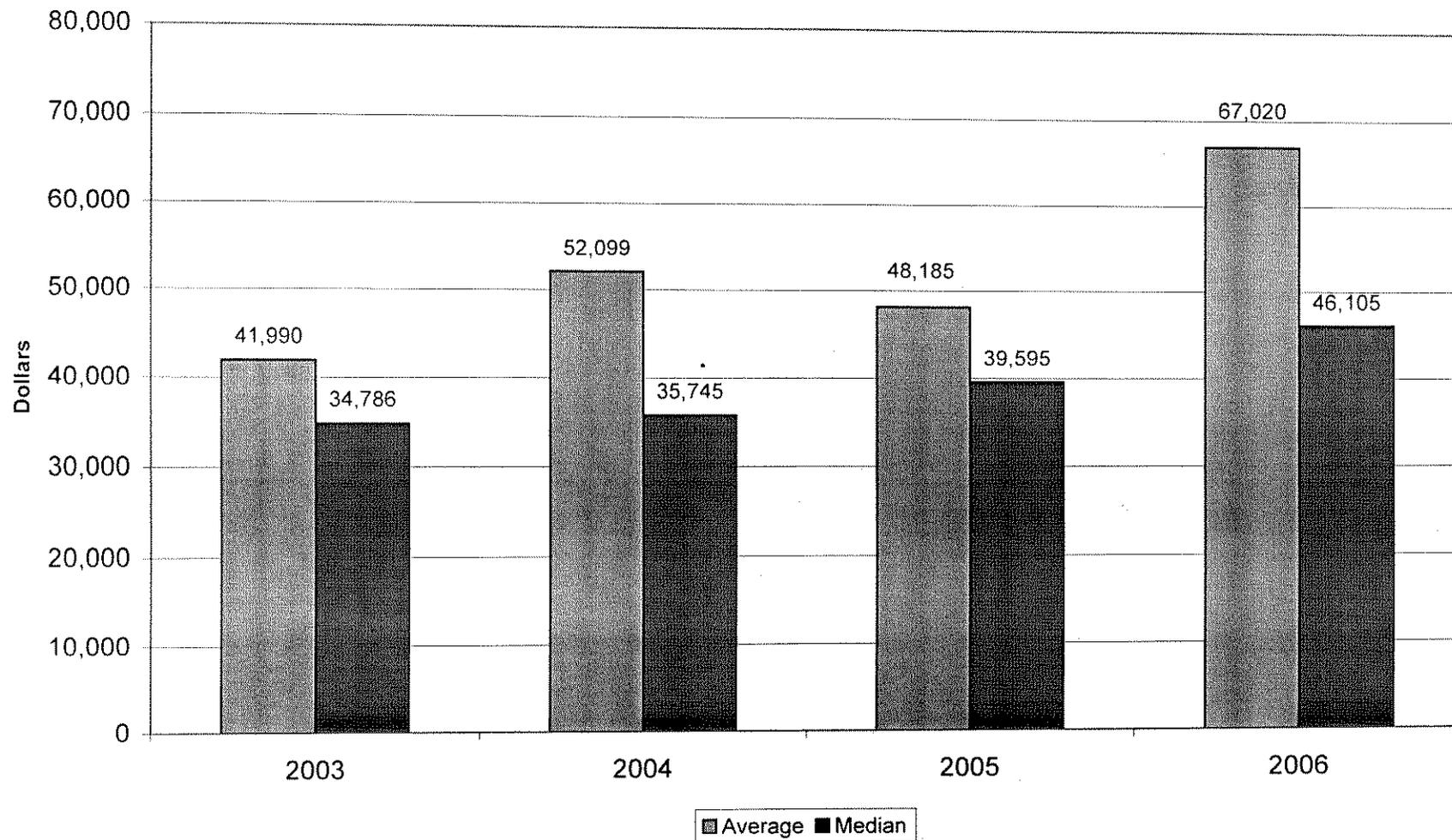
2/ Includes employees outside of the State of Hawaii.

Figure 7-- Total Salaries Paid ^{1/} by QHTBs



^{1/} Includes salaries paid outside of the State of Hawaii.

Figure 8-- Average and Median of the Salaries Paid ^{1/} by QHTBs



^{1/} Median salary is equal to the median of the QHTB salary averages.

APPENDIX III

**SUMMARY AND HISTORY OF THE
HIGH TECHNOLOGY BUSINESS
INVESTMENT TAX CREDIT AND
TAX CREDIT FOR RESEARCH
ACTIVITIES**

**SUMMARY AND HISTORY OF THE HIGH TECHNOLOGY BUSINESS
INVESTMENT TAX CREDIT AND TAX CREDIT FOR RESEARCH
ACTIVITIES**

CURRENT LAW

The following is a summary of the high technology business investment tax credit and the tax credit for research. This summary is not intended to be authoritative or comprehensive.

High technology business investment tax credit (the "Investment Credit")

In general, Hawaii's income tax law currently includes a non-refundable credit against income taxes for cash investments in a qualified high technology business ("QHTB") made by a taxpayer before December 31, 2010. The amount of the Investment Credit is 100% of the cash invested in a QHTB up to \$2,000,000 per QHTB per taxable year. The entire credit amount is not available to the taxpayer in the year of investment; instead the tax credit claim is staggered over a five-year period. The taxpayer is allowed to claim only 35% of the tax credit in the year of investment; 25% of the tax credit in the year following the investment; 20% in the third year; and 10% in the fourth and fifth years. A properly claimed credit that cannot be used in full against income taxes for a particular tax year may be carried forward to subsequent years until exhausted.

Any claim, original or amended, must be made by the end of the year which follows the year any portion of the Investment Credit may first be claimed. Failure to

make the claim by the end of the following year acts as a waiver of the claim, and any credit not claimed by the deadline is lost.

In order for the taxpayer to properly claim the credit in the year of investment and the following four years, the business receiving the investment must continuously meet the QHTB requirements for the year of investment and for each of the following four years, and the investment must remain in the QHTB for each of those years without being sold by the taxpayer. Should (1) the business no longer qualify as a QHTB; (2) the business or an interest in the business be sold by the taxpayer investing in the QHTB; or (3) the taxpayer withdraw its investment wholly or partially from the QHTB, then the credit generated by that investment cannot be claimed in that year and 10% of the amount of the total tax credit claimed by the taxpayer in each of the two taxable years prior to that year must be added to the taxpayer's tax liability for that taxable year.

To be considered a QHTB for purposes of the Investment Credit, in each of the years for which the credit will be claimed, the business must employ or own capital or property, or maintain an office, in Hawaii and meet either the Activity Test or the Gross Income Test. A business will meet the Activity Test if more than 50% of its total business activities are in qualified research and more than 75% of its qualified research is conducted in Hawaii. A business will meet the Gross Income Test if more than 75% of its gross income is derived from qualified research and the income from this qualified research is received from either (a) products sold from, manufactured, or produced in

Hawaii or (b) services performed in Hawaii. For purposes of the Investment Credit, "qualified research" is simply defined as:

- (1) The same as in § 41(d), Internal Revenue Code;
- (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.

When an investment is made through an entity taxed as a partnership, the entity may allocate this credit without regard to the normal allocation rules, which require allocation based upon the interests of its partners or members. However, any allocation that allows a taxpayer to receive a credit which is more than 100% of the taxpayer's original investment must satisfy the common law doctrines of economic substance and business purpose, which is presumed to be satisfied if a taxpayer receives a credit allocation that is 1.5 times or less than the taxpayer's original investment.

Tax credit for research activities (the "Research Credit")

Hawaii's income tax law also includes a credit against income taxes for performing certain qualified research in Hawaii. The credit amount is 20% of certain qualifying expenses incurred by a QHTB prior to December 31, 2010.

Only QHTBs may claim the Research Credit. If the business is a QHTB for purposes of the Investment Credit, it is a QHTB for purposes of the Research Credit. The credit amount, however, is based only upon the expenses incurred for research conducted in Hawaii that meets the requirements of § 41 of the Internal Revenue Code, which section is made operative for purposes of the Hawaii income tax law.

Like the Investment Credit, any claim, original or amended, must be made by the end of the year which follows the year the Research Credit may first be claimed. Failure to make the claim by the end of the following year acts as a waiver of the claim, and any credit not claimed by the deadline is lost. Unlike the Investment Credit, the Research Credit is a refundable credit, meaning that any portion of the credit that remains after the credit is applied to the income tax is refunded instead of being carried forward for use in subsequent tax years.

CURRENT REPORTING REQUIREMENTS

Certain reporting requirements are included in the provisions of the Investment Credit and the Research Credit. If a QHTB receives any investments, the QHTB or the investing taxpayer must apply for certification of those investments to the Department of Taxation by March 30 of the following year using Form N-318A, Statement of Investment in a Qualified High Technology Business. If a QHTB conducts activities in Hawaii that meet the definition of "qualified research" in § 41(d) of the Internal Revenue Code, the QHTB must apply for certification of the qualifying expenditures to the Department of Taxation by March 30 of the following year using Form N-319A, Statement of Research and Development Costs. If the required form and information is not submitted to the Department before March 31 (hence the March 30 deadline), then a certificate will not be issued. The certificate must be filed with the taxpayer's tax return on which the credit is claimed. The Investment Credit is claimed by filing Form N-318, High Technology Business Investment Tax Credit, with the taxpayer's return and the Research Credit is claimed by filing Form N-319, Credit for Research Activities, with the taxpayer's return.

The Department also created Form N-317, Statement by a Qualified High Technology Business, which is required to be filed by all QHTBs by the twentieth day of the fourth month following the end of a taxable year. A new reporting requirement was mandated by Act 206, Session Laws of Hawaii ("SLH") 2007. If a QHTB receives an investment after June 30, 2007 for which the Investment Credit may be claimed, the

QHTB is required to complete an electronic survey on the Department's website for each year of the five-year period the credit may be claimed.

HISTORY

1999: Act 178, SLH 1999 ("Act 178")

Both the high-technology business investment tax credit and the tax credit for research activities were introduced into Hawaii's income tax law in 1999 with Act 178. In Section 1 of Act 178, the legislature found that "businesses – particularly small, start-ups associated with high technology – no longer need[ed] to factor in Hawaii's geographic isolation," instead it was the "cost of doing business in the State" and the "confusing, often overlapping, group of state agencies that provided support for technology-related business" that presented the hurdles to the development and support of high technology resources. Act 178 was designed with the goal of "providing targeted assistance to these businesses, as well as a clear focus of responsibility with state government for aggressive development and support of high technology resources."¹ Part IX of Act 178 added the High-technology business investment tax credit (section 24) (the "Investment Credit") and the Tax credit for increasing research activities (section 25) (the "Research Credit"). Section 23 of the Act explains "the purpose of this Part is to assist in the creation of opportunities for high technology companies through the creation of tax credits for investing in high technology businesses and for increasing research activities."

¹ Section 1 of Act 178.

Both the Investment Credit and the Research Credit were set to expire on December 31, 2005.

The original Investment Credit was equal to ten per cent of the investment, up to a maximum credit of \$500,000 for the taxable year. The Investment Credit originally defined a "Qualified high technology business" in much the same way it is currently defined; however, among other things, it required that either 100% of the activities of the business be in qualified research or 100% of its gross income be derived from qualified research. The Investment Credit also listed a number of specific businesses that could not be "Qualified high technology business" under any circumstance. The Investment Credit also limited "Qualified research" to the same as section 41(d) of the Internal Revenue Code and the developing, designing, modifying, programming, and licensing computer software.

The legislature originally intended the Research Credit to conform to Internal Revenue Code ("IRC") sections 41 and 280,² which, in general, only provided a tax credit for research expenditures that exceeded research expenditures in previous tax years. The Research Credit was limited to 2.5% of the excess, as opposed to the 20% allowed by the federal government. Unlike the current law, the Research Credit, as originally adopted, was not refundable.

² Floor discussion regarding Conference Committee Report 122 (1999): "Allows a tax credit for increased research activities performed in Hawaii by conforming State tax provisions to the federal IRC 41 and 280, relating to qualified research."

The legislature revisited these incentives in 2000 (Act 297), 2001 (Act 221) and 2004 (Act 215).

2000: Act 297, SLH 2000 ("Act 297")

As part of Act 297, relating to the New Economy legislation, the legislature amended the Investment Credit and the Research Credit. Again, the legislature supported application to high technology businesses in a broad sense: "The purpose of this Act is to encourage the continued growth and development of high technology businesses and associated industries."³ As a further indication of the broad scope of the high technology incentives, Act 297 added explicit legislative intent that the amendments made by Act 297 to the Investment Credit and the Research Credit should be "liberally construed" and that "the department of taxation is given latitude to interpret those amendments in light of current industry standards."⁴

The Investment Credit was amended to lower the activity and gross income thresholds from 100% to more than 50% (of which 75% must be done in Hawaii) and more than 75%, respectively. Also the legislature redefined "Qualified research" by altering the description of qualifying computer software activities, adding biotechnology, and removing the exception regarding research conducted outside of the State. The definitions of "Computer software" and "Investment" were moved to section 235-1, to which definitions for "Biotechnology," "Computer data," and "Computer Program" were

³ Section 1 of Act 297.

⁴ Section 10 of Act 297.

also added. Also of significance to the Investment Credit was the addition of section 235-2.45(d), which excepted allocation of the Investment Credit from the operation of section 704 of the Internal Revenue Code, allowing "partnership investors the flexibility of allocating the [Investment Credit] among partners without regard to their proportionate interests in their partnership investment vehicle."⁵

The Research Credit was amended to make it a refundable credit. It was also increased from 2.5% to 20% "to match the federal rate."⁶

2001: Act 221, SLH 2001 ("Act 221")

In 2001, the legislature made the "third in Hawaii's efforts to provide tax relief to high technology activities to encourage growth of this industry."⁷ Section 1 of Act 221 explains:

Through Act 178, Session Laws of Hawaii (SLH) 1999, and Act 297, SLH 2000, the legislature provided a platform to encourage the continued growth and development of high technology businesses and associated industries in Hawaii. These legislative efforts have resulted in growing interest in Hawaii as a "New Economy" marketplace. Additional incentive must now be put in place to set Hawaii

⁵ Section 2 of Act 297.

⁶ Section 2 of Act 297.

⁷ From Conference Committee Report 107, 2001 Senate Journal, p. 900.

apart as a tech-friendly place to do business for both technical and non-technical businesses.

Act 221 also expanded the reach of the Investment Credit by including "other technology intensive industries that are helping revitalize Hawaii's economy."⁸ The legislature did, however, refrain at conference committee from expanding the Research Credit to performing arts products, biotechnology, computer software design, sensor and optic technologies, ocean sciences, astronomy, or non-fossil fuel energy-related technology without having to meet the requirements of section 41 of the Internal Revenue Code.⁹ The legislature added explicit legislative intent that the amendments made by Act 221 to the Investment Credit and the Research Credit were to be "liberally construed" and that "[t]he department of taxation is further given latitude to interpret these amendments in light of industry developments."¹⁰

The Investment Credit was increased from 10% (up to \$500,000) to 100% (up to \$2,000,000), but staggered over five years. Due to the staggered recovery of the Investment Credit, a recapture provision was added in order to ensure that the investment stayed in a qualified high technology business for the full five years. Qualified research was again redefined by incorporating the definition used for section 235-7.3. The effect of incorporating this definition was to allow investments made in certain businesses involved in IRC Section 41, research, performing arts products, certain computer software development and design, biotechnology, sensor and optic technologies, ocean

⁸ From House Standing Committee Report 528, 2001 House Journal, p. 1332.

⁹ From Conference Committee Report 107, 2001 Senate Journal, p. 900.

¹⁰ Section 13 of Act 221.

sciences, astronomy, or nonfossil fuel energy-related technology to qualify for the Investment Credit. Further, the specific restrictions on certain businesses from qualifying as a high technology business were removed.

Although the Research Credit remained tied to only those expenditures that satisfied section 41, IRC, the act expanded the tax credit to include all qualifying research expenditures, not just those expenditures that exceeded the expenditures from previous tax years.

2004: Act 215, SLH 2004 ("Act 215")

Section 2 of Act 215 states that Part II of the Act is intended to "improve currently available tax incentives developed for the high technology industry." The Conference Committee reviewing House Bill 2396¹¹ found that "the high technology business in Hawaii is growing quickly and maturing into a promising and competitive industry" and that "[t]o continue growing and to ensure that these industries remain in Hawaii, new financing opportunities must be developed and implemented."¹² The Act added certification requirements and removed from the previous Acts¹³ the statements of legislative intent that amendments to the Investment Credit and Research Credit be liberally construed. Instead, the legislature directed that all of the amendments be construed in a manner consistent with the intent of the particular act amending the high

¹¹ H.B. 2396 became Act 215.

¹² From Conference Committee Report 144-04 RE: H.B. 2396 HD2 SD2, CD1 (2004).

¹³ In particular Act 297 and Act 221.

technology incentives. Act 215 also extended the expiration of the Investment Credit and the Research Credit to December 31, 2010.

Besides the certification requirements, Act 215 added an allocation safe harbor provision to the common law principle requiring that investment transaction have economic substance and business purpose. Since Act 297, the allocation requirements of IRC Section 704, did not operate with respect to the Investment Credit. The legislature created a rebuttable presumption that any allocation of the Investment Credit of one and one-half times or less of the original investment amount satisfied economic substance and business purpose. The legislature, however, required that taxpayers substantiate economic substance and business purpose for transactions involving an allocation of the Investment Credit equal to more than twice the original investment amount.

Prior to Act 215 in 2004, the Research Credit was available to all taxpayers. Act 215 limited the Research Credit to only qualified high technology businesses, effective July 1, 2004.

Form N-317:

In April 2003, the Department announced the filing requirements for new and revised tax forms, including new tax form N-317, created to allow the Department to administer the high technology business investment tax credit for calendar year 2002.¹⁴

Form N-317, Statement by a Qualified High Technology Business, is used to report cash

¹⁴ Department of Taxation Announcement No. 2003-01, dated April 8, 2003.

investments received by a QHTB in the applicable calendar year and to provide support of the QHTB qualification for that applicable calendar year.

Every QHTB was required to file the initial Form N-317 by June 16, 2003 for calendar year 2002. For each calendar year after 2002, every QHTB has been required to file Form N-317 by, in most instances, April 20th of the following year.

APPENDIX IV
FACSIMILES OF FORM N-317

Name of Qualified High Technology Business	SSN or FEIN	GE ID No.
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Please complete all applicable parts of Form N-317 on a calendar year basis and attach all required information. If a completed and signed Form N-317 and the required attachments are not filed by June 16, 2003, the QHTB will be subject to sections 231-34, 231-35, and 231-36, Hawaii Revised Statutes (HRS). See Department of Taxation Announcement No. 2003-1, RE: New and Revised High Technology Business Investment Tax Credit. Please mail a completed and signed Form N-317 and attachments to the High Technology Filing Unit, Department of Taxation, P.O. Box 259, Honolulu, HI 96809-0259.

Part I. QUALIFICATION AS A QHTB

- A. Enter the date the QHTB began doing business in Hawaii: ___ / ___ / ___
- B. Describe the nature of the QHTB's business and briefly explain the product or service created or envisioned to be created by the QHTB. Check here if a statement is attached: _____

C. Check the boxes that describe the qualified research activities performed by the QHTB in calendar year 2002.

<input type="checkbox"/>	The same as in section 41(d) of the Internal Revenue Code	
<input type="checkbox"/>	Biotechnology, as defined in section 235-1, Hawaii Revised Statutes (HRS)	The development and design of computer software, as defined in section 235-1, HRS, using fourth generation or higher software development tools or native programming languages to design and construct unique and specific code to create applications and design databases for sale or license.
<input type="checkbox"/>	Performing arts products, as defined in section 235-7.3(c), HRS	
<input type="checkbox"/>	Sensor and optic technologies	
<input type="checkbox"/>	Ocean sciences	
<input type="checkbox"/>	Astronomy	
<input type="checkbox"/>	Nonfossil fuel energy-related technology	<input type="checkbox"/>

- D. Please provide the following information based on actual activities of the QHTB during the calendar year 2002. Otherwise provide the following information based on proposed activities of the QHTB for the calendar year 2003 and indicate that the information is based on (a) QHTB's proposed activities for the calendar year 2003 and (b) the QHTB's best faith estimate: (1)(i) list the number and describe the TOTAL jobs created by the QHTB, (ii) list the number and describe the NEW jobs created by the QHTB, and (iii) list and describe whether such jobs are PERMANENT or TEMPORARY (temporary meaning a job in which a new employee is hired for a specific duration of time or season); (2)(i) provide the total salaries and wages (by job classification) paid by the QHTB, (ii) explain briefly whether any salaries, wages, or compensation for each job classification involves or contemplates property (e.g., stock options), and (iii) provide a description of the quality and quantity of such property compensation; (3) list, generally, the costs incurred in Hawaii, including employee costs (e.g., rental or purchase of property from Hawaii sources, payments to Hawaii independent contractors for services); (4) briefly describe the QHTB's long-term business plans in Hawaii and elsewhere and the benefits provided to Hawaii; and (5) describe any tax incentives, including the tax credit for research activities as provided in section 235-110.91, HRS, claimed by the QHTB. If additional space is necessary, please attach a statement. Check here if a statement is attached: _____

Part II. INVESTMENTS RECEIVED BY THE QHTB

- A. Enter the total amount of investments received by the QHTB from investors in calendar year 2002: \$ _____
- B. Attach a list containing the following information about each investor:
- Name, address, and SSN/FEIN of each investor of the QHTB;
 - The amount of the investment and the date the investment was received;
 - A description of the investment (e.g., cash, intangible personal property, tangible personal property, real property);
 - If the investment is property, briefly explain and attach documentation supporting the valuation of the property; and
 - What the investor received in return for this investment (e.g., the number of shares of stock in the QHTB, the number of units in the QHTB, promissory note, license, etc.)

Declaration

I hereby certify under the penalties of perjury that I have the authority to sign Form N-317 on behalf of the QHTB. I declare, under the applicable penalties set forth in sections 231-34, 231-35, and 231-36, HRS, and chapter 431, HRS, (if applicable) that the information reported on Form N-317 (including any accompanying lists, schedules, statements, etc.) has been examined by me and, to the best of my knowledge and belief, is true, correct, and complete and made in good faith, pursuant to Chapter 235, HRS (Hawaii Income Tax Law); and if applicable, pursuant to Chapter 241, HRS (Hawaii Taxation of Banks or Other Financial Corporations) and Chapter 431, HRS (Hawaii Insurance Code).

Signature _____

Date _____

Print Name _____

Title _____

Name of Qualified High Technology Business	SSN or FEIN	GE ID No.
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Please complete all applicable parts of Form N-317 on a calendar year basis and attach all required information. If a completed Form N-317 and the required attachments are not filed by April 20, 2004, the QHTB will be subject to sections 231-34, 231-35, and 231-36, Hawaii Revised Statutes (HRS). Please mail Form N-317 and attachments to the High Technology Filing Unit, Department of Taxation, P.O. Box 259, Honolulu, HI 96809-0259.

Part I QUALIFICATION AS A QHTB

A. Enter the date the QHTB began doing business: _____ / _____ / _____
 B. Describe the nature of the QHTB's business and briefly explain the product or service created or envisioned to be created by the QHTB. Check here if a statement is attached: _____

- C. Check the boxes that describe the qualified research activities performed by the QHTB in calendar year 2003.
- | | |
|--|--|
| <input type="checkbox"/> The same as in section 41(d) of the Internal Revenue Code | <input type="checkbox"/> Astronomy |
| <input type="checkbox"/> Biotechnology, as defined in section 235-1, HRS | <input type="checkbox"/> Nonfossil fuel energy-related technology |
| <input type="checkbox"/> Performing arts products, as defined in section 235-7.3(c), HRS | <input type="checkbox"/> The development and design of computer software, as defined in section 235-1, HRS, using fourth generation or higher software development tools or native programming languages to design and construct unique and specific code to create applications and design databases for sale or license. |
| <input type="checkbox"/> Sensor and optic technologies | |
| <input type="checkbox"/> Ocean sciences | |

- D. Please provide the following information:
- (a) Actual number of jobs created by the QHTB since inception _____
 (b) Actual number of NEW jobs created by the QHTB in 2003 _____
 (c) Total Salaries paid in 2003 \$ _____
 Number of employees paid in 2003 _____
 (d) Do any salary amounts or compensation involve property? (e.g., stock options) Yes No
 - Amount of costs incurred in Hawaii during 2003 (including employee costs) \$ _____
 - Separate sheet must be attached providing the following information:
 - description of jobs created or to be created (include when jobs created and whether such jobs are PERMANENT or TEMPORARY);
 - description of any property compensations;
 - breakdown of costs incurred in Hawaii during 2003;
 - description of the QHTB's long-term business plans in Hawaii and elsewhere and the benefits provided to Hawaii; and
 - list the tax incentives, including the tax credit for research activities as provided in section 235-110.91, HRS, claimed or expected to be claimed by the QHTB.

Part II INVESTMENTS RECEIVED BY THE QHTB

- A. Enter the total amount of investments received by the QHTB from investors in calendar year 2003: \$ _____
 B. Attach a list containing the following information about each investor:
- Name, address, and SSN/FEIN of each investor of the QHTB;
 - The amount of the investment, the date the investment was received;
 - A description of the investment (e.g., cash, intangible personal property, tangible personal property, real property);
 - If the investment is property, briefly explain and attach documentation supporting the valuation of the property; and
 - What the investor received in return for this investment (e.g., the number of shares of stock in the QHTB, the number of units in the QHTB, promissory note, license, etc.)

DECLARATION

I hereby certify under the penalties of perjury that I have the authority to sign Form N-317 on behalf of the QHTB. I declare, under the applicable penalties set forth in sections 231-34, 231-35, and 231-36, HRS, and chapter 431, HRS, that the information reported on Form N-317 (including any accompanying lists, schedules, statements, etc.) has been examined by me and, to the best of my knowledge and belief, is true, correct, and complete and made in good faith, pursuant to Chapter 235, HRS (Hawaii Income Tax Law); Chapter 241, HRS (Hawaii Taxation of Banks or Other Financial Corporations); and Chapter 431, HRS (Hawaii Insurance Code).

SIGNATURE

DATE

PRINT NAME

TITLE

Name of Qualified High Technology Business	SSN or FEIN
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Please complete all applicable parts of Form N-317 on a calendar year basis and attach all required information. If a completed Form N-317 and the required attachments are not filed by April 20, 2005, the QHTB will be subject to sections 231-34, 231-35, and 231-36, Hawaii Revised Statutes (HRS). Please mail Form N-317 and attachments to the High Technology Filing Unit, Department of Taxation, P.O. Box 259, Honolulu, HI 96809-0259.

Part I QUALIFICATION AS A QHTB

- A. Enter the date the QHTB began doing business: _____/_____/_____
- B. Describe the nature of the QHTB's business and briefly explain the product or service created or envisioned to be created by the QHTB. Check here if a statement is attached: _____

- C. Check the boxes that describe the qualified research activities performed by the QHTB in calendar year 2004.
- | | |
|--|--|
| <input type="checkbox"/> The same as in section 41(d) of the Internal Revenue Code | <input type="checkbox"/> Astronomy |
| <input type="checkbox"/> Biotechnology, as defined in section 235-1, HRS | <input type="checkbox"/> Nonfossil fuel energy-related technology |
| <input type="checkbox"/> Performing arts products, as defined in section 235-7.3(c), HRS | <input type="checkbox"/> The development and design of computer software, as defined in section 235-1, HRS, 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 shall have substantial control and retain substantial rights to the resulting intellectual property. |
| <input type="checkbox"/> Sensor and optic technologies | |
| <input type="checkbox"/> Ocean sciences | |

- D. Please provide the following information:
- (a) Actual number of jobs created by the QHTB since inception _____
 - (b) Actual number of NEW jobs created by the QHTB in 2004 _____
 - (c) Total Salaries paid in 2004 \$ _____
 - (d) Do any salary amounts or compensation involve property? (e.g., stock options) Yes No
2. Amount of costs incurred in Hawaii during 2004 (including employee costs) \$ _____
3. Separate sheet must be attached providing the following information:
- (a) description of jobs created or to be created (include when jobs created and whether such jobs are PERMANENT or TEMPORARY);
 - (b) description of any property compensations;
 - (c) breakdown of costs incurred in Hawaii during 2004;
 - (d) description of the QHTB's long-term business plans in Hawaii and elsewhere and the benefits provided to Hawaii; and
 - (e) list the tax incentives, including the tax credit for research activities as provided in section 235-110.91, HRS, claimed or expected to be claimed by the QHTB.

Part II INVESTMENTS RECEIVED BY THE QHTB

- A. Enter the total amount of investments received by the QHTB from investors in calendar year 2004: \$ _____
- B. Attach a list containing the following information about each investor:
1. Name, address, and SSN/FEIN of each investor of the QHTB;
 2. The amount of the investment, the date the investment was received;
 3. A description of the investment (e.g., cash, intangible personal property, tangible personal property, real property);
 4. If the investment is property, briefly explain and attach documentation supporting the valuation of the property; and
 5. What the investor received in return for this investment (e.g., the number of shares of stock in the QHTB, the number of units in the QHTB, promissory note, license, etc.)

DECLARATION

I hereby certify under the penalties of perjury that I have the authority to sign Form N-317 on behalf of the QHTB. I declare, under the applicable penalties set forth in sections 231-34, 231-35, and 231-36, HRS, and chapter 431, HRS, that the information reported on Form N-317 (including any accompanying lists, schedules, statements, etc.) has been examined by me and, to the best of my knowledge and belief, is true, correct, and complete and made in good faith, pursuant to Chapter 235, HRS (Hawaii Income Tax Law); Chapter 241, HRS (Hawaii Taxation of Banks or Other Financial Corporations); and Chapter 431, HRS (Hawaii Insurance Code).

SIGNATURE

DATE

PRINT NAME

TITLE

Name of Qualified High Technology Business	SSN or FEIN
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Please complete all applicable parts of Form N-317 on a calendar year basis and attach all required information. If a completed Form N-317 and the required attachments are not filed by April 20, 2006, the QHTB will be subject to sections 231-34, 231-35, and 231-36, Hawaii Revised Statutes (HRS). Please mail Form N-317 and attachments to the High Technology Filing Unit, Department of Taxation, P.O. Box 259, Honolulu, HI 96809-0259.

Part I QUALIFICATION AS A QHTB

A. Enter the date the QHTB began doing business: _____ / _____ / _____
B. Describe the nature of the QHTB's business and briefly explain the product or service created or envisioned to be created by the QHTB. Check here if a statement is attached: _____

C. Check the boxes that describe the qualified research activities performed by the QHTB in calendar year 2005.

<input type="checkbox"/> The same as in section 41(d) of the Internal Revenue Code	<input type="checkbox"/> Astronomy
<input type="checkbox"/> Biotechnology, as defined in section 235-1, HRS	<input type="checkbox"/> Nonfossil fuel energy-related technology
<input type="checkbox"/> Performing arts products, as defined in section 235-7.3(c), HRS	<input type="checkbox"/> The development and design of computer software, as defined in section 235-1, HRS, 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 shall have substantial control and retain substantial rights to the resulting intellectual property.
<input type="checkbox"/> Sensor and optic technologies	
<input type="checkbox"/> Ocean sciences	

D. Please provide the following information:

1. (a) Actual number of jobs created by the QHTB since inception _____	(c) Total Salaries paid in 2005 \$ _____
(b) Actual number of NEW jobs created by the QHTB in 2005 _____	Number of employees paid in 2005 _____
2. Amount of costs incurred in Hawaii during 2005 (including employee costs) \$ _____	(d) Do any salary amounts or compensation involve property? (e.g., stock options) <input type="checkbox"/> Yes <input type="checkbox"/> No
3. Separate sheet must be attached providing the following information:	
(a) description of jobs created or to be created (include when jobs created and whether such jobs are PERMANENT or TEMPORARY);	
(b) description of any property compensations;	
(c) breakdown of costs incurred in Hawaii during 2005;	
(d) description of the QHTB's long-term business plans in Hawaii and elsewhere and the benefits provided to Hawaii; and	
(e) list the tax incentives, including the tax credit for research activities as provided in section 235-110.91, HRS, claimed or expected to be claimed by the QHTB.	

Part II INVESTMENTS RECEIVED BY THE QHTB

A. Enter the total amount of investments received by the QHTB from investors in calendar year 2005: \$ _____
B. Attach a list containing the following information about each investor:

- Name, address, and SSN/FEIN of each investor of the QHTB;
- The amount of the investment, the date the investment was received;
- A description of the investment (e.g., cash, intangible personal property, tangible personal property, real property);
- If the investment is property, briefly explain and attach documentation supporting the valuation of the property; and
- What the investor received in return for this investment (e.g., the number of shares of stock in the QHTB, the number of units in the QHTB, promissory note, license, etc.)

DECLARATION

I hereby certify under the penalties of perjury that I have the authority to sign Form N-317 on behalf of the QHTB. I declare, under the applicable penalties set forth in sections 231-34, 231-35, and 231-36, HRS, and chapter 431, HRS, that the information reported on Form N-317 (including any accompanying lists, schedules, statements, etc.) has been examined by me and, to the best of my knowledge and belief, is true, correct, and complete and made in good faith, pursuant to Chapter 235, HRS (Hawaii Income Tax Law); Chapter 241, HRS (Hawaii Taxation of Banks or Other Financial Corporations); and Chapter 431, HRS (Hawaii Insurance Code).

SIGNATURE

DATE

PRINT NAME

TITLE

Name of Qualified High Technology Business	SSN or FEIN
--	-------------

Please complete all applicable parts of Form N-317 on a calendar year basis and attach all required information. If a completed Form N-317 and the required attachments are not filed by April 20, 2007, the QHTB will be subject to sections 231-34, 231-35, and 231-36, Hawaii Revised Statutes (HRS). Please mail Form N-317 and attachments to the High Technology Filing Unit, Department of Taxation, P.O. Box 259, Honolulu, HI 96809-0259.

Part I QUALIFICATION AS A QHTB

- A. Enter the date the QHTB began doing business: _____ / _____ / _____
- B. Describe the nature of the QHTB's business and briefly explain the product or service created or envisioned to be created by the QHTB. Check here if a statement is attached: _____

- C. Check the boxes that describe the qualified research activities performed by the QHTB in calendar year 2006.
- | | |
|---|---|
| <input type="checkbox"/> The same as in section 41(d) of the Internal Revenue Code
<input type="checkbox"/> Biotechnology, as defined in section 235-1, HRS
<input type="checkbox"/> Performing arts products, as defined in section 235-7.3(c), HRS
<input type="checkbox"/> Sensor and optic technologies
<input type="checkbox"/> Ocean sciences | <input type="checkbox"/> Astronomy
<input type="checkbox"/> Nonfossil fuel energy-related technology
<input type="checkbox"/> The development and design of computer software, as defined in section 235-1, HRS, 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 shall have substantial control and retain substantial rights to the resulting intellectual property. |
|---|---|

- D. Please provide the following information:
- | | |
|---|--|
| 1. (a) Actual number of jobs created by the QHTB since inception _____
(b) Actual number of NEW jobs created by the QHTB in 2006 _____
2. Amount of costs incurred in Hawaii during 2006 (including employee costs) \$ _____
3. Separate sheets must be attached providing the following information:
(a) description of jobs created or to be created (include when jobs created and whether such jobs are PERMANENT or TEMPORARY);
(b) description of any property compensations;
(c) breakdown of costs incurred in Hawaii during 2006;
(d) description of the QHTB's long-term business plans in Hawaii and elsewhere and the benefits provided to Hawaii; and
(e) list the tax incentives, including the tax credit for research activities as provided in section 235-110.91, HRS, claimed or expected to be claimed by the QHTB. | (c) Total Salaries paid in 2006 \$ _____
Number of employees paid in 2006 _____
(d) Do any salary amounts or compensation involve property? (e.g., stock options) <input type="checkbox"/> Yes <input type="checkbox"/> No |
|---|--|

Part II INVESTMENTS RECEIVED BY THE QHTB

- A. Enter the total amount of investments received by the QHTB from investors in calendar year 2006: \$ _____
- B. Attach a list containing the following information about each investor:
1. Name, address, and SSN/FEIN of each investor of the QHTB;
 2. The amount of the investment and the date the investment was received;
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 5. What the investor received in return for this investment (e.g., the number of shares of stock in the QHTB, the number of units in the QHTB, promissory note, license, etc.)

DECLARATION

I hereby certify under the penalties of perjury that I have the authority to sign Form N-317 on behalf of the QHTB. I declare, under the applicable penalties set forth in sections 231-34, 231-35, and 231-36, HRS, and chapter 431, HRS, that the information reported on Form N-317 (including any accompanying lists, schedules, statements, etc.) has been examined by me and, to the best of my knowledge and belief, is true, correct, and complete and made in good faith, pursuant to Chapter 235, HRS (Hawaii Income Tax Law); Chapter 241, HRS (Hawaii Taxation of Banks or Other Financial Corporations); and Chapter 431, HRS (Hawaii Insurance Code).

SIGNATURE

DATE

PRINT NAME

TITLE

