

1  
2  
3  
4  
5  
6  
7  
8  
9  
10  
11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25

House Committee on Finance  
Public Hearing  
R&D Tax Credit  
Pittsburgh Technology Council  
2000 Technology Drive  
Pittsburgh, Pennsylvania 15129-3112

---

Date: Wednesday, March 26, 2008

Reporter: Donna M. McMullen, RMR

1 Committee Members:

2

3 Representative David K. Levdansky (D)  
4 Finance Committee, Chairperson  
5 39th Legislative District  
6 Allegheny County (part)  
7 Washington County (part)

6

7 Representative Chris Sainato (D)  
8 9th Legislative District  
9 Beaver County (part)  
10 Lawrence County (part)

9

10 Representative Tim Seip (D)  
11 125th Legislative District  
12 Berks (part) and Schuylkill (part) Counties

12 Representative Dante Santoni, Jr. (D)  
13 126th Legislative District  
14 Berks County (part)

14

15 Representative Dan Frankel (D)  
16 23rd Legislative District  
17 Allegheny County (part)

17

18 Representative William C. Kortz, II (D)  
19 38th Legislative District  
20 Allegheny County (part)

20 Representative Daryl D. Metcalfe (R)  
21 12th District  
22 Butler County (part)

22

23

24

25

1	I N D E X	
2	SPEAKER	PAGE
3		
4	Introductions/Opening Remarks Representative Levdansky	4
5		
6	Brian Kennedy, Vice President of Government Relations and External Affairs, Pittsburgh Technology Council	7
7		
8	Dr. William Hsu, Vice President and Chief Technology Officer	
9	Kennametal	23
10	Sean Rollman, Chief Financial Officer Plextronics	30
11		
12	Joseph Jacobson, Chief Financial Officer Akustica	35
13	Larry Sweeney, Vocollect	44
14		
15		
16		
17		
18		
19		
20		
21		
22		
23		
24		
25		

1  
2  
3  
4  
5  
6  
7  
8  
9  
10  
11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25

---

P R O C E E D I N G S

(10:15 a.m.)

REPRESENTATIVE DAVID KEVDANSKY: Good morning.

I want to welcome everybody, both members and people that are testifying in the audience to this meeting of the House Finance Committee. My name is David Levdansky. I'm a legislator from the 39th District down around Clairton and Elizabeth and over into Washington County, around New Eagle and Finleyville, in that area. And we're having this hearing today on House Bill 2250, which is legislation I think of vital importance to Pennsylvania's business community.

So much of our Pennsylvania businesses operate in not just a national, but a global economy. And the key to our companies' competitive edge is their ability to invest in research and development. And the technologies and processes that come out of that enable our companies to stay competitive in the global marketplace.

This legislation that we're having a hearing on today would increase the research and development tax credit from the present level of 45 million and increase it to 75 million. It

1           would also increase the set aside for small  
2           businesses from 8 million to 15 million. It would  
3           make some other changes in the utilization of the  
4           tax credits I think to make them more useful to  
5           the business community. So I want to thank you  
6           all of you for being here.

7                         Let me first call on the members, and we  
8           apologize for being a little bit late. We had a  
9           couple of stragglers from the other end of the  
10          state arriving a little bit late, and we  
11          appreciate them being here. Let me start by  
12          having members introduce themselves starting from  
13          the far left.

14                        REPRESENTATIVE DAN FRANKEL: I'm Representative  
15          Dan Frankel from here in the City of Pittsburgh. My  
16          district just neighbors this area Second Avenue.

17                        REPRESENTATIVE WILLIAM C. KORTZ: Good morning.  
18          My name is Bill Kortz from Allegheny County, the 38th  
19          District, West Mifflin area.

20                        REPRESENTATIVE TIM SEIP: Representative Tim  
21          Seip. I represent parts of Berks and Schuylkill  
22          Counties, the Cabela's and Yuengling district.

23                        REPRESENTATIVE WILLIAM KORTZ: And Pottstown.

24                        REPRESENTATIVE TIM SEIP: The Pottsville  
25          Maroons, the real 1925 World Champions.

1                   REPRESENTATIVE DANTE SANTONI: I'm Dante  
2                   Santoni from Berks County, also the Reading area.

3                   REPRESENTATIVE CHRIS SAINATO: I'm  
4                   Representative Chris Sainato. I represent the 9th  
5                   District in Lawrence County, and I have a small  
6                   section of Beaver County.

7                   REPRESENTATIVE DARYL METCALFE: Good morning.  
8                   I'm State Representative Daryl Metcalfe from Butler  
9                   County. I represent the 12th District and Vice  
10                  Chairman from the Republican side of the committee.  
11                  Yesterday I sat on Dave's very extreme left and was  
12                  introduced last, and today I sit on the extreme right,  
13                  thought I'd get introduced first, missed it again.  
14                  But good to be with you. The token Republican to  
15                  your -- back here today.

16                  REPRESENTATIVE DAVID KEVDANSKY: Back where you  
17                  belong.

18                  REPRESENTATIVE DARYL METCALFE: Good to be  
19                  here.

20                  REPRESENTATIVE DAVID KEVDANSKY: That's  
21                  inappropriate there. Let me thank Brian Kennedy and  
22                  the people at the Pittsburgh Technology Council for  
23                  hosting this. I can't think of a more appropriate  
24                  place for us to be having this hearing on this  
25                  legislation than here in the offices in the area where

1 I think it's key to technology and development here in  
2 western Pennsylvania, Brian.

3 What I'd like to suggest is to  
4 have Brian, if you could introduce the people from  
5 your panel, have each of the members give their  
6 testimony. And then I would ask that the members  
7 hold their questions until all the panelists have  
8 had a chance to offer their prospectus to us, if  
9 that's okay.

10 MR. BRIAN KENNEDY: Thank you, Mr. Chairman.  
11 Just as a brief introduction of myself, I'm Brian  
12 Kennedy, and I'm the Vice President of Government  
13 Relations for the Pittsburgh Technology Council.

14 As a quick background, we are a trade  
15 association representing innovative companies in  
16 southwestern Pennsylvania, 1400 companies from the  
17 13-county region. And I don't think we could have  
18 assembled a more appropriate panel of testifiers  
19 this morning.

20 With me today is the Chief Technology  
21 Officer for Kennametal. It's a small company  
22 located here in western Pennsylvania, William Hsu.

23 We also have Sean Rollman, the Chief  
24 Technology Officer of an exciting company that's  
25 making revelations in the clean technologies space

1           called Plextronics.

2                         We have Joseph Jacobson. He's also the  
3 Chief Financial Officer of Akustica, and  
4 Akustica's doing some great things in the MEMS  
5 space.

6                         And I'm also very pleased to have with us  
7 this morning Larry Sweeney who's one of the  
8 founders of Vocollect, which is one of the fastest  
9 growing companies, technology companies here in  
10 southwestern Pennsylvania. He's going to tell you  
11 about some of the great things going on at that  
12 company.

13                        We're really pleased to have each of  
14 these people. I think you're going to be excited  
15 to hear about some of the things going on in the  
16 companies, about the jobs that they're creating,  
17 and really about the real-world technology  
18 challenges that their companies are solving.

19                        You're going to know these companies in some way  
20 or another and use some of their products for  
21 sure. So with that, if you'd like me to begin my  
22 testimony.

23                        On behalf of our CEO, Audrey Russo, and  
24 our 1400 member companies, I'd like to bring you  
25 greetings. I'm particularly pleased this morning



1 to welcome you to southwestern Pennsylvania, which  
2 was recently recognized in the MoneyTree Report,  
3 which was done jointly by the National Venture  
4 Capital Association and Price Waterhouse Coopers,  
5 and they ranked southwestern Pennsylvania as the  
6 second fastest growing region in the country for  
7 venture capital activity.

8 And that's just fantastic news. It's in  
9 no small part because of some of the things that  
10 the state legislature has done in supporting the  
11 availability of venture capital and supporting  
12 groups like Innovation Works and the Pittsburgh  
13 Life Sciences Greenhouse and some of the other  
14 things you have done.

15 Pittsburgh is really turning around, and  
16 let me just tell you a little bit. Pennsylvania  
17 right now has 700,000 employees working in  
18 venture-backed firms across Pennsylvania. In  
19 terms of raw employees, we're behind only Texas  
20 and California in terms of employees working for  
21 venture-backed companies.

22 Here in southwestern Pennsylvania in 2006  
23 19 firms raised nearly a quarter of a billion  
24 dollars in venture capital to help fund their  
25 commercialization efforts. So, there are some

1 great things going on across the state,  
2 particularly here in southwestern Pennsylvania.

3 Innovation, which is what we're here to  
4 talk about today, plays a key role in that. There  
5 is a lot of work remaining though.

6 Before I start my testimony, I'd just  
7 again like to thank you, Chairman Levdansky, for  
8 holding this committee here in Pittsburgh. I'd  
9 like to thank each of the committee members for  
10 traveling here to talk about how the public sector  
11 and the private sector can work together to help  
12 make Pennsylvania the world's strongest economy.

13 To be sure, the benefits of promoting the  
14 innovation economy are clear. Here in  
15 southwestern Pennsylvania we're now home to more  
16 than 7,000 technology firms in various fields,  
17 including advanced manufacturing, life sciences,  
18 information technology, environmental technology,  
19 which, by the way, is one of our fastest growing  
20 clusters, and the advanced materials cluster.

21 Combined those firms now represent more  
22 than 10 percent of all businesses in the region,  
23 but they employ 17 percent of all employees, and  
24 at \$11 billion they account for almost a quarter  
25 of our annual payroll.

1                   Let me say that again. We're 10 percent  
2 of all businesses in the region, but almost a  
3 quarter of the payroll. These are some great  
4 jobs. As you might imagine, employees that  
5 support this industry are among the region's  
6 highest paid.

7                   For example, in the software industry,  
8 9300 employees are earning an annual salary in  
9 excess of \$75,000 annually. So, when we're  
10 talking about family-sustaining jobs here in  
11 Pennsylvania increasingly we're really talking  
12 about innovation economy jobs.

13                   As we look to the future of the role  
14 innovation is going to play in our economy, it's  
15 going to determine the outlook for our citizens  
16 and really for our government. To understand this  
17 let me talk a little bit about the manufacturing  
18 issue and some of the challenges that face now  
19 Pennsylvania's manufacturing economy and how  
20 innovation impacts that.

21                   You might know that in 2004  
22 Pennsylvania's Industrial Resource Centers joined  
23 forces with Team Pennsylvania, and they  
24 commissioned Deloitte to do really one of the most  
25 exhaustive studies that's ever been done on the

1 state of Pennsylvania's manufacturing economy.

2 One of the problems that they identified  
3 and something that really kind of surprises you  
4 and you really have to look into was the  
5 productivity of our workers was actually lower  
6 here in Pennsylvania. Now, when you look at it by  
7 gross product produced per worker it was at  
8 \$86,000 per worker and is somewhat below \$96,000,  
9 which is the national average.

10 So, it was kind of puzzling. We couldn't  
11 really get our arms around what that meant. And  
12 what really Deloitte concluded is it has nothing  
13 at all to do with the workers themselves. It has  
14 a whole lot more to do with the products that the  
15 workers are producing.

16 In Pennsylvania, our manufacturing sector  
17 really tends to be focused on commodity  
18 industries. Commodity industries, as you know,  
19 compete largely on price and are particularly  
20 vulnerable to global competition. And as prices  
21 go down and manufacturers don't find more  
22 efficient ways to produce their products their  
23 productivity rates as measured are going to also  
24 decline. And this leaves them in difficult  
25 positions and with difficult decisions to make.

1                   So to combat this dilemma and avoid the  
2                   so-called "race to the bottom," manufacturers  
3                   must, and in many cases are, working to develop  
4                   both innovative new products that are less  
5                   susceptible to low-cost competition and innovative  
6                   new manufacturing processes that increase their  
7                   ability to remain competitive in their existing  
8                   markets as well as the emerging market.

9                   Pennsylvania's economy has already made  
10                  some great progress in moving towards a more  
11                  innovation-focused economy. In fact, according to  
12                  a report compiled by the State Science and  
13                  Technology Institute, SSTI, there was more than  
14                  \$7 billion, there was more than \$7 billion of  
15                  annual industrial research and development  
16                  activity going on in Pennsylvania, so not  
17                  university research, industrial-funded research.

18                  When you look at that in gross dollars  
19                  that ranks Pennsylvania ninth in comparison to the  
20                  rest of the states. When you normalize that,  
21                  however, when you look at states on their gross  
22                  products, their gross state products and you  
23                  compare it to their R&D spending, we fall to 19th.

24                  Obviously still that's above average, but  
25                  there's considerable room to grow in terms of

1 encouraging more industrial research and  
2 development, to improve their process to become  
3 more efficient and to develop new products so they  
4 can increase topline revenues and grow here in  
5 Pennsylvania.

6 So as we look to accelerate the important  
7 transition to reverse the loss of manufacturing  
8 employment, there are many roles that the state  
9 can play. As it relates to the tax code, for  
10 example, we must quickly remove some of the  
11 components of our tax climate that are harmful to  
12 the growth of manufacturers. And on those issues,  
13 we're making some progress, including capital  
14 stock and franchise tax.

15 We're on track to have that tax  
16 eliminated by 2011. We really think we need to  
17 keep on track and get rid of that uncompetitive  
18 tax. Also net operating losses, we're one of the  
19 only states that caps NOL's. Those are two things  
20 that are just making us uncompetitive, and we have  
21 to fix that.

22 To enhance our competitiveness and to  
23 actually give us an edge on some of our  
24 competitors, the tech council is actually  
25 promoting two other ideas: One, move to a single

1 sales factor for the CNI; and, two, to create a  
2 very strong research development tax credit.

3 There will be plenty of opportunities to  
4 discuss the single sales and NOL issues, and  
5 perhaps the council will talk about those whenever  
6 we get an opportunity. But today I'm going to  
7 limit my testimony to the importance of improving  
8 and expanding Pennsylvania's R&D tax credit.

9 As a brief background, for those of you  
10 who might be new to the credit, it was originally  
11 created in 1997 as a way of keeping pace with  
12 other states in their efforts to capture increased  
13 industrial research and development activity  
14 within their borders and the great jobs and the  
15 results, of course, that that R&D results in for  
16 their manufacturing economy.

17 Pennsylvania's credit was modeled closely  
18 after the federal government's policy,  
19 particularly in that it rewards companies. It  
20 does not reward companies merely for investing in  
21 R&D.

22 So just because you do an R&D does not  
23 mean you get a credit. In fact, only companies  
24 that increase their expenditures on research and  
25 development tax credits are eligible. And, in

1 fact, only that increased amount is what's  
2 eligible for the credit.

3 Right now when it was created it was  
4 intended to be a 10 percent tax credit. So, for  
5 example, if you increased your R&D expenditures by  
6 a million dollars over your historical spending  
7 levels, you in theory would be eligible for a  
8 10 percent tax credit on that one million dollar  
9 increase, even though you might have been spending  
10 ten million and you increased it to 11 million,  
11 you're only eligible for a tax credit on that one  
12 million dollar increase.

13 And the General Assembly has done some  
14 pretty creative things in the last few years, and  
15 I'll talk about them later, but small businesses  
16 are actually eligible for a 20 percent tax credit.

17 Now, what's happening is that because  
18 Pennsylvania caps the amount of credits at  
19 \$40 million per year, companies are not actually  
20 receiving a 10 percent tax credit. So this year  
21 the state received qualified applications in  
22 excess of \$95 million for the R&D tax credit.

23 Now, right off the top, 8 million of the  
24 40 million is set aside for small business, and  
25 we're very happy about that. But what that means



1 is that on average not small businesses, the  
2 mid-size companies and the larger businesses are  
3 getting only 37 percent this year of what they  
4 applied for.

5 So instead of having a 10 percent tax  
6 credit what we really have is a 3 percent,  
7 3.7 percent tax credit, effective tax credit,  
8 unless we address the cap.

9 You've done some great things for small  
10 businesses. You've created a set-aside pool of  
11 \$8 million, you've let them claim a 20 percent tax  
12 credit, and you also allow them to sell unused tax  
13 credit. So there are a lot of small businesses  
14 who are just in their start-up mode who don't have  
15 tax liabilities.

16 But they can now get this tax credit. If  
17 they can't use it they can sell it. It puts that  
18 money right back into the commercialization of  
19 their products and their growth here in  
20 Pennsylvania.

21 As a result, these changes have resulted  
22 in strong growth and participation from small  
23 businesses. In fact, from 2004 to 2007, their  
24 participation increased from 81 firms who claimed  
25 over just over \$1 million to 193 firms last year

1           who claimed almost \$7 million in tax credits.

2                       So you're looking at a pretty sizeable  
3 increase in both the number of firms participating  
4 and the amount of credits they're claiming, and  
5 this is great news for our economy.

6                       Again, as I said, the smaller, not small  
7 businesses didn't fair as well because of the cap.  
8 So for this reason and a few others I'm here today  
9       to ask you to support House Bill 2250 introduced  
10 by Representative Levdansky before your committee,  
11 as we speak.

12                      Among other changes, this legislation  
13 would increase the cap from \$40 million to  
14 \$75 million. It's going to bring us a whole lot  
15 closer to meeting the actual demand for credits,  
16 and it's going to create a much stronger incentive  
17 for companies to consider further increases in the  
18 credit or in the research and development.

19                      So, let me just simplify this. What  
20 we're trying to do with the R&D tax credit is  
21 we're trying to give companies a greater reason to  
22 take a risk here in Pennsylvania. The nature of  
23 R&D is you don't know what's going to come from  
24 R&D. It's very high risk and the processes often  
25 take a lot of times. But we want, as a

1 Commonwealth, to encourage more of it.

2 The problem with our R&D tax credit right  
3 now is that it's not reliable. Dr. Hsu cannot go  
4 to his fellow management team and say, listen, if  
5 we spend a million dollars next year more on R&D  
6 at Kennemetal, we can expect to get a \$100,000 tax  
7 credit.

8 As a matter of fact, he doesn't have any  
9 idea how much he's going to get because the state  
10 can't tell him until all the companies have  
11 applied, and they then award the extra credits  
12 proportionately.

13 So we really need to help Dr. Hsu make  
14 his case and give him the tools that really we  
15 intended to give him when we created this credit  
16 back in 1997.

17 I might mention quickly that the credit  
18 this legislature has done many things to improve  
19 the credit over the past five years. Just five  
20 years ago the credit was at 15 million. It was  
21 capped at \$15 million, but good bipartisan  
22 support, we increased it, we doubled it to  
23 30 million, and then three years later we  
24 increased it to 40 million.

25 So there's definitely a precedent and

1           there's strong bipartisan support to increase the  
2           cap on the credit.

3                       I want to talk about a couple of the  
4           other things the legislation does that we consider  
5           to be more technical, of a more technical nature.  
6           One of the things is that companies who are  
7           allowed to sell the credit, they are now being  
8           asked to hold the credit for one year from the  
9           date that it's awarded before they're allowed to  
10          sell.

11                      Let me tell you how this works. In 2007,  
12          these companies are doing research and  
13          development. They apply for the credit for the  
14          work they're doing this year in September of next  
15          year. They're awarded the credits in December of  
16          2009.

17                      So small businesses who want to sell the  
18          credit, they have to wait until December of 2010  
19          to sell the credits. Now, remember, they're doing  
20          their R&D now. The budget for their R&D was made  
21          in 2007, not 2008.

22                      So, there's a three-year lapse really  
23          from the decision-making time to increase R&D  
24          expenditures to the time where the credit can  
25          actually have benefit.

1                   This legislation that eliminates that  
2                   one-year hold. We're very pleased with that. We  
3                   think it makes a lot of sense. I think if you  
4                   look at it, I think you'll agree that it's a  
5                   common sense policy that probably has outlived its  
6                   usefulness.

7                   The other thing we'll ask you to take a  
8                   look at, not in this legislation, but we'd like  
9                   you to take a look at is the definition right now  
10                  of small businesses. Right now small business,  
11                  for the purpose of this set aside, is defined as a  
12                  company with \$5 million or less in net assets, and  
13                  that's it. Nothing about their employment,  
14                  nothing about their revenues. And this is a  
15                  really unorthodox approach to defining and  
16                  characterizing small businesses.

17                  So what we would suggest is for the  
18                  committee to work with the Department of Community  
19                  and Economic Development and really try to come up  
20                  with a more accurate way of defining small  
21                  businesses because the result is that right now  
22                  small businesses are not claiming the \$8 million  
23                  that's available for their use. They're only  
24                  claiming 7 million. A few years ago they were  
25                  only claiming 2 million.

1                   And a lot of it is because of this  
2                   definition, how we characterize small businesses.  
3                   And what's happening is real small businesses in  
4                   the eyes of existing statutes are not being seen  
5                   as small businesses. So we'd like to see you work  
6                   with the Department of Community and Economic  
7                   Development and come up with a more traditional  
8                   way of defining small businesses and one that  
9                   allows us to fully leverage the small business set  
10                  aside.

11                  So as I conclude I'd like to again thank  
12                  you on behalf of our 1400 companies for evaluating  
13                  this. I'll tell you that we have 88 companies who  
14                  benefited from the R&D tax credit over the past  
15                  few years.

16                  And as you consider this issue and other  
17                  issues, we hope you'll consider us and our member  
18                  companies as an important resource in your  
19                  deliberations. Thank you again.

20                  So, next I'd now like to introduce one of  
21                  our esteemed panelists this morning. It's  
22                  Dr. William Hsu, who again serves as the Chief  
23                  Technology Officer of Kennametal, which is really,  
24                  as you'll soon hear, is going to be one of our  
25                  region's anchor manufacturing firms. It's at the

1 top of the food chain and is really doing a lot to  
2 help drive the economy.

3 With no further ado, I introduce  
4 Dr. William Hsu.

5 DR. WILLIAM HSU: Thank you, Brian.  
6 Mr. Chairman, Honorable Representative Levdansky and  
7 distinguished members of the Finance Committee. I  
8 usually go by my nickname Bill instead of my formal  
9 name William. So, I am Bill Hsu, Vice President and  
10 Chief Technical Officer of Kennametal.

11 And, Mr. Chairman, I'm really delighted  
12 by your good grasp of what the reality is. In  
13 your short opening statement you actually have  
14 taken the key point I wanted to relate to the  
15 committee anyway, but I think I will now give you  
16 a bit more details.

17 But the reality is that we are as a  
18 global competition, and we are using R&D to drive  
19 the competitive edge, not for ourselves, but for  
20 our customers. In fact, I cannot think of even a  
21 better paid commercial from you because I've paid  
22 mine. And our available position to the customer  
23 is engineering your competitive edge is the very  
24 opening statement that you make, so I'm delighted,  
25 Mr. Chairman. Thank you.

1 Kennametal is the leading global supplier  
2 of tooling solutions, engineered components and  
3 advanced materials that are consumed in our  
4 customers' manufacturing process. We improve our  
5 customers' competitiveness by providing superior  
6 economic returns through the delivery of advanced  
7 technology and application knowledge that master  
8 the toughest of materials processing demands of  
9 our customers.

10 Companies producing everything from  
11 airframes to coal, from medical implants to oil  
12 wells, and from turbo charges to motorcycle parts  
13 recognize our extraordinary contributions in the  
14 value chain.

15 We are a 2.4 billion global corporation  
16 representing 14,000 employees. Seven of our  
17 facilities are right here in the Commonwealth  
18 employing nearly 1,500 people where we also have  
19 our world headquarters in our global technology  
20 center.

21 In fact, Kennametal is the only publicly  
22 held corporation in our industry still  
23 headquartered in the United States. Our major  
24 competitors are companies in Israel, Sweden and in  
25 Japan, and we are competing for businesses at the



1 global stage. We win market shares customer by  
2 customer, application by application through our  
3 state-of-the-art technologies. We have to invest  
4 heavily and continuously in R&D application  
5 knowledge in order to satisfy the demanding needs  
6 of our customers.

7 We help our customers enhance their  
8 competitiveness in their market space against  
9 low-cost manufacturing countries by improving our  
10 customers' throughputs and lowering their unit  
11 production cost continuously. So that's why our  
12 valued purpose stature is "Engineering Your  
13 Competitive Edge."

14 To do this effectively, we created a  
15 breakthrough technology group in our corporate  
16 research center in Latrobe recently to work on  
17 cutting edge solutions for our customers.

18 Kennametal has more than a thousand  
19 highly trained and experienced research scientists  
20 and development engineers. We average more than  
21 40 U.S. patents every year recently and have been  
22 named three times best practice partner by  
23 American Productivity and Quality Center on three  
24 different areas: On R&D Productivity, Innovation  
25 and Product Development Portfolio Management.

1                   A measure of our commitment to R&D is our  
2                   realization of 47 percent of sales from products  
3                   less than five years old in the fiscal year 2007.  
4                   This is up from 17 percent of the late '90s, which  
5                   is all because of the R&D investment we have put  
6                   in recently. Additionally, since 2005, we have  
7                   increased our investment in R&D by \$5.8 billion.  
8                   A commitment in investment resulted in very  
9                   tangible successes. Over the past few years we  
10                  grew our revenues from \$1.7 billion in fiscal year  
11                  2003 to \$2.4 billion the last fiscal year. This  
12                  growth, half of it suddenly is because of the  
13                  economic cycle, but the other 50 percent is  
14                  definitely coming from the hard-won share gains  
15                  against our competitors in the global marketplace  
16                  through our superior new products. So, that's how  
17                  we drive growth, and that's why we have to  
18                  continuously invest in R&D.

19                  In today's competitive business and  
20                  climate and with the competition, both community  
21                  and economic development are at an all time high.  
22                  It is more important than ever that business and  
23                  government work together to meet the challenges of  
24                  not only a global economy, but the impact of a  
25                  global economy on our own state.

1                   It is important to note the following  
2                   with regard to the Commonwealth's business facts:  
3                   The manufacturing sector is the largest  
4                   contributor to Pennsylvania's economy generating  
5                   15.1 percent of the gross state product, and  
6                   directly adding nearly \$74 billion in value every  
7                   year.

8                   Nearly 660,000 Pennsylvanians are  
9                   directly employed in manufacturing. Pennsylvania  
10                  manufacturers sell almost 21 billion worth of  
11                  goods overseas representing 94 percent of all  
12                  Pennsylvania exports.

13                  Large manufacturers, including  
14                  pharmaceuticals and corporations, such as  
15                  Kennametal, are at the forefront and industry  
16                  leaders in the sectors we serve helping  
17                  manufacturers creating their products, and we are  
18                  the driving forces behind R&D.

19                  The Commonwealth's R&D tax credit is the  
20                  discussion of today, but the more important  
21                  question is how effective is it in assisting large  
22                  companies. The answer from Kennametal's  
23                  perspective is that it is an unreliable and  
24                  unpredictable tool, but a tool that would be  
25                  greatly valued if its full potential would be

1 realized. Keep in mind that we have to invest  
2 regardless, but then with the help from the state,  
3 we can be even more competitive in the global  
4 stage.

5 Since the inception of the R&D tax  
6 credit, it was promised that a 10 percent credit  
7 would be established. With revisions to the  
8 program, corporations such as Kennametal are  
9 waffling to take advantage of the program because  
10 we cannot use it as a definitive tool to increase  
11 our R&D efforts, but nevertheless, we still have  
12 to invest.

13 It is important for this committee to  
14 take the next step to make the necessary capital  
15 investment for the future of the Commonwealth to  
16 deliver on what was promised when the R&D tax  
17 credit was established, and that is to provide the  
18 definitive 10 percent of credit.

19 Currently Pennsylvania is ranked 42nd for  
20 economic competitiveness by the National Tax  
21 Foundation's corporate tax index last year.

22 Currently Pennsylvania's corporation net income  
23 tax of 9.99 percent is among the highest rate of  
24 its kind in the nation.

25 Further, the tax is calculated based on

1           70 percent of company sales, 15 percent of assets  
2           and 15 percent of payroll. This disadvantages,  
3           this discourages capital growth and hiring. Even  
4           worse, in out of state companies, such as one of  
5           Kennametal's principal competitors that sells in  
6           this Commonwealth, which we know is happening, but  
7           has no presence here, is advantaged over those who  
8           choose to locate in Pennsylvania.

9                     The R&D tax credit and corporate tax  
10           structure reform are intimately related. We need  
11           to do both. A major issue we are currently  
12           dealing with is the escalation of raw materials  
13           and energy. That means we have to invent  
14           manufacturing processes that will get us the  
15           finished products as much as possible with minimal  
16           secondary or posterior finishing process.

17                    The advent of these new near net shape  
18           technologies require us to invest heavily in new  
19           plant capability, and that's why in the last two  
20           years our capital investment, which is increasing  
21           the assets, have gone from the traditional, about  
22           \$30 million a year, to the last two years of  
23           \$80 million a year ago, and \$130 million this  
24           year. And the current corporate tax structure  
25           punishes us for doing the right thing, to stay

1 competitive in the global marketplace.

2 So, in summary, it is important to  
3 recognize the impact of the global economy on the  
4 Commonwealth. It is even more important that  
5 Pennsylvania is well positioned to remain  
6 competitive and support corporations with global  
7 footprints that remain rooted in Pennsylvania.

8 It is critical for the Pennsylvania  
9 legislature to recognize that every little bit  
10 helps. The expansion of the R&D tax credit for  
11 large corporations is a key for Pennsylvania  
12 companies to remain a driving force in R&D. And  
13 more importantly, it is a small step in helping to  
14 influence a business tax structure that has not  
15 been encouraging to business growth. Thank you.  
16 Thank you very much.

17 MR. BRIAN KENNEDY: We're going to hold  
18 questions until the end of the panel. So, our next  
19 testifier is Sean Rollman. Again, the Chief Financial  
20 Officer for Plextronics, and I think you're going to  
21 enjoy hearing about his company.

22 MR. SEAN ROLLMAN: Okay. Thanks, Brian.  
23 Thanks to the committee for giving me an opportunity  
24 to tell our story. Plextronics' story is certainly  
25 one of a much different spectrum than Kennametal.

1 We're only a few years old and have just grown to 50  
2 employees.

3 We were founded a few years ago off  
4 technology and a discovery at Carnegie Mellon  
5 University. We're an early stage company that  
6 develops and produces conductive inks for printed  
7 electronics. Our customers will take those inks  
8 and produce printed LED displays, LED lighting to  
9 replace incandescent and fluorescent light bulbs,  
10 and more significantly make printed solar cells  
11 that can be printed onto existing applications.

12 Our customers, such as Philips, Sony, GE,  
13 Sharp, Samsung, LG, they envision the world within  
14 18 months to maybe three years where you will go  
15 to a Best Buy and Circuit City, and you'll buy a  
16 television that isn't LCD or plasma. It's an LED  
17 television that can be rolled like an  
18 architectural drawing and thrown under your couch  
19 when you don't want to watch it or see it anymore.

20 We are working with the Department of  
21 Defense right now to develop flexible displays to  
22 deploy to over 300,000 soldiers by the end of 2009  
23 that will be on the sleeves of their uniform.

24 So imagine a quarterback in a football  
25 game where the soldiers will have a GPS map on

1           their displays and will move and need to carry 10  
2           to 15 pounds of devices for those maps.

3                         And we're also working with the  
4           Department of Energy to use our technology to make  
5           printed solar cells that will be deployed on the  
6           goggles or the helmets or on the shoulders of  
7           those uniforms that could power those devices.

8                         So our technology can take a very small  
9           amount of power and emit light, and it can take  
10          light to emit power. In a sense, that's the  
11          effect of what our conductive ink does.

12                        A few years down the road after that we  
13          envision solar cells where you would instead of go  
14          Best Buy and Circuit City and buy those lighting  
15          products that I've talked about you will go to  
16          Home Depot and Lowe's and buy roof shingles or  
17          windows that you can install in your home and  
18          remove the need to pay your utility bill to your  
19          First Energy or PPL or whomever your power company  
20          may be. So, we're working with large companies to  
21          develop that product.

22                        But the key is, as I mentioned, we're an  
23          early stage company still developing those  
24          products, and we've had success developing,  
25          generating some revenue and garnering some



1 investments from large companies and venture  
2 capitalists, but we're still a small growing  
3 company.

4 Today we're at 50 employees. We've grown  
5 five fold over the last three years from just nine  
6 a few years ago. We have benefited greatly from  
7 the R&D tax credit. Over the last four years  
8 we've spent over \$10 million in pure research and  
9 development cost, and that has so far earned us a  
10 little over \$500,000 of R&D tax credits. And  
11 we've been able to use that to deploy back into  
12 hiring our folks.

13 Two particular issues that Brian had  
14 mentioned that affect a company such as ours is  
15 the small business definition and the waiting time  
16 it takes to sell those credits. Up until 2006, we  
17 qualified for the small business definition, and  
18 we were able to get a 20 percent share of what we  
19 were eligible for, and which has greatly benefited  
20 us to be able to sell those credits to large  
21 profitable companies who wanted to use those  
22 credits, and then we could deploy that cash into  
23 new hiring.

24 In 2007, because our assets are now over  
25 \$5 million, we're now classified as a large

1 business effectively, so we are subject to the  
2 same disproportionate sharing as a company the  
3 size of Kennametal would be.

4 And our asset base is large not because  
5 we have yet turned a profit or because we're  
6 making billions in dollars of revenue, it's large  
7 because we were fortunate enough to find  
8 investors. And so, therefore, the cash from those  
9 investments we're using to hire employees and pay  
10 our people for this R&D gets us over that hurdle  
11 of \$5 million in assets.

12 So, we will, from Plextronics'  
13 perspective, the small business definition, we  
14 think is somewhat skewed a bit to a company such  
15 as ours in its early stage for those investments.

16 And also the waiting period, I can give  
17 you a real life example. Just two weeks ago we  
18 were able to secure the selling of our R&D tax  
19 credits that we earned back in 2005. We applied  
20 for those 2005 credits in September of 2006. They  
21 were approved by the state. We had to wait until  
22 December of '07 to be able to sell those credits,  
23 and we were able to find a buyer of those credits  
24 just a few weeks ago. And we sell that at a  
25 discount because there's an incentive obviously

1           for the buyer to use those credits and save money  
2           on their taxes.

3                       But it took us nearly 36 months after we  
4           had made the spending in R&D to be able to secure  
5           those R&D tax credits. So, again, from  
6           Plextronics' perspective, the small business  
7           definition and the waiting period to monitor those  
8           credits are the two things that affect companies  
9           like ours the most.

10                   MR. BRIAN KENNEDY: Thanks, Sean. Next we have  
11           Joseph Jacobson, who is the Chief Financial Officer of  
12           Akustica.

13                   Just before Joe starts, I've mentioned  
14           that there is a copy of the most recent report  
15           from the Department of Revenue on the R&D tax  
16           credit in all of the packets, and in the back of  
17           that you see who gets the credits and how much  
18           they are.

19                   MR. JOSEPH JACOBSON: First of all, I  
20           appreciate the opportunity to testify here today.  
21           Akustica is a similar situation with a very small  
22           start-up company, and we have benefited significantly  
23           from the R&D tax credit.

24                   But similar to the situation that you  
25           just heard, being a small company in the start-up

1 environment, we have a similar situation. Being  
2 that we just recently also got our R&D tax credit  
3 that we had sold, but again, that process started  
4 back in 2005. We benefited from that to the tune  
5 of about \$500,000, which was a significant benefit  
6 to the company at the time to put into more R&D  
7 type investment, to invest more in capital, but  
8 also to invest in hiring more people to grow our  
9 company.

10 So that money that we do get back goes  
11 directly back into the company itself, so it is a  
12 very beneficial type of arrangement. It's just  
13 the time it takes from once you've spent that  
14 initial R&D to actually receive the benefit. It's  
15 significantly long. And from the standpoint in  
16 terms of what we're doing in trying to grow the  
17 company, the quicker we can get that money, the  
18 better we can invest it.

19 Also, the same situation relative to our  
20 size, we are, by nature, in terms of the  
21 definition, a small business. However, we do go  
22 through several rounds of venture funding, so when  
23 that funding does come available, a similar  
24 situation, our cash goes up significantly. It  
25 doesn't mean that our sales go up significantly.

1           It just means that we're sitting on cash that we  
2 could use to further commercialize our product out  
3 to our customers and out to other types of  
4 suppliers.

5                       So from that standpoint I think in terms  
6 of really identifying what a small business is  
7 relative to whether it be revenue or the number of  
8 employees will be a much better indication of  
9 that.

10                      So let me tell you a little bit about  
11 Akustica. We were founded in 2001, headquartered  
12 here in Pittsburgh. What we produce is something  
13 quite revolutionary. It's a single-chip MEMS  
14 sensor that goes either in cell phones or laptops  
15 is its primary application.

16                      Currently we have 65 employees of which  
17 four are currently in Taiwan. Our major customer  
18 base is in the greater China area because these  
19 are where most of our cell phones and laptops come  
20 from.

21                      So in 2006 we turned our first revenue.  
22 We basically shipped roughly 200K units. We went  
23 up to 2.8 million this year and we're projected to  
24 even go up to 30 million in 2008.

25                      So to give you some sort of indication in

1 terms of what we are and what we do, if you look  
2 over to the left, that little dot there is the  
3 actual dye size that we produce. What that dye is  
4 is actually a microphone, okay.

5 And we then put that into packages which  
6 then go into like the laptop that you see there  
7 that allows communication through your laptop. So  
8 your laptop becomes a communication device. I  
9 don't know if you witnessed via the internet, you  
10 can do Skype and do phone calls over the internet.  
11 Well, this allows you to take that as a laptop and  
12 have digital quality sound via a phone  
13 conversation over your laptop.

14 So, what we're seeing is, in terms of  
15 everybody has one of these (indicating), has one  
16 of those (indicating) and numerous other devices,  
17 but to integrate it all into one device via the  
18 microphone is beneficial to both our customers and  
19 even the general public, okay.

20 Basically, we have engineers working on  
21 designing these products here in Pittsburgh.

22 We're actually just across the river here in the  
23 SouthSide Works, and those engineers are basically  
24 what drive most of our company right now.

25 We're predominantly engineering based,



1           Our first product, like I said, was digital  
2           microphone chips for laptops. We now are shipping  
3           in volume to Dell, Gateway, Fujitsu and other  
4           ODM's that produce these laptops within the  
5           marketplace. But right now Dell has incorporated  
6           our product into every single laptop that they're  
7           going to sell.

8                       Our next generation of product we're  
9           actually going to do an analogue version of this,  
10          which would be used within cell phones, you know,  
11          iPhones. Any type of communication device that  
12          would be used by our customer.

13                      So the whole MEMS revolution is really  
14          starting to explode. It was about a \$5 billion  
15          market in 2005 and expected to go to 12 billion in  
16          2010. So we believe based on us coming into the  
17          marketplace at this point there's a tremendous  
18          upside opportunity for us to commercialize this.

19                      Now, where we've changed the game in this  
20          relative to our competition is that we base the  
21          platform in terms of what these microphones and  
22          analogue chips are based on is on a standard CMOS  
23          platform.

24                      What that means is that's kind of the  
25          vanilla approach that is used to develop



1           semiconductors around the world. It's been highly  
2           commercialized, therefore, you can get it at a  
3           relatively low cost. From that we put the MEMS  
4           top on it, package it and send it out.

5                       We actually own no manufacturing. It is  
6           all outsourced. So we're using places in Texas,  
7           China, Taiwan and so forth to produce our parts.

8                       This actual experience in pioneering all  
9           of this was the work of Ken Gabriel, who is our  
10          chairman and CTO of our company. He started at  
11          MIT and was last at CMU. So, him and Jim Rock are  
12          the ones who started the company, and Jim is on  
13          the Technology Council.

14                      So, again, because of our ability that we  
15          don't own any manufacturing facilities gives us a  
16          lot more flexibility and also give us the ability  
17          to identify certain type of suppliers that we can  
18          pick and choose in order to get the best cost  
19          available because it is a competitive marketplace  
20          with a semiconductor industry.

21                      So we're not tied down to our own  
22          capacity, so that gives us a lot of flexibility,  
23          able to turn products quickly, and of not having  
24          to have that huge capital investment that is  
25          required.

1                   So, again, our strategy is basically  
2                   trying to commercialize in terms of what that  
3                   CMOS, MEMS products are, leverage of that platform  
4                   to do more designs of low cost innovative  
5                   products. And, again, we're continuing to recoup  
6                   and retain talent within the Pittsburgh area.

7                   Myself, I was recruited out of Phoenix,  
8                   out of a large semiconductor company, and just  
9                   relocated to Pittsburgh here January 1st. So it's  
10                  kind of -- it's a good day because the sun's out  
11                  for me so. But, again, that's going on in terms  
12                  of trying to find that talent to bring to the  
13                  company, as well as looking at the local  
14                  university, engineers and so forth.

15                  So predominantly the people that are part  
16                  of our company do come from the Pittsburgh area,  
17                  but we are recruiting from outside so. It just  
18                  tells a little bit in terms of our supply chain,  
19                  like I said, we are completely outsourced, so we  
20                  use foundries in Germany, in Texas. We use other  
21                  companies in Japan and Canada. So, our parts do  
22                  get a lot of air miles on them in terms of the  
23                  process that they go through in order to be  
24                  produced, but everything is coordinated and done  
25                  here out of Pittsburgh.

1                   But, again, as we continue to grow -- and  
2                   we already have a presence in Taiwan, and just  
3                   because most of our customers are basically in  
4                   China, again, that's where these end products are  
5                   produced, we are looking at expanding our presence  
6                   internationally. But the heart and soul in terms  
7                   of where the technology comes comes completely out  
8                   of Pittsburgh.

9                   Again, that's kind of a little basis in  
10                  terms of what our company is. Again, we are in a  
11                  start-up mode in the standpoint that, honestly, we  
12                  haven't turned a profit. We're still in an  
13                  operating loss situation. We spend roughly about  
14                  \$10 million from an operating expense standpoint,  
15                  which about 50 percent of that is salaries alone  
16                  in terms of engineers we have working here in  
17                  Pittsburgh.

18                 The remaining part of that for the most  
19                 part is based on technology and new development  
20                 that we're doing to move to the next platform to  
21                 make us more competitive in the marketplace. But,  
22                 roughly about 20 percent is all the overhead that  
23                 goes with that in terms of all the lawyers and the  
24                 office supplies, to rent and everything else that  
25                 we pay that goes directly to global economy.

1           So, again, like I said, from a tax credit  
2 standpoint, our biggest issues that we have from a  
3 small company is again the time frame involved,  
4 especially to sell those credits to when you  
5 actually receive the dollars into the company.

6           And the designation of a small business in terms  
7 of its net asset value, which again, like I said,  
8 based on our next round of investing, if we were  
9 to cut off that level right now, we would qualify  
10 as a small business. So, thank you.

11           MR. BRIAN KENNEDY: Thank you, Joe. Next I'm  
12 really pleased to introduce you to Larry Sweeney, who  
13 is one of the founders of Vocollect, and if you're  
14 heading back to the turnpike today you can actually  
15 see Vocollect's headquarters located right off to the  
16 left, between Squirrel Hill and what, the Forest Hills  
17 exit?

18           MR. LARRY SWEENEY: Right at the Rodi Road  
19 exit. It's up on the left.

20           MR. BRIAN KENNEDY: You'll see there, they have  
21 a great facility. They're growing. And we're very  
22 pleased to have Larry with us here this morning.

23           MR. LARRY SWEENEY: Thanks, Brian. Thank you  
24 everybody, this morning. First, I have to apologize.  
25 I got thrown into this at the last minute. I hopped

1 off a plane, the early hours of Monday morning from  
2 Korea, and they told me yesterday I needed to do this.

3 Do what? So, I apologize if I'm not 100 percent  
4 prepared. But a little bit about Vocollect, who are  
5 we and where are we from.

6 Well, a little over 20 years, three guys  
7 left Westinghouse and had an interest, had an  
8 idea, and had brown hair, actually (indicating).  
9 I can relate a lot to the stories of Akustica and  
10 Plextronics. Certainly we've been there. We  
11 started in a machine shop, in an office above a  
12 machine shop in North Versailles.

13 Today Vocollect, we cracked a \$100  
14 million market revenue in 2006. We have over 400  
15 employees worldwide, about 40 in Europe, about 40  
16 outside of Pittsburgh, in the United States. We  
17 have about eight in Japan, and the rest are all  
18 right here in Pittsburgh.

19 What do we do probably you're asking?  
20 Well, you've all been in the grocery store late at  
21 night, Sears, Lowe's, whatever. You see people  
22 walking around with a hand-held terminal, has a  
23 little screen on it, a little keyboard.

24 What Vocollect does is something similar  
25 to that, but it's a wearable computer, no screen



1 and they've been growing this way -- will come  
2 more from outside the United States than inside  
3 the United States. We're growing globally.

4 What are our challenges? Well, our  
5 challenges are we need to stay ahead. We own  
6 about 80 percent of the market that we're in,  
7 which is really unusual, but we're in a great  
8 spot.

9 And how do we stay there? Well, we stay  
10 there because we innovate. We spend a lot of  
11 money on research and development. As an example,  
12 2006, we just got over \$100 million market in  
13 revenue. We spent \$20 million in R&D.  
14 Twenty percent, that's a huge amount for a company  
15 like Vocollect, but that's how we do it.

16 We know we're products driven. We know  
17 we need to stay ahead of the competition. There's  
18 new competition that comes out of Germany, France,  
19 Italy, probably Japan shortly. So, we're always  
20 looking to stay ahead globally against this  
21 competition.

22 Now, we targeted the supply chain, okay,  
23 in the distribution end and warehousing. We're  
24 working down that chain into the retail stores.  
25 We have retail applications. We're working back

1 up that supply chain to manufacturing.

2 That's great. We're growing globally,  
3 but what else do we do? Well, about two years ago  
4 we started Vocollect Healthcare Systems taking the  
5 same idea of voice and applying it to healthcare.

6 Where did we start? Well, we chose to  
7 start in the long-term healthcare facilities  
8 directing the work of nurse's aides in these  
9 facilities. Mr. Jones needs to be turned every  
10 two hours, he needs his meds in an hour. He needs  
11 to have his vitals taken.

12 All of this is tracked and driven by  
13 voice. The eventual goal and vision here is every  
14 nurse will have a voice system associated with  
15 them to direct their work because, guess what?  
16 The nurse patient ratio keeps going the wrong way,  
17 and they need a lot of help to be able to maintain  
18 that level of care.

19 So when you think about it voice can be  
20 applied in a lot of different areas, right? We  
21 chose distribution as our starting point. We're  
22 now branching into healthcare, but everybody  
23 sitting here can think of, wow, there's about nine  
24 different areas where I think I can apply  
25 something like voice to make people more





1 Mr. Chairman. I must say this is very informative,  
2 each one of you, when Brian says it will be really  
3 interesting. I'm into electronics and all this stuff  
4 that you're talking about, so I mean it's like, wow,  
5 it gets you feeling good inside when you start talking  
6 about all this stuff that you're planning, especially  
7 with no more LCD's. I just bought one of those at  
8 Christmas. So, now you're telling me I should have  
9 waited a couple of years, Sean.

10 But, no, I mean, it is amazing, and I  
11 don't think a lot of people realize what's being  
12 done here at the center, in our region when it  
13 comes to this. And this is just so important that  
14 all of you grow and keep growing, because  
15 technology keeps changing, as we all know. And  
16 that's really just more of a comment than  
17 anything.

18 And I've been informed here just  
19 listening to what you've done and just keep  
20 getting the word out in the community because it's  
21 important that people understand what you're doing  
22 because a lot of times people don't realize what's  
23 being done right here in Pittsburgh. So, thank  
24 you, Mr. Chairman.

25 REPRESENTATIVE DAVID KEVDANSKY: Thank you.

1 Representative Frankel.

2 REPRESENTATIVE DAN FRANKEL: Thanks. Good  
3 morning. I want to get maybe your perspective, and I  
4 know we're here to talk about the R&D tax credits, but  
5 obviously we have in front of us proposals for a whole  
6 spectrum of business, of tax cuts to change the  
7 environment, and a very difficult environment for us  
8 right now, as Pennsylvania probably is headed in the  
9 direction of many of the other states across the  
10 country that are experiencing significant revenue  
11 shortfalls, below the projections.

12 So we don't have the opportunity, really,  
13 to probably enact the full vision, I think, of a  
14 tax policy to make us more competitive in the end.

15 Where do you put -- and it's interesting  
16 because we have, really, three different levels of  
17 maturity in terms of companies here, to very young  
18 companies, one extremely mature, but innovative  
19 company, one that's currently middle range here in  
20 terms of growth.

21 We're looking at, obviously, phasing out  
22 capital stock, the franchise tax, reducing  
23 corporate net income tax. We're looking at  
24 lifting the cap on net operating loss, carry  
25 forward, and R&D tax credit, among the kind of

1 portfolio. We have to prioritize, obviously. I  
2 have to think this is a very good place to start,  
3 but where do you see this tax heading in that  
4 portfolio? Understanding you'd want to see the  
5 whole thing, I'm sure, in terms of your individual  
6 companies, I can make some assumptions. I would  
7 think that Plextronics and Akustica probably would  
8 find this one to be the most useful one.

9 But we have to make some choices in  
10 allocating the credits and the amount of money we  
11 have to budget for this. Maybe you can give us  
12 your prospective of where you see this in terms of  
13 the priority in terms of tax policy and what we're  
14 considering.

15 MR. LARRY SWEENEY: I guess speaking as a  
16 Pennsylvanian, I'd love to see it go into the -- and  
17 not speaking Vocollect, but speaking as  
18 Pennsylvanian -- I'd love to see it go into the  
19 research tax credits. I mean that's where we get  
20 companies off the ground. That is the hardest hurdle  
21 to get over.

22 And if it wasn't for the Ben Franklin  
23 money that we received in the early years, we  
24 wouldn't be here today. I'll be quite frank.  
25 That was instrumental in Vocollect getting to the

1 point where not where we were self-sufficient, but  
2 it got us to the point where we could raise the  
3 revenue, raise some capital. So, tax credits are  
4 huge in those early years getting over those early  
5 hurdles.

6 MR. JOSEPH JACOBSON: Yeah, I'm going to agree  
7 from our standpoint in terms of most of the dollars  
8 that went into our company are developing next  
9 generation product. Again, with our introduction of  
10 the microphone out into the marketplace, the  
11 competition was much larger, much stronger, is  
12 currently on our tail, driving to find, make something  
13 very similar to what we have. They have the benefit  
14 associated with a much better distribution system,  
15 additional working capital, so forth. So, they can  
16 compete on a price much better than we can.

17 So for our long-term longevity, from a  
18 company prospective, we really depend upon what we  
19 put into R&D. And, you know, we talked about in  
20 terms of what we're doing, as far as shrinking  
21 that microphone down smaller and smaller, but  
22 there also are several other applications besides  
23 this that we are working on relative to sensors  
24 and so forth that lend itself to this technology  
25 that would also be revolutionary.

1                   So I see from our standpoint, over the  
2                   next five years, to spend a tremendous amount of  
3                   additional R&D. And where that really comes from  
4                   is again a lot of our processes are outsourced.  
5                   That R&D spend will go into people. Hiring  
6                   engineers and to bringing people in if not from  
7                   outside Pittsburgh, from inside Pittsburgh.

8                   So, from any sort of advantage we get  
9                   from this R&D tax credit, honestly, that goes  
10                  right into payroll.

11                  MR. SEAN ROLLMAN: You're correct,  
12                  Representative. For a company like Plextronics, the  
13                  R&D tax credit certainly benefits most directly to a  
14                  company like us. We do encourage capital stock tax  
15                  now. In fact, a significant amount for a company like  
16                  ours because we are in the early stage.

17                  And I would also echo Larry's comments,  
18                  the money that comes from any kind of economic  
19                  development activity is critical for companies  
20                  like us or in ours two or three years ago. And  
21                  our story is exactly true. Innovation Works was a  
22                  critical funder of Plextronics, and I know we  
23                  would not for a fact be here today if it weren't  
24                  for that funding a few years ago.

25                  So, any kind of economic development

1 initiative can benefit those companies getting off  
2 the ground.

3 DR. WILLIAM HSU: From a more mature  
4 corporation, bigger corporation like PPG and  
5 Kennametals, and our prospective has to be a more  
6 balanced approach. Ultimately, the acid test is to  
7 whether you make enough money to pay tax to begin  
8 with, right? You know, you can give all the credits  
9 to all the start-ups, which are very good. Eventually  
10 20 years or later, when you plant a tree, like later  
11 the tree will bear fruit and give you shade and all  
12 that, but until you get to a point that they can  
13 really contribute, you have to wonder, do you continue  
14 to support those for the credits at an expense of the  
15 bigger corporation? Because, ultimately, you ended up  
16 killing the Golden Goose, right?

17 And the example I just cited, we know the  
18 reality is that we have to continue to invest  
19 because we cannot play the commodity game. If  
20 we're going to play a price game against our  
21 competition we would have folded shops long ago.  
22 We cannot against the low-cost countries.

23 And the only reason we are surviving and  
24 we are thriving is because of the value adding  
25 contributions in terms of products. We can't help

1           our customers to improve their competitiveness,  
2           and that's the win/win situation. It is so  
3           important that we come up with all of these near  
4           net shape technologies that we can actually lower  
5           our manufacturing cost more than we actually  
6           lowered the price.

7                        So, it would be a win/win because we can  
8           then sell the same products with better  
9           performance to our customers.

10                      In the meantime, my margin does not erode  
11           so that actually forces into all these capital  
12           investments, right? And all of these things that  
13           we talk about, if you don't make those kind of tax  
14           reforms, we end up basically taxed twice. You tax  
15           us on the revenue and then we improve our  
16           competitiveness, we improve our asset base, you  
17           tax us again, you know?

18                      So, it's kind of a very difficult  
19           situation. So from the big corporation point of  
20           view, even though you said you have to make some  
21           priorities, my encouragement is to at least with  
22           those two points of view, that the credit and the  
23           overall tax restructure, I think you need to  
24           address them both in a fair-handed manner.

25           Otherwise, the big corporation will suffer, I will



1 tell you that.

2 You know, our competitors, like this  
3 company that we're dealing with in Israel, how  
4 much of a government subsidy did they get? I  
5 mean, you just cannot even begin to imagine. That  
6 is the battle we are dealing with.

7 MR. BRIAN KENNEDY: I just had a couple of  
8 quick thoughts. I'll be very quick about it.

9 From the Pittsburgh Technology Council's  
10 point of view what we would like the General  
11 Assembly to focus on is in terms of prioritization  
12 are those tax policies that either hurt our  
13 competitiveness or could improve our  
14 competitiveness as it relates to attracting and  
15 retaining manufacturing and technology companies.

16 So, in some regards, everyone is paying  
17 the second highest corporate in income tax rate in  
18 Pennsylvania, and I'd love to come before you and  
19 tell you that that's something that we need to fix  
20 this year, but we recognize that lowering the rate  
21 is a very expensive proposition.

22 So from a prioritization point of view  
23 what we've done is targeted a very narrow agenda,  
24 to say listen, you know, what you should be  
25 focusing on with your limited resources is on

1 removing some of the competitive things that hurt  
2 manufacturers and in putting some in that help  
3 them.

4 Single sales factor, for example, rewards  
5 companies that are manufacturing products here in  
6 Pennsylvania, but selling them into the global  
7 marketplace. The fiscal note on that is  
8 relatively small in the grander scheme of things.

9 The net operating loss is something --  
10 there's only one other state in the country that  
11 limits NOL's, and it's just bad for manufacturing.  
12 It's bad for start-up companies, so we've targeted  
13 the single sales and the NOL, and then last, we've  
14 talked about the research and development tax for  
15 this being one of those that we can improve.

16 So we really have as a trade association  
17 and I think as a business community come forth  
18 with a prioritized approach, with the priority  
19 being on those companies that are at the top of  
20 the food chain that are employing other  
21 Pennsylvanians and that are supporting the local  
22 governments, the county governments and state  
23 governments, your tax revenues. And that's really  
24 today, it's your manufacturing and your technology  
25 economy.

1                   REPRESENTATIVE DAN FRANKEL: Thank you.

2                   REPRESENTATIVE DAVID KEVDANSKY: Representative  
3 Kortz.

4                   REPRESENTATIVE WILLIAM C. KORTZ: Thank you,  
5 Mr. Chairman, and thank all of you for the information  
6 today. I have a couple of questions.

7                   First off, all of you said you like the  
8 tax credit, you want it to go forward, and you  
9 would like the bill, you'd like it being improved.

10                  The question I have is some of you have  
11 said that you want to sell these off.

12                  Why not use them all, carry them forward  
13 and use them? Larry, start with you. Why  
14 wouldn't you want to use it all up?

15                  MR. LARRY SWEENEY: I think we do.

16                  REPRESENTATIVE WILLIAM C. KORTZ: You do. But  
17 I heard some people say they sold them.

18                  MR. SEAN ROLLMAN: We monetize them. It's  
19 really just a financial association of time value of  
20 money. We foresee profits within the next two to  
21 three years, but depending on the NOL caps and  
22 limitations that that imposes, rather than realizing  
23 100 percent of that credit two or three years from  
24 now, I'd rather get 90 cents on the dollar today and  
25 use that cash to hire people rather than waiting a few

1 years.

2 So for a company like an early stage  
3 company that's the reason why we would make that  
4 financial decision.

5 DR. WILLIAM HSU: We use it.

6 REPRESENTATIVE WILLIAM C. KORTZ: You use it?

7 DR. WILLIAM HSU: We use it completely. We  
8 don't monetize it.

9 REPRESENTATIVE WILLIAM C. KORTZ: The next  
10 question I have -- and maybe it's a little bit off  
11 base -- but your competitors reengineering the  
12 products, obviously you've got to stay one step ahead.

13 MR. LARRY SWEENEY: Yes.

14 REPRESENTATIVE WILLIAM KORTZ: I would suspect  
15 it's mostly off-shore competitors, take your product  
16 and figure out how those things work, and then try to  
17 really jam into your market.

18 Will this tax credit help you to stay one  
19 step ahead?

20 MR. JOSEPH JACOBSON: Most definitely. I mean,  
21 it's, again, it's cored directly into, like I said,  
22 from a people standpoint, designing that next  
23 generation product. Interestingly enough, I mean our  
24 greatest competitor actually is a U.S. company. Now,  
25 we have patents that protect our technology of what

1 we've done.

2 REPRESENTATIVE WILLIAM KORTZ: All they have to  
3 do is change it a hair, right?

4 MR. JOSEPH JACOBSON: Exactly. I mean,  
5 right --

6 REPRESENTATIVE WILLIAM C. KORTZ: Make it blue  
7 instead of red.

8 MR. JOSEPH JACOBSON: Right. It's a little,  
9 you know, slight modification can mean that they can  
10 come into the market standpoint. But definitely, I  
11 mean, it is going into that next generation. We are  
12 already looking in terms of how products we would then  
13 take to market two years out at this point.

14 REPRESENTATIVE WILLIAM KORTZ: Okay, thank you.

15 REPRESENTATIVE DAVID KEVDANSKY: Representative  
16 Tim Seip?

17 REPRESENTATIVE TIM SEIP: Thank you,  
18 Mr. Chairman. I want to thank all of you gentlemen  
19 for your testimony. It's very enlightening. And Joe,  
20 I'm very encouraged and find it very refreshing that  
21 we're actually exporting technology to China. Thank  
22 you.

23 MR. JOSEPH JACOBSON: Yes, we are.

24 REPRESENTATIVE TIM SEIP: That's wonderful to  
25 hear. Getting back to I think Brian had said that

1 we're looking at a really two-fold approach here. You  
2 want to try to make products that are innovative and  
3 good to sell and market, but at the same time we want  
4 to make them more efficiently.

5 And in my legislative district we have a  
6 landfill right now pumping methane gas down to a  
7 textile mill. Maybe one of those industries that  
8 we talked about is getting priced out of the  
9 market, but they're able to save \$2 million on  
10 their oil bill by hooking up this methane gas.

11 And I think we're trying to address some  
12 of your concerns from that side of the house with  
13 our energy package and doing things like that to  
14 help you reduce your costs.

15 So, I don't really have any questions. I  
16 just wanted to throw that comment out. Thank you,  
17 Mr. Chairman.

18 REPRESENTATIVE DAVID KEVDANSKY: Thank you.  
19 Representative Metcalfe?

20 REPRESENTATIVE CHRIS SAINATO: Go ahead, Daryl.

21 REPRESENTATIVE DAVID KEVDANSKY: Representative  
22 Sainato.

23 REPRESENTATIVE CHRIS SAINATO: Just yesterday,  
24 I thought it was very interesting at our hearing  
25 yesterday, and I would just like to know what effect

1           it has on you on work force development. Are you  
2           finding any problems with your employees as far as  
3           finding people to work in your industry?

4                        I mean, they said yesterday 35 percent of  
5           high school seniors are dropping out or people are  
6           dropping out before they graduated, and they were  
7           having problems with people in just the skills of  
8           showing up on time for work, behaving themselves at  
9           work, and doing things. Are you experiencing  
10          that?

11                      MR. LARRY SWEENEY: It's one of our greatest  
12          challenges finding people to fill the void, fill the  
13          holes as we grow. Each quarter our CFO gets up in  
14          front of the company and shows the numbers and the  
15          trends. It's revenue and it's bookings and it's  
16          profits, and it's all this thing, and it's head count.  
17          And that's the one thing we're always behind on. It's  
18          a very difficult market, at least in Pittsburgh, to  
19          find good people, professional people.

20                      DR. WILLIAM HSU: Yes, we have the same  
21          problem. And we could get people, but typically it  
22          takes a long time. And we have to do a national  
23          search. And imagine with all the universities here.  
24          You say, well, it shouldn't be that much of a  
25          difficulty, but we have problems.

1                   And when you come to wage row people, the  
2                   work ethics, a lot of the time, I don't know what  
3                   it is, but it just seems the people, the younger  
4                   people have an entitlement kind of a mind set,  
5                   which is just not going to work in the long-run  
6                   because they're very hungry people oversea. They  
7                   would very much like to have the manufacturing  
8                   plant.

9                   So, yeah, we do have those development  
10                  issues.

11                  MR. SEAN ROLLMAN: Because of how small we are  
12                  we're somewhat immune to that problem so far. Also,  
13                  because of the national demographics of our employees,  
14                  we've brought in of our 15 employees, nearly  
15                  40 percent of them are from outside of the region,  
16                  another third of them are not American-borne citizens.  
17                  So, we've had success in bringing those employees to  
18                  here.

19                  Also, 25 of our 51 employees are Ph.D.'s  
20                  so the demographics of our particular company, I  
21                  think, has not encountered those problems yet, but  
22                  I'm sure hopefully when we have several hundred  
23                  employees some day we probably will have  
24                  encountered the same problems.

25                  REPRESENTATIVE CHRIS SAINATO: That was just



1 something I think that was a little surprising to many  
2 of us yesterday when you're telling us just the  
3 problems. And even in your lower end employees, okay,  
4 just not having the work ethic, not showing up on  
5 time, getting into trouble, either with drugs or other  
6 legal problems outside of the work, and it's like, you  
7 know...

8 DR. WILLIAM HSU: Take, for example, Germany.  
9 They have a very structured apprenticeship program.  
10 So people who don't want to go to universities, they  
11 have other choices to give them the vocational skills.  
12 And typically they would -- actually not only they  
13 would go to classes, they would actually be assigned  
14 to different companies and take classes during a  
15 certain period of time, and then actually the rest of  
16 the time actually hand-on. And after they graduated  
17 typically where they actually go to work would employ  
18 them. But we don't see anything like this in this  
19 country. We just don't see it.

20 MR. BRIAN KENNEDY: I just had a quick, quick  
21 point onto that is as a Trade Association for  
22 companies, I'd like to tell you the No. 1 challenge  
23 facing them is the research and development tax  
24 credit, except that would be a small challenge, one  
25 this committee could address.

1                   But the No. 1 issue we hear constantly --  
2                   and we poll companies and we bring them together.  
3                   It's all people, it's all talent. So, we're more  
4                   in the business of selling memberships in some  
5                   regards, and we sell memberships, it's our Career  
6                   Center, access to our Career Center is one of our  
7                   strongest selling points. People, probably 50,000  
8                   people a month come to our website looking for a  
9                   job.

10                   Last year we posted 6,000 technology jobs  
11                   on our Career Center. Today, I think we're over  
12                   1,500 current jobs posted on that job site.  
13                   People are hiring. They're hiring  
14                   family-sustaining jobs. They have to, though,  
15                   very often pull talent in from around the country  
16                   and around the world to build these highly  
17                   technical positions.

18                   And on that front, there's a lot of work  
19                   really that needs to be done here in Pennsylvania.  
20                   We, one, would like to get the word out that there  
21                   are jobs here in Pittsburgh, but there are folks  
22                   who have left Pittsburgh and gone away, gotten  
23                   some great experience, we want them to come home.  
24                   Immigrants, we want them to consider locating here  
25                   in Pittsburgh.

1                   And we think that, really, the technology  
2                   community can help stem the loss of jobs because  
3                   some of you may have seen last week, the Post  
4                   Gazette ran a report that said that the region  
5                   lost I think another 6,000 people. Allegheny  
6                   County lost 6,000 people in population.

7                   We had one of our internal research staff  
8                   members pull data on the IRS, and we actually  
9                   identified a net loss of I believe the number of  
10                  \$225 million of wages from those folks.

11                  So, when we lose people we're losing  
12                  economic activity, we're losing the future of our  
13                  technology companies. We need to really work to  
14                  get the message out that there are positions here  
15                  in Pittsburgh; that there's 6,000 alone that we  
16                  filled last year on our Career Center.

17                  But they're the types of positions that  
18                  are high-skilled positions. Our companies don't  
19                  have much of a problem of people not showing up to  
20                  work. There is much more problem they have  
21                  finding the highly-skilled talent they need.

22                  Behavior, I think, probably the tech  
23                  council is probably one of those misbehaved  
24                  employees, but certainly there are jobs here, and  
25                  it is a big challenge. And what you're doing to

1 help create a future pipeline of workers on the  
2 other legislation, you're talking about something  
3 that the council could wholeheartedly support  
4 because it does speak to the need to create a  
5 future pipeline of workers in the region.

6 REPRESENTATIVE CHRIS SAINATO: Thank you,  
7 Mr. Chairman.

8 REPRESENTATIVE DAVID KEVDANSKY: Thank you.  
9 Representative Metcalfe.

10 REPRESENTATIVE DARYL METCALFE: Thank you, Mr.  
11 Chairman, and thank you all for your testimony today.  
12 It's exciting to hear the technology that we're on the  
13 cutting edge of, and it's good to hear American  
14 innovation is still keeping us ahead in the world,  
15 even when there's so many cut labor costs out there  
16 around the world and the hunger that Dr. Bill  
17 mentioned that's out there around the world.

18 I think that our culture has to  
19 understand that we've got the most prosperous and  
20 greatest nation in the world, and I think you kind  
21 of get fat and happy sometimes when you're in the  
22 situation for a long extended period of time, and  
23 I think that's what our culture's experiencing.

24 So, I think we need that hunger back, and  
25 especially in our youth to understand you have to

1 go after it if you're going to be successful.

2 But I appreciate all of the testimony  
3 you've given. It's just exciting products. My  
4 background coming right out of high school was  
5 military and my foundational training in the U.S.  
6 Army working on radar and IFF to tell if you're  
7 friendly or enemy aircraft from a vacuum tube  
8 technology, transistor technology.

9 So, hearing about the ink, the conductive  
10 ink and the microphones that size and just as a  
11 former soldier understanding the capability that  
12 we would have on the military battlefield with  
13 that technology at our disposal to keep our  
14 military leading as we always have with technology  
15 on their side and saving lives through it is  
16 exciting.

17 But as far as our tax structure and my  
18 service in the legislature, I would agree with  
19 Dr. Bill's approach that we have to have the all  
20 encompassing tax structure reform to help all of  
21 you, both in your early stages of development and  
22 as you become successful and create more product  
23 and create more profits. We have to bring the CNI  
24 rate down, we have to finish the capital stock of  
25 franchise tax elimination, the net loss issue and

1 single sales factor. We have to address those  
2 issues.

3 And I'm all for the tax credits and  
4 making sure that we're able to do that also, but I  
5 think ultimately businesses will flourish when  
6 they have a lower tax burden to deal with and a  
7 lower regulatory burden to deal with so that they  
8 can do what you all do best, and that's create  
9 jobs and innovate.

10 So, thank you all for the work that  
11 you're doing, and I'm excited to follow the  
12 success of your companies in the future. And  
13 whatever we can do to help out of my office feel  
14 free to contact me any time.

15 Thank you, Brian. I enjoyed your  
16 testimony also. Thank you, Mr. Chairman.

17 REPRESENTATIVE DAVID KEVDANSKY: Thank you,  
18 Representative Metcalfe. Just a follow-up from  
19 Representative Seip.

20 REPRESENTATIVE TIM SEIP: If I could just  
21 quickly, talking about staff and kind of going back to  
22 what Represent Sainato was saying, are you finding  
23 bigger challenges with those basic skills? I don't  
24 know, dealing with coworkers, showing up on time and  
25 those kind of things? Or is it bigger challenges with

1 identifying the people that have technological  
2 capabilities that your industry needs?

3 Because, I mean, in my mind, if I think  
4 of somebody graduating from a top notch school,  
5 the University of Pittsburgh, Duquesne, Carnegie  
6 Mellon, I'm not envisioning somebody who has  
7 trouble getting up in the morning and getting to  
8 work. Maybe I'm missing something there.

9 And if I could ask Joe, you said you were  
10 from Arizona. I'm just curious, what made you  
11 say, hey, I'm going to go to Pennsylvania and work  
12 there. That's my question.

13 REPRESENTATIVE DAVID KEVDANSKY: That's my  
14 question.

15 MR. JOSEPH JACOBSON: A lot of people have  
16 asked me that question. A lot of people in Phoenix  
17 asked me that question when I was getting ready to get  
18 on the plane.

19 It was really the company and the  
20 opportunity. I came from a much larger  
21 corporation in the Phoenix area. It was in the  
22 semiconductor industry, and the thought of coming  
23 here, building something from scratch, getting  
24 involved in several different activities that you  
25 wouldn't necessarily in a large corporation, and

1 the people here.

2 I have to say, I mean, I was a little bit  
3 hesitant coming here, to be honest, to make that  
4 move. But since I've been here, I mean, when I  
5 moved into my neighborhood, I think every neighbor  
6 came over and brought me something to eat, which  
7 would never happen in Arizona. I didn't even talk  
8 to my neighbors in Arizona. You know, I basically  
9 waved to them when you'd go in and out of your  
10 garage.

11 But the people here are amazing. And,  
12 you know, to your comment about, I mean, we have  
13 some lower skilled positions within our company,  
14 and we have not had issues that you're addressing.

15 They show up on time. They're willing to  
16 work late. We're actually having some parts that  
17 we're trying to get out now that we're actually  
18 testing here in Pittsburgh, and we have 24/7  
19 testing going on in our facility. Not a problem  
20 working nights and everything else.

21 But, again, on the higher technical  
22 aspect in terms of some of our job requirements,  
23 yeah, we do run into an issue. And by the nature  
24 of our industry, most of those individuals are  
25 located, you know, in the Phoenix, California,



1 Texas area. That's where that technology is, so  
2 we do recruit out of those areas.

3 But we also have recruited directly out  
4 of the universities here, too, so it's kind of a  
5 mix.

6 But, no, I think Pittsburgh's wonderful.  
7 I think I'm enjoying it much more, other than the  
8 weather, which I'm getting used to. But the  
9 people here are great.

10 REPRESENTATIVE DAVID KEVDANSKY: Thank you. I  
11 just want to follow up on a couple of things. One is  
12 this issue of the definition of small businesses. You  
13 all say that defining it is less than 5 million in net  
14 assets really isn't the best way to go to enable the  
15 small businesses like yours and others to fully  
16 utilize the set aside that we have.

17 If not defining it as assets, any other  
18 suggestions or any thoughts on a more appropriate  
19 definition for utilization of the tax credit?

20 MR. SEAN ROLLMAN: Speaking selfishly from a  
21 Plextronics perspective, I think revenues may  
22 potentially be a better measure of size than assets.  
23 Assets, as I mentioned before, can somewhat be skewed  
24 because of the timing of an investment round. And the  
25 dollars, when we bring in investment dollars, they are

1 already targeted for hiring and growth over the next  
2 several years until we get to profitability. So the  
3 fact that at a particular point in time that cash  
4 is sitting there as an asset, and it hurts that  
5 definition.

6 Revenues, I think, are a true reflection  
7 of a company's success and growth of their  
8 business. And it's certainly our goal to continue  
9 increasing revenues. We don't want to fit any  
10 kind of small business definition for too long,  
11 but at our stage today assets hurts a company like  
12 ours.

13 REPRESENTATIVE DAVID KEVDANSKY: If we use  
14 revenue, any idea what level, roughly?

15 MR. SEAN ROLLMAN: Well, each industry I think  
16 would be different. We eclipsed \$2 million of  
17 revenues last year, but the vast majority of it is  
18 from government agency contracts funding our research,  
19 like I mentioned earlier.

20 I wouldn't even venture a guess. I'm  
21 sure there's some data out there that would  
22 pinpoint. If you looked at a population of all  
23 entities in Pennsylvania that have applied for R&D  
24 credits, there must be some data point that shows  
25 what our revenue number would be.

1           MR. BRIAN KENNEDY: I'll just say, the federal  
2           government actually defines small businesses by the  
3           number of employees, and I think they also look at  
4           gross revenue. It's kind of a hybrid approach. I  
5           think the SBR program -- Carla, you're here to help me  
6           out -- I think they say less than 500 employees and  
7           less than a \$100 million in revenue. I'm not  
8           positive.

9           MS. KARLA BECKNER WHITE: I'm not sure about  
10          the revenue. It's definitely bigger than 500  
11          employees.

12          MR. BRIAN KENNEDY: But here's what we would  
13          suggest, is to work with the Department of Revenue so  
14          this is what we'd like to see happen.

15                 First, we would like to see the \$8  
16          million that's set aside for small businesses be  
17          fully utilized.

18                 So, we would say, listen, let's work with  
19          the Department of Revenue, the Department of  
20          Community and Economic Development to run some  
21          models to see what type of definition would allow  
22          us to use that.

23                 And if this legislation passes and we  
24          increase it to 15 million, we would like to use  
25          that 15 million, too. And let's make sure that we

1 create a definition that allows us to use 100  
2 percent of the 15 million.

3 I can assure you that any definition that  
4 you generate is not going to be one that was just  
5 made up so that you could use 15 million. They're  
6 going to be small businesses. You're going to be  
7 creating a definition of somebody that has fewer  
8 than a certain number of employees and a certain  
9 amount of revenue.

10 But right now we're not using the set  
11 aside program, and as a result you're not fueling  
12 growth in small businesses. And so that's really  
13 what our goal is is just to make sure we have a  
14 set aside provision, that we have a definition of  
15 small businesses that allows that set aside to be  
16 utilized and allows that money to be put on the  
17 street the way we intended it to be.

18 REPRESENTATIVE DAVID KEVDANSKY: Okay. I can  
19 understand and will support in working together to  
20 make that happen, but I wanted to make it real, real  
21 clear, too, that we need to create that definition for  
22 the applicability of the research and development tax  
23 credit. And the reason for that is this:  
24 Pennsylvania already has, if not the greatest, one of  
25 the greatest differentials between what are C

1 corporations and what are subchapter S corporations  
2 actually pay in terms of taxes. Subchapter S's pay a  
3 personal income tax. Maybe not Kennametal. They  
4 might be a C, but my guess is you are probably are all  
5 S's.

6 MR. BRIAN KENNEDY: We're all C's.

7 REPRESENTATIVE DAVID KEVDANSKY: You're all  
8 C's, okay. S's pay the personal income tax rate at  
9 3.07. C's pay, at least on paper, okay, you pay 9.9,  
10 but we know that hardly anybody pays that anyhow,  
11 okay, you know, because we have these different  
12 mechanisms in place in law that you're allowed to  
13 utilize, that enable you to pay a lot less, okay?

14 So, between 3.7 and 9.9, there's a huge,  
15 even though that's the nominal rate, the effective  
16 rate is something less than 9.9, but, nonetheless,  
17 even the differential between the effective rate  
18 of the CNI at less than 9.9 and the PIT. There's  
19 such a skewed differential, okay.

20 And we've already had a proliferation of  
21 S corporations in this state over the last decade.  
22 Ten years ago or so we had about 100,000, a little  
23 more than a 100,000 S corporations. Today we have  
24 over 400,000, okay.

25 Now, obviously, a lot of that's because

1 of the start-up of a lot of new businesses, and  
2 that's good, and we want to encourage that. But a  
3 lot of it also happened because a lot of  
4 corporations have become reclassified out of C and  
5 into S. And there's that huge differential then  
6 in terms of revenues that they pay to the  
7 Commonwealth, okay.

8 So I think to the extent we can work on a  
9 definition that is relevant and useful to you all,  
10 we need to make sure that it stays focused on the  
11 utilization of the R&D tax credit, okay.

12 One question that you all could answer  
13 however you want kind is kind of the question that  
14 Tim asked, I mean, what are you doing here in  
15 western Pennsylvania? I mean, come on, this is  
16 the worst state in the nation to do business.

17 We've got the highest CNI in the whole  
18 country. We're the only state, maybe outside of  
19 New Hampshire, that hasn't uncapped NOL's. You  
20 know, we're this smoggy, dirty place. Living in  
21 the past with more municipalities and like  
22 over-fragmented global governments and everything.  
23 I don't understand this, but we're attracting  
24 venture capital investment at record levels, and  
25 you all are here.

1                   Why are people doing business here and  
2                   investigating here? Why?

3                   MR. LARRY SWEENEY: I'll take a shot. Founders  
4                   of our company are from Pittsburgh, not all borne and  
5                   raised, but from Pittsburgh. We decided that we  
6                   wanted to stay in this area.

7                   Why? It has a lot to do with core  
8                   values. Our company is very strong when it comes  
9                   to core values based on pretty much the root of it  
10                  is integrity, and we find that in the Pittsburgh  
11                  community you have a lot of that in western  
12                  Pennsylvania. And it breeds a type of person that  
13                  has a certain level of loyalty, a certain level of  
14                  integrity and honestly and truthfulness. And we  
15                  value that very highly in our work force.

16                  REPRESENTATIVE DAVID KEVDANSKY: Thank you.  
17                  Does anybody else want to take a stab at this?

18                  DR. WILLIAM HSU: It's the same thing for  
19                  Kennametal. Kennametal, even though that name doesn't  
20                  reflect original family, it's the Kenna family. They  
21                  dropped the Mac and become Kenna.

22                  It's McKenna family that started the  
23                  whole thing, and it was actually rooted back to  
24                  when this whole area was the center of steel  
25                  manufacturing. That's how we started. That's how

1 we come up with the hot metal to help process the  
2 steel.

3 And we have been here for over 75 years.

4 This is the home. I mean, we are still based in  
5 Latrobe. That's where the world headquarters is,  
6 and that's where the global technology center is.

7 And we like the blue collar work ethic,  
8 and we like what is described to be the  
9 friendliness of the people. I'm not a native  
10 Pennsylvanian. I actually spend a lot of my  
11 career in Delaware, Wilmington, but when I move  
12 here I really like the friendliness of the people.

13 So, this is an outstanding environment in  
14 terms of raising a family and doing necessary  
15 work, you know? But you are very well said that  
16 the weather of these things could be distracting.

17 REPRESENTATIVE DARYL METCALFE: I agree.

18 DR. WILLIAM HSU: My wife didn't like it in the  
19 wintertime. It got her depressed because she couldn't  
20 see the sunlight. Whereas on the east coast you see  
21 the blue skies all the time.

22 But it has its distractions, but overall,  
23 Kennametal decided that this is our corporate  
24 home. That's why we insisted on being here. We  
25 could at one time. In fact, the history suggested



1           that at one time we could have moved the whole  
2           corporation down to Carolina, North Carolina,  
3           because at one time, the whole engineering, design  
4           center of our metal working part is actually based  
5           in Raleigh.

6                         And so there was whole discussion should  
7           the whole company be split in two? One part here  
8           and one part in North Carolina? Should we all  
9           move down to North Carolina? And then the answer,  
10          after a lengthy debate, they said, the family  
11          members said this is our home. We need to be  
12          here.

13                        So we built the technology center. We  
14          moved everybody back from North Carolina. In  
15          doing so, we lost 70 percent of the work force.  
16          We had already built the entire engineering  
17          competency. So, we are here to stay. So you  
18          don't have to worry us fleeing, in spite of all  
19          the negatives you mentioned.

20                        REPRESENTATIVE DAVID KEVDANSKY: Anybody else  
21          have a comment?

22                        MR. SEAN ROLLMAN: The younger, early stage  
23          companies that reflect a lot of the members of the  
24          Technology Council, borne out of the seeds that are  
25          planted out of the universities.

1                   My former employer was also founded out  
2                   of some brains that came out of the local  
3                   universities. They did a search and they chose  
4                   Pittsburgh because of the cost of living. So, the  
5                   evaluation that I know we did at that last company  
6                   was not as much from a business perspective, as  
7                   from a personal perspective in the eyes of our  
8                   employee base.

9                   The fact is our wages here in Pittsburgh  
10                  are about 60 percent less than they are on the  
11                  west coast. So, if you can convince those skills,  
12                  those technological skills to come into  
13                  Pittsburgh, which we were successful at doing at  
14                  our last company and today's, there's a benefit to  
15                  it.

16                  You're right. There's going to be folks  
17                  that have that stereotyped image that it's hard  
18                  for them to get over. I think two of our biggest  
19                  goals is to get national sports television to not  
20                  show the blast furnaces every time they show  
21                  Pittsburgh Steelers or the Penguins. That was  
22                  driving me crazy.

23                  My ten-year old son was watching the  
24                  Penguins last week, and they come from a  
25                  commercial break, and there's this big blast

1           furnace. And my son says, what was that?

2                         That's exactly the point. Unfortunately,  
3           the world is thinking that we still have black  
4           smoke and steel mills downtown, and by no means  
5           the steel industry is certainly critical to our  
6           economy, but the fact is it's not the case.

7                         But a lot of it comes from the  
8           universities. We have great universities. I  
9           think way disproportionately more strength here  
10          than in a lot of cities, and companies like ours  
11          take advantage of that. We were borne out of  
12          that.

13                        MR. JOSEPH JACOBSON: And I would echo all of  
14          that what you heard. I would also add from in terms  
15          of the venture capital, that is, it's backing our  
16          company, they are from the Pittsburgh area. And given  
17          that as opposed to someone coming out of Silicon  
18          Valley, I mean, there's a totally different approach  
19          on how they manage a company, all right.

20                        I've been with companies before that were  
21          under venture capitalists that were much more  
22          aggressive, much more concerned about their bottom  
23          line in terms of how quickly they could turn and  
24          spin the company. But with our partners at this  
25          point, they're much more patient, not involved in

1 the day-to-day activities, and are more concerned  
2 about developing industries within the Pittsburgh  
3 area. So, it's a win/win for all of us.

4 REPRESENTATIVE DAVID KEVDANSKY: Brian, do you  
5 want to take a stab?

6 MR. BRIAN KENNEDY: Well, I would just say that  
7 you've seen some of the great companies that are here.  
8 But I would say that we believe that some of the  
9 uncompetitive facts of our business climate are  
10 impacting our growth, right? So, we are growing, our  
11 economy, and every states' growing their economy.  
12 We're just not growing as quickly as other regions.

13 And we do think that we could accelerate  
14 that growth by knocking off some of these  
15 uncompetitive pieces of our tax climate, and by  
16 putting in some of the things like single sales  
17 factor, which everybody is going to do single  
18 sales factor. The last one to do it is going to  
19 be the one that doesn't have any benefit out of  
20 it, of any single sales.

21 So, now, we just think we could  
22 accelerate our growth, and we could have more  
23 companies like the ones before you. We could do  
24 things like increase and expand the R&D tax within  
25 Pennsylvania, and to send advice to manufacturers

1 to make investments.

2 Like our good friends at U.S. Steel this  
3 year announced -- I think the governor  
4 characterized it as one of the largest corporate  
5 sector capital investments in the state's history.  
6 And there are some tax ramifications for those  
7 investments that really don't make sense in terms  
8 of public policy.

9 So great things going on in Pennsylvania.  
10 The venture capital growth, you guys are doing a  
11 lot in the General Assembly to fuel some of that  
12 growth by supporting early stage things through  
13 groups like Innovation Works and the Ben Franklin  
14 Program, the Life Sciences Greenhouse.

15 It's really a partnership. It really  
16 does involve investing and creating a business, a  
17 competitive business by even having a balanced  
18 approach. And you've done a very good job at  
19 balancing it. You've made some progress I think  
20 in the capital stock and franchise tax. You made  
21 progress on the NOL. You made progress on the  
22 single sales factor. We're just here today to say  
23 keep moving forward and let's make some more  
24 progress here in 2008.

25 REPRESENTATIVE DAVID KEVDANSKY: Let me sum up

1 with a summary of what I heard, and then just put this  
2 all in context. I appreciate your response.

3 I mean, what it tells me is for some  
4 reason those of us from western Pennsylvania like  
5 to beat ourselves up a lot. We always seem to  
6 talk about what's bad, what doesn't work. We're  
7 our own worst enemies sometimes, to be honest with  
8 you, okay.

9 There are a lot of good things that you  
10 obviously pointed out. You know, we've got access  
11 to capital. We are competitive in labor cost and  
12 labor markets. We certainly have some of the best  
13 medical and education research facilities in the  
14 world, if not the country. We do have a strong  
15 work ethic, friendly people.

16 And for those of us that like four  
17 seasons, we got that, too, okay. And not  
18 everybody's a sunbird, okay. But there's a lot of  
19 assets that we have here in Pennsylvania and  
20 particularly in our region. And I think sometimes  
21 that all gets drowned out by the self-inflicted  
22 negative perception that we have.

23 And, Sean, just one thing. I think we  
24 ought to take, for our region, we ought to have  
25 two images. It ought to be all this investments.

1           This old steel mill. Joe, you have no idea what  
2           this facility along here was 20 years ago.

3                   MR. JOSEPH JACOBSON: Right.

4                   REPRESENTATIVE DAVID KEVDANSKY: Okay? It was  
5           old the J&L Works. We've taken an old industrial,  
6           contaminated -- you know, it had a lot of really good  
7           jobs here. I mean, you can't believe back in the  
8           1970's in our region. I mean, from 1979 to 1984, this  
9           region lost 150,000 manufacturing jobs. You have no  
10          idea the enormity of these steel complexes, okay.

11                   And, you know, that is our past, but it's  
12          also part of our present, too, because that  
13          \$1 billion that U.S. Steel's investing in coke  
14          making technology, that's in my district, okay.

15                   So, I think there's two images here. One  
16          is what we've done with the old brown fields and  
17          how we've renovated them and made significant  
18          public investment to put an environment together  
19          where some of our most innovative companies can be  
20          nurtured and grow, right along here.

21                   But it's also down in Bill Kortz's area  
22          and my area of the Mon Valley, too, where our  
23          manufacturers, thanks to companies like  
24          Kennametals, are helping to develop the new  
25          technologies, the manufacturing processes to keep

1           our existing manufacturing competitiveness as  
2           well.

3                         So while I really will continue to do  
4           everything I can to try to help grow our new  
5           economy, manufacturing does matter, too. And that  
6           ought to be made sure that we keep that in mind  
7           and integrate that in our efforts as well. Brian?

8                         MR. BRIAN KENNEDY: Can I just follow up on  
9           that point because it's really relevant to today's  
10          discussion. I mentioned in my testimony the Deloitte  
11          study and that it was conducted by the state's  
12          Industrial Resource Centers.

13                        What I didn't mention was the response of  
14          Industrial Resource Centers. Catalyst Connection,  
15          which is co-located with us and has been partner  
16          of ours, they have been working to help --  
17          historically have been working with companies to  
18          help make them more efficient and to manufacture  
19          and increase their productivity.

20                        As a result of this study, they are now  
21          working with manufacturers in probably each of  
22          your districts to help them not only become  
23          state-of-the-art in their manufacturing process,  
24          but also to help them understand product  
25          development processes and how to transition away



1 from some of these historically commoditized  
2 industries into these value-added sectors where  
3 they can grow their topline revenue.

4 And as a result you're seeing some  
5 tremendous impact at the firms that work with the  
6 Industrial Resource Center. So, that's just  
7 another example of how the General Assembly has  
8 been supportive.

9 I know that after that study you guys  
10 actually increased their funding by 50 percent.  
11 So that's just another example of how you've been  
12 working together to support innovation and  
13 manufacturing in Pennsylvania, and as an example  
14 of that balanced approach that I was talking  
15 about.

16 REPRESENTATIVE DAVID KEVDANSKY: And now just  
17 my final observations, to put this all in context. I  
18 mean you obviously know how I feel about R&D, want to  
19 make it happen. And I recognize there are these other  
20 business tax issues that are important in various  
21 degrees for different companies, depending on where  
22 you are, what kind of business you're in, and whether  
23 you're a start-up or a mid range or a mature industry  
24 and company.

25 The uncapping the NOL's, doing the full

1 sales factor on apportioning, the CNI, lowering  
2 the CNI, all of those, I understand, are things  
3 that the business community wants. I'm an  
4 economist by training, so I understand that we  
5 have these wants and you've got to match that  
6 against the ability to pay. And as Representative  
7 Frankel spoke a little bit earlier, given what's  
8 going on nationally with the economy and with  
9 states surrounding Pennsylvania, we're looking  
10 at a pretty tight fiscal situation. We got to be  
11 really careful what we do in terms of tax code  
12 changes.

13 I think even within that bleak picture,  
14 that bleak economic picture that we're looking at,  
15 I still think we can make an argument that  
16 investment and research and development is really  
17 important, okay. I think it's the most important  
18 thing.

19 I hear about work force development, too,  
20 but I think this is really key to  
21 our competitiveness, which is really in the  
22 long-run is what we need to stay focused on. But  
23 we have all these wants, but the reality is in this  
24 fiscal year we're not going to be able to do  
25 everything. So, it boils down to making choices.

1           And that's what we elect public officials to do is  
2           to make those choices.

3                        I'd like to see some movement on these  
4           other business tax issues as well, but I just  
5           can't pass the opportunity when I have four  
6           important business people in front of me to talk  
7           about two ways that we could do that.  
8           Notwithstanding, we don't have a whole lot of  
9           budget surplus to be able to fund tax cuts.  
10          There's still two other ways to do it.

11                       One of them is called adopting a way of  
12          making all corporations pay their fair share.  
13          It's called unitary combined reporting. A couple  
14          dozen, almost a couple dozen other states have  
15          done this. This requires companies and all the  
16          subsidiaries to report all their revenue on a  
17          unitary basis and then apportion that fairly and  
18          accurately, okay, amongst all the different  
19          divisions and subsidiaries.

20                       If we -- and the Governor had a tax  
21          reform commission about four or five years ago  
22          that looked at our business tax structure and said  
23          we want to do all these things. We want to uncap  
24          NOL's, we want to do single sales factor, we want  
25          to drive CNI down to 7.5, taken us from the

1           highest or second highest to the mid range. And  
2           we want to aggressively ramp up R&D investment.  
3           We could do all that, okay, if we adopted unitary  
4           combined reporting.

5                         It would generate -- the state would  
6           collect about 483 million more revenue from the  
7           business community, but we would use all that  
8           money to lower all these taxes, okay. And  
9           different companies feel different ways about it  
10          because some companies who aren't paying 9.9,  
11          okay, would say I'm not paying it anyhow, so don't  
12          give me combined reporting.

13                        But I think for a lot of small, medium  
14          sized businesses, okay, who can't employ a whole  
15          battery of tax accountants and tax lawyers or pay  
16          a bunch of outside legal and accounting expertise  
17          to help you take advantage of creating a pick in  
18          Delaware and transferring your intangible assets,  
19          you can't play that whole game. Chances are  
20          you're probably paying more than your fair share  
21          of business taxes, so we could make that change.  
22          That's one way, and that involves some tough  
23          choices for us and the business community.

24                        There's another way to do it. You want  
25          to uncap the NOL's this year? It's \$180 million,

1           roughly. Can I cut \$180 million out of work force  
2           development and work force training? We can cut  
3           taxes and we can cut spending to match, too.

4                    REPRESENTATIVE DARYL METCALFE: Hear, hear.

5                    REPRESENTATIVE DAVID KEVDANSKY: Okay. That's  
6           another choice. But those are tough choices. And  
7           from what I'm hearing yesterday, today and a couple of  
8           weeks ago in Philadelphia and the suburbs, work force  
9           development is really crucial to our competitiveness  
10          as well. R&D is, okay, but our investment in our work  
11          force development program is really crucial as well.  
12          But that's another tough choice.

13                    So that's the context in which those of  
14          us that are elected have got to make these tough  
15          choices. We want to do everything, but the  
16          economic reality is we live in a fiscal world of  
17          finite limits.

18                    So that's where this discussion on R&D is  
19          going to take place in that larger context of  
20          everything else that we have to try to do in  
21          Harrisburg, okay.

22                    Anyhow, Brian, thank you, again, for not  
23          only hosting this, but putting together, Brian, a  
24          really good diversified panel of business people  
25          to tell us about how this works. And

1           let's continue to work together with the business  
2           community, Democrats and Republicans to try to  
3           make this happen this year.

4                    REPRESENTATIVE DARYL METCALFE:   Republican.

5                    REPRESENTATIVE DAVID KEVDANSKY:   I said  
6           Democrats and Republican.

7                    REPRESENTATIVE DARYL METCALFE:   You said  
8           Republicans.  I'm just one today.

9                    REPRESENTATIVE DAVID KEVDANSKY:   You and your  
10          colleagues, Daryl, okay?  Thank you much.

11          (THEREUPON, proceedings concluded at 11:54  
12          a.m.)

13

14

15

16

17

18

19

20

21

22

23

24

25

1  
2  
3  
4  
5  
6  
7  
8  
9  
10  
11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25

COURT REPORTER'S CERTIFICATE

I hereby certify that I, Donna M. McMullen, RMR, Notary Public, reported in stenotype the record of proceedings in the above-entitled matter, and that this copy is a full, true, and accurate transcript of my said stenotype notes.

---

Court Reporter, RMR