

Honolulu, Hawaii

FEB 17

, 2006

RE: S.B. No. 2100
S.D. 1

Honorable Robert Bunda
President of the Senate
Twenty-Third State Legislature
Regular Session of 2006
State of Hawaii

Sir:

Your Committees on Media, Arts, Science, and Technology and Business and Economic Development, to which was referred S.B. No. 2100 entitled:

"A BILL FOR AN ACT RELATING TO VENTURE FINANCING,"

beg leave to report as follows:

The purpose of this measure is to provide matching funds to the Hawaii Strategic Development Corporation for the purpose of attracting additional private venture capital to accelerate the growth of Hawaii's technology sectors.

Your Committees received testimony in support of the measure from the Department of Business, Economic Development, and Tourism, the Hawaii Strategic Development Corporation, the University of Hawaii's Vice Chancellor for Research and the Director of the University Connections program, The Hawaii Venture Capital Association, the Hawaii Science and Technology Council, the Hawaii Crop Improvement Association, and the Hawaii PacifiCap Group.

Your Committees find that Hawaii's emerging growth companies continue to face a shortage of available private sector venture capital. Much progress has been made in recent years, but the continued shortfall of equity growth financing stifles new company expansion and the State's economic development. The Hawaii Strategic Development Corporation has been effective as a catalyst in generating venture funding in conjunction with private investors, directly leveraging its \$16,000,000 of public funds



over seven times with private capital and indirectly leveraging its funds over thirty times for investment in Hawaii's startup companies. Act 221, Session Laws of Hawaii 2001, and Act 215, Session Laws of Hawaii 2004, have greatly stimulated new private investment by providing incentives to investors in qualified high technology businesses.

However, as pointed out by several testifiers, "Hawaii tech businesses need access to later stage capital to take them through their most critical growth phase, when the most jobs and revenues are created. Unfortunately, there is a significant lack of venture capital in Hawaii necessary to support the larger capital needs of later stage technology companies . . . this funding gap must be addressed if we want to build a sustainable tech industry in Hawaii" (University of Hawaii Vice Chancellor for Research testimony).

The Department of Business, Economic Development, and Tourism compared the benefits of using refundable or contingent tax credits to provide an adequate level of venture funds for the State Private Investment Fund, created under Act 215, Session Laws of Hawaii 2004, against the benefits of direct appropriations. Ultimately, the Department of Business, Economic Development, and Tourism concluded that the benefits of a direct appropriation – e.g., providing the most return for the State, being the most straightforward to understand, and the most efficient, with certainty of cost – outweighed the tax credits approach that has characterized the State Private Investment Fund venture financing model.

Your Committees are concerned that this bill's funding level of \$10,000,000 to the Hawaii Strategic Development Corporation, which is to be matched on a one-to-one basis by private sector funds, would still not be enough to meet the larger funding needs of later stage companies and to keep them in Hawaii. As such, your Committees believe that a direct appropriation to a larger state investment partner may be a more appropriate route by which to address the venture financing concerns expressed by the University of Hawaii and the Department of Business, Economic Development, and Tourism.

In light of this understanding, your Committees also believe that, if a Hawaii-based entity that possesses formidable investment capital resources invests in Hawaii-based high technology businesses, such actions would most likely spur the



interest of out-of-state venture capital investors to also invest in these businesses. This would further augment interest in the State's high technology industry and stimulate new private investment.

To this end, your Committees also find that the Employees' Retirement System has been effective as a proven investment leader, possesses formidable investment capital, and currently has the authority to act as a catalyst in generating venture funding in conjunction with private investors.

Your Committees believe that, with additional resources, the Employees' Retirement System could expand its public/private partnerships with market-based investment firms that can provide equity capital to high-growth companies and strengthen and diversify Hawaii's economy. These opportunities can potentially yield additional economic stability and vitality to the State's economy, which in turn strengthens the State's ability to pay its employer contributions to the Employees' Retirement System. Consequently, any successful Hawaii-based high technology business investments made by the Employees' Retirement System will not only ensure that the Employees' Retirement System will meet its pension benefit obligations, but will concomitantly assist in growing and diversifying the State's economy.

Your Committees have amended the measure by:

- (1) Deleting its substantive provisions, except for the measure's purpose section;
- (2) Inserting provisions that appropriate \$25,000,000 in general funds to the Employees' Retirement System for it to invest in sound, Hawaii-based high technology investment opportunities for the benefit of public employees and to attract additional private venture capital that will accelerate the growth of Hawaii's technology sectors;
- (3) Providing that the investments made, and any interest accrued or losses incurred thereon, by the Employees' Retirement System pursuant to this measure will not be included in any calculation of its statutorily-mandated investment yield rate; and



- (4) Amending the purpose section of the measure to reflect the amendments made by your Committees.

Your Committees note that the Employees' Retirement System already has the authority to invest in Hawaii-based high technology businesses pursuant to section 88-119(11), Hawaii Revised Statutes, and that the appropriation of moneys under this measure are provided to ensure that the Employees' Retirement System allocates adequate investment capital toward sound, Hawaii-based high technology businesses.

As affirmed by the records of votes of the members of your Committees on Media, Arts, Science, and Technology and Business and Economic Development that are attached to this report, your Committees are in accord with the intent and purpose of S.B. No. 2100, as amended herein, and recommend that it pass Second Reading in the form attached hereto as S.B. No. 2100, S.D. 1, and be referred to the Committee on Ways and Means.

Respectfully submitted on
behalf of the members of the
Committees on Media, Arts,
Science, and Technology and
Business and Economic
Development,



WILL ESPERO, Chair



CAROL FUKUNAGA, Chair



