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# A BILL FOR AN ACT

RELATING TO THE INNOVATION ECONOMY.

**BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF HAWAII:**

1 PART I

2 SECTION 1. The legislature finds that Hawaii's desire for  
3 economic growth that benefits all residents depends on building  
4 our State's human resources, and in turn, applying these highly  
5 skilled resources to the creation and adoption of innovation  
6 across its economy.

7 The legislature further finds that economic growth and  
8 diversification throughout many communities has been enhanced by  
9 the availability of venture capital funding for entrepreneurs  
10 engaged in building innovative new ventures. Well-known regions  
11 such as Silicon Valley, Route 128 in Boston, Austin, Texas, and  
12 the Research Triangle in North Carolina have benefited greatly  
13 from the combination of scientific research, an entrepreneurial  
14 culture driving high technology growth, and funding availability  
15 for early stage equity investments. Other areas similar in size  
16 and population to Hawaii, including San Diego, Salt Lake City,



1 Seattle, and Boulder have also developed strong technology-based  
2 businesses with the assistance of venture capital.

3 The source of this venture capital is derived in large part  
4 through employee pension funds. Of the approximately  
5 \$25,000,000,000 of venture investment taking place in 2006, over  
6 half was provided by pension funds. Many public pension funds  
7 target investments in-state to provide enhanced returns to the  
8 pensioners and support the development of high-growth businesses  
9 within local communities.

10 The employees' retirement system of the State of Hawaii has  
11 committed approximately \$300,000,000 to the alternative asset  
12 category, including venture capital, but none of it is invested  
13 in Hawaii. The legislature finds that this lack of investment  
14 in Hawaii venture capital by the employees' retirement system may  
15 be due to a lack of large-scale qualified investment  
16 opportunities and concerns over the possible breach of fiduciary  
17 duty and prudent investor rules related to early stage  
18 investing. Some jurisdictions such as Arkansas and Michigan  
19 encourage local investment by pension funds by relieving  
20 fiduciaries of liability for investing in local venture capital.  
21 Others, such as the state of Oregon, have legislated investment



1 by the public pension fund in local venture capital where  
2 prudent.

3 The purpose of this part is to require the employees'  
4 retirement system to give a preference to Hawaii venture capital  
5 and other alternative asset category investments that offer an  
6 equal or lesser risk and equal or greater return as compared to  
7 out-of-state investments.

8 SECTION 2. Section 88-119, Hawaii Revised Statutes, is  
9 amended to read as follows:

10 **"§88-119 Investments.** Investments may be made in:

11 (1) Real estate loans and mortgages. Obligations (as  
12 defined in section 431:6-101) of any of the following  
13 classes:

14 (A) Obligations secured by mortgages of nonprofit  
15 corporations desiring to build multirental units  
16 (ten units or more) subject to control of the  
17 government for occupancy by families displaced as  
18 a result of government action;

19 (B) Obligations secured by mortgages insured by the  
20 Federal Housing Administration;



1 (C) Obligations for the repayment of home loans made  
2 under the Servicemen's Readjustment Act of 1944  
3 or under Title II of the National Housing Act;  
4 (D) Other obligations secured by first mortgages on  
5 unencumbered improved real estate owned in fee  
6 simple; provided that the amount of the  
7 obligation at the time investment is made therein  
8 shall not exceed eighty per cent of the value of  
9 the real estate and improvements mortgaged to  
10 secure it, and except that the amount of the  
11 obligation at the time investment is made therein  
12 may exceed eighty per cent but no more than  
13 ninety per cent of the value of the real estate  
14 and improvements mortgaged to secure it; provided  
15 further that the obligation is insured or  
16 guaranteed against default or loss under a  
17 mortgage insurance policy issued by a casualty  
18 insurance company licensed to do business in the  
19 [~~State.~~] state. The coverage provided by the  
20 insurer shall be sufficient to reduce the  
21 system's exposure to not more than eighty per  
22 cent of the value of the real estate and



1 improvements mortgaged to secure it. The  
2 insurance coverage shall remain in force until  
3 the principal amount of the obligation is reduced  
4 to eighty per cent of the market value of the  
5 real estate and improvements mortgaged to secure  
6 it, at which time the coverage shall be subject  
7 to cancellation solely at the option of the  
8 board. Real estate shall not be deemed to be  
9 encumbered within the meaning of this  
10 subparagraph by reason of the existence of any of  
11 the restrictions, charges, or claims described in  
12 section 431:6-308;

13 (E) Other obligations secured by first mortgages of  
14 leasehold interests in improved real estate;  
15 provided that:

16 (i) Each leasehold interest at the time shall  
17 have a current term extending at least two  
18 years beyond the stated maturity of the  
19 obligation it secures; and

20 (ii) The amount of the obligation at the time  
21 investment is made therein shall not exceed  
22 eighty per cent of the value of the



1           respective leasehold interest and  
2           improvements, and except that the amount of  
3           the obligation at the time investment is  
4           made therein may exceed eighty per cent but  
5           no more than ninety per cent of the value of  
6           the leasehold interest and improvements  
7           mortgaged to secure it;  
8           provided further that the obligation is insured  
9           or guaranteed against default or loss under a  
10          mortgage insurance policy issued by a casualty  
11          insurance company licensed to do business in the  
12          [~~State.~~] state. The coverage provided by the  
13          insurer shall be sufficient to reduce the  
14          system's exposure to not more than eighty per  
15          cent of the value of the leasehold interest and  
16          improvements mortgaged to secure it. The  
17          insurance coverage shall remain in force until  
18          the principal amount of the obligation is reduced  
19          to eighty per cent of the market value of the  
20          leasehold interest and improvements mortgaged to  
21          secure it, at which time the coverage shall be



1 subject to cancellation solely at the option of  
2 the board;

3 (F) Obligations for the repayment of home loans  
4 guaranteed by the department of Hawaiian home  
5 lands pursuant to section 214(b) of the Hawaiian  
6 Homes Commission Act, 1920; and

7 (G) Obligations secured by second mortgages on  
8 improved real estate for which the mortgagor  
9 procures a second mortgage on the improved real  
10 estate for the purpose of acquiring the  
11 leaseholder's fee simple interest in the improved  
12 real estate; provided that any prior mortgage  
13 does not contain provisions that might jeopardize  
14 the security position of the retirement system or  
15 the borrower's ability to repay the mortgage  
16 loan.

17 The board may retain the real estate, including  
18 leasehold interests therein, as it may acquire by  
19 foreclosure of mortgages or in enforcement of  
20 security, or as may be conveyed to it in satisfaction  
21 of debts previously contracted; provided that all the  
22 real estate, other than leasehold interests, shall be



1 sold within five years after acquiring the same,  
2 subject to extension by the governor for additional  
3 periods not exceeding five years each, and that all  
4 the leasehold interests shall be sold within one year  
5 after acquiring the same, subject to extension by the  
6 governor for additional periods not exceeding one year  
7 each;

8 (2) Government obligations, etc. Obligations of any of  
9 the following classes:

10 (A) Obligations issued or guaranteed as to principal  
11 and interest by the United States or by any state  
12 thereof or by any municipal or political  
13 subdivision or school district of any of the  
14 foregoing; provided that principal of and  
15 interest on the obligations are payable in  
16 currency of the United States; or sovereign debt  
17 instruments issued by agencies of, or guaranteed  
18 by foreign governments;

19 (B) Revenue bonds, whether or not permitted by any  
20 other provision hereof, of the State or any  
21 municipal or political subdivision thereof,  
22 including the board of water supply of the city





- 1 and county of Honolulu, and street or improvement  
2 district bonds of any district or project in the  
3 [~~State;~~] state; and
- 4 (C) Obligations issued or guaranteed by any federal  
5 home loan bank, including consolidated federal  
6 home loan bank obligations, the Home Owner's Loan  
7 Corporation, the Federal National Mortgage  
8 Association, or the Small Business  
9 Administration;
- 10 (3) Corporate obligations. Below investment grade or  
11 nonrated debt instruments, foreign or domestic, in  
12 accordance with investment guidelines adopted by the  
13 board;
- 14 (4) Preferred and common stocks. Shares of preferred or  
15 common stock of any corporation created or existing  
16 under the laws of the United States or of any state or  
17 district thereof or of any country;
- 18 (5) Obligations eligible by law for purchase in the open  
19 market by federal reserve banks;
- 20 (6) Obligations issued or guaranteed by the International  
21 Bank for Reconstruction and Development, the



1 Inter-American Development Bank, the Asian Development  
2 Bank, or the African Development Bank;

3 (7) Obligations secured by collateral consisting of any of  
4 the securities or stock listed above and worth at the  
5 time the investment is made at least fifteen per cent  
6 more than the amount of the respective obligations;

7 (8) Insurance company obligations. Contracts and  
8 agreements supplemental thereto providing for  
9 participation in one or more accounts of a life  
10 insurance company authorized to do business in Hawaii,  
11 including its separate accounts, and whether the  
12 investments allocated thereto are comprised of stocks  
13 or other securities or of real or personal property or  
14 interests therein;

15 (9) Interests in real property. Interests in improved or  
16 productive real property in which, in the informed  
17 opinion of the board, it is prudent to invest funds of  
18 the system. For purposes of this paragraph, "real  
19 property" includes any property treated as real  
20 property either by local law or for federal income tax  
21 purposes. Investments in improved or productive real  
22 property may be made directly or through pooled funds,



1 including common or collective trust funds of banks  
2 and trust companies, group or unit trusts, limited  
3 partnerships, limited liability companies, investment  
4 trusts, title-holding corporations recognized under  
5 section 501(c) of the Internal Revenue Code of 1986,  
6 as amended, similar entities that would protect the  
7 system's interest, and other pooled funds invested on  
8 behalf of the system by investment managers retained  
9 by the system;

10 (10) Other securities and futures contracts. Securities  
11 and futures contracts in which in the informed opinion  
12 of the board it is prudent to invest funds of the  
13 system, including currency, interest rate, bond, and  
14 stock index futures contracts and options on the  
15 contracts to hedge against anticipated changes in  
16 currencies, interest rates, and bond and stock prices  
17 that might otherwise have an adverse effect upon the  
18 value of the system's securities portfolios; covered  
19 put and call options on securities; and stock; whether  
20 or not the securities, stock, futures contracts, or  
21 options on futures are expressly authorized by or  
22 qualify under the foregoing paragraphs, and



1           notwithstanding any limitation of any of the foregoing  
2           paragraphs (including paragraph (4)); and  
3       (11) Private placements. Investments in institutional  
4           blind pool limited partnerships, limited liability  
5           companies, or direct investments that make private  
6           debt and equity investments in privately held  
7           companies, including but not limited to investments in  
8           Hawaii high technology businesses or venture capital  
9           investments that, in the informed opinion of the  
10          board, are appropriate to invest funds of the  
11          system~~[—In]~~; provided that as of January 1, 2008,  
12          and to the extent that it is prudent to so do, the  
13          board in considering any investment in an out-of-state  
14          private placement shall determine whether there is  
15          available, and instead invest in any Hawaii private  
16          placement that is of equal or lesser risk and equal or  
17          greater return; provided further that Hawaii private  
18          placement investments shall not exceed three per cent  
19          of the funds of the system; and provided further that  
20          in evaluating venture capital investments, the board  
21          shall consider, among other things, the impact an



1 investment may have on job creation in Hawaii and on  
2 the state economy."

3 PART II

4 SECTION 3. Universities that generate new knowledge and  
5 discoveries can be important contributors in developing a  
6 state's technology-based economy. But for a university to make  
7 that contribution, there must be effective mechanisms to move  
8 innovation into the marketplace. At the University of Hawaii,  
9 commercialization assistance is provided by the office of  
10 technology transfer and economic development. Activities  
11 include securing patents, seeking licensing opportunities, and  
12 assisting university researchers to transform ideas and  
13 innovations into products ready for commercialization. The  
14 office of technology transfer and economic development's ability  
15 to fulfill its mandate would be enhanced by collaboration with  
16 commercialization experts and funding from the private sector.

17 The purpose of this part is to enhance the ability of the  
18 office of technology transfer and economic development to  
19 increase commercialization of University of Hawaii discoveries  
20 by providing funds to the office of technology transfer to fund  
21 a partnership with a qualified and experienced private sector  
22 entity. This partnership will provide the University of Hawaii



1 with resources and expertise to ramp up the number of  
2 discoveries disclosed and the number of partnerships and  
3 arrangements to commercialize those discoveries. The department  
4 of business, economic development, and tourism, the private  
5 sector partner, and the University of Hawaii shall contribute to  
6 this commercialization joint venture; and the private sector  
7 partner and the University of Hawaii shall share in the return  
8 of their efforts.

9 SECTION 4. There is appropriated out of the general  
10 revenues of the State of Hawaii the sum of \$ , or so  
11 much thereof as may be necessary for fiscal year 2007-2008, and  
12 the same sum, or so much thereof as may be necessary for fiscal  
13 year 2008-2009, for the public-private university research  
14 commercialization partnership.

15 The sums appropriated shall be expended by the University  
16 of Hawaii office of technology transfer and economic development  
17 for the purposes of this part.

18 SECTION 5. Statutory material to be repealed is bracketed  
19 and stricken. New statutory material is underscored.

20 SECTION 6. This Act shall take effect on July 1, 2050.



**Report Title:**

Innovation Economy; Employees' Retirement System; University of Hawaii

**Description:**

Requires the Employees' Retirement System, as of January 1, 2008, to give preference to Hawaii venture capital investments of equal risk and return to out-of-state investments and caps these investments at three percent of system funds. Appropriates funds to the UH Office of Technology Transfer and Economic Development to enter into a partnership with a private sector entity. Effective July 1, 2050. (SB1365 HD1)

