

MINUTES OF THE SENATE COMMERCE COMMITTEE

The meeting was called to order by Chairperson Susan Wagle at 8:30 a.m., on February 15, 2011, in Room 548-S of the Capitol.

All members were present except:
Senator Emler - excused

Committee staff present:

Ms. Margaret Cianciarulo, Committee Assistant
Mr. Ken Wilke, Office of the Revisor of Statutes
Mr. Reed Holwegner, Kansas Legislative Research Department
Ms. Dorothy Noblitt, Kansas Legislative Research Department

Conferees appearing before the Committee:

Mr. Thomas Thornton, President & CEO, Kansas Bioscience Authority

Others attending:

See attached list.

Overview of The Kansas Bioscience Authority

Upon calling the meeting to order, the Chair called on Mr. Thomas Thornton, President & CEO of the Kansas Bioscience Authority, who referred the Committee to two booklets:

1. "Kansas Bioscience Authority, Testimony & Progress Report" that was included in his testimony, a summary of commitments, financials, a summary of outcome reports (economic development impact in the state), and the venture accelerator.

The Chair asked Mr. Thornton where the financials were listed in this booklet? (It would be under Tab 3.)

2. "Kansas Bioscience Authority 2010 Progress Report." tells a story of the vision of the legislature in terms of establishing the authority to position our state for leadership in the biosciences. We are attracting companies and researchers from all over the country. Biosciences in all corners of the State are attracting capital and creating jobs.

In terms of the Bioscience Authority, he was asked to provide an overview stating as an orientation, he offered KBA's:

1.) History - stating KBA was established under Kansas the Economic Development Growth Act of 2004, with a \$581M fund that specifically invests in projects to expand research, foster formation and growth of bioscience start-ups, and facilitates expansion of bioscience companies statewide.

2.) Major goals - the main goal is undisputed national leadership, and more importantly in areas where we have an advantage like animal health, bio materials, plant biology and others. We also feel we are effectively trying to bring the fourth leg to our state's economy, to position the biosciences to be a peer. As a reminder, the Bioscience Authority is effectively managing a TIF, under which the state withholding tax, base codes, and classification codes are deemed to be bioscience by the Kansas Legislature and capped at the end of the year for 2003. And 95% of the incremental growth from the caps are put in a fund managed from the authority accumulating over time, \$581.8M to invest in the types of projects he had just mentioned, referring the Committee to a graph on page 7 of his testimony, which shows how this will work.

He said it is important for the Legislature to understand the major goals, what are we trying to accomplish, driving us forward, and where do we stand. The key as mentioned earlier, is to expand our state's research and development infrastructure. When they first started in 2004, the bioscience research investment was around \$130M and their goal is to take it to \$650M. To date, we rest at around \$279M, which is a substantial growth, a 27% increase. The state though, ranks as the single, fastest, research and development enterprise in the nation. Venture capital investment was zero in 2004 but last year, \$35M was invested in 13 bioscience companies with their goal to take it to \$200M.

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Regarding bioscience companies – 883 in 2004, now 1,126, which is 243 new firms, 27% growth. Employment in the biosciences is 3,187 new jobs, 22% increase, and wage growth alone is \$212M. If we are successful though, ultimately the outcome will be that there will be several billion in annual recurring outcomes associated with this. So just do the 650, \$200M in venture funds will help there, it gets to be extremely large.

Focus matters. We invest in areas where Kansas has an existing strength in terms of both research and industrial cluster and where that overlap exists, that becomes a sweet spot for the KBA in terms of investments. We invest in game-changing projects, in both research and commercialization, and it is absolutely essential. We think one helps drive the other in many respects. We are a very valued organization in many respects. We operate and rightly fund, both our staff and Board of Directors, and are very focused on outcomes. Every investment we make, we need to clearly understand what the outcomes are going to be.

The KBA statutory authority allows us to invest in a rather wide variety of projects. The key on the research side is the ability to work with academic institutions that foster the attraction of distinguished researchers. This has been a particularly powerful program and another key element of supporting early-stage companies. We have a dedicated team inside the bioscience authority, six experienced bioscience entrepreneurs/investors that provide assistance to these companies, and help them to create jobs.

Regarding outcomes - he stated our key element for any presentation like this as an orientation and the total outcomes report is under Tab 4 if you would like to refer to details. The KBA to date has committed \$217.7M and have paid on those commitments, approximately \$45.7M. The realized outcomes are truly remarkable and as listed on page 14 of the handout. For every dollar that KBA has invested, we have yielded or turned an economic return of \$9.41. Those are just outcomes associated with achievements of existing milestones, and, as those existing investments achieve additional milestones over time, get substantially larger and these are presented on page 16. But that is \$1.9B in projected outcomes and that again, comes just from existing commitments.

National recognition – when KBA was formed, they were ranked in the top 40 in bioscience states. We now are ranked fifth in the nation and our gross state product ranks us either thirty-second or thirty-third. He then covered some of the KBA's top programs to give the Committee a sense of what the market is and what they are trying to do to position the state to be a major player in that market. Those included:

1.) Biological attack - they won the National Bio and Agro-Defense Facility (NBAF), the \$650M federal grant. We did it because we have an extraordinary research capacity at KSU, the best concentration of animal health companies and so called animal health corridor. NBAF is a \$650M facility. 1,500 construction jobs, a \$3.65B economic impact and the international leadership that goes with that. Appropriations – the President's budget request yesterday, he requested \$150M in new funding in year 2012 to invest in the NBAF. FY2011 funding has been tied up in the so-called continuing resolution. One of the things about NBAF, it will be completed, commissioned, and available for operation in 2018. Here in Kansas, we have executed a strategy that will accelerate that research mission now. Why are we doing this? Because we think if we are smart about this, we can turn that \$3.65B number, again just associated with the construction and operations of the NBAF, into 2X or 3X that number by initiating the research mission now, attracting companies to the state now, and beginning to commercialize technologies out of that lab right now.

Regarding the Texas lawsuit, it has been thrown out. The Department of Homeland Securities Inspector General, at the request of Congress, conducted an investigation into the conduct of the site selection that located the NBAF here in Kansas and concluded the process was fair and done in accordance with federal regulations associated with projects of this sort.

Cancer Care – KSU has the Cancer Center and of course, the Community Clinical Oncology Program (CCOP) in Wichita. The University of Kansas Cancer Center is trying to pursue so-called National Cancer Institute Designation as a Cancer Center. KBA has invested, along side the university, to recruit 7 eminent scholars to the Cancer Center, the minimum number required to pursue cancer center designation, \$11.4M in cancer research and NCI funding has been met and achieved this year.

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Bioscience Entrepreneurship – helping early-stage bioscience companies around the state. They recruited 6 successful executives, selected for their experience as founders and executives of early-stage bioscience companies and their ability to help these early-stage companies get off the ground, to provide not only business assistance services but also capital, to effectively de-risk investments. And the goal always is to take a product to market where you can raise additional private funding.

Private Funding – Kansas is known as a “fly-over” state. There was zero venture capital investment in 2004 when KBA was formed. To date, what we have figured out is that the KBA making direct equity investments does make sense, and also makes sense to recruit venture investors into Kansas. We have invested in three venture capital funds and the stipulation of their investment in those 3 funds is they must locate in Kansas. An example is MPM Capital, the largest life sciences venture fund in the world, started in Boston, opened an office in San Francisco, and a third office in Kansas City, Kansas in the old Ronald McDonald House near the KU Med Center. KBA has invested \$20M in those funds and to date those 3 funds have already invested \$23.3 back into Kansas bioscience companies.

Centers of Innovation – the program is intended to link extraordinary research and development capabilities, equipment, and other support that might be imbedded inside a research institution to link that with bioscience companies. They have funded to date, three: bioenergy, biomaterials and plant biology. An example of this he uses in his presentation, is Centers of Innovation (CIBOR). They have committed \$4M and paid that out to date. An additional \$1.5M was recently approved by their Board of Directors. He spoke of some of their staff, their priorities and their partners, which were listed on page 39 and for KBA's funding for CIBOR, found on page 40. Page 41 lists the progress of CIBOR.

Expansions – found on page 42, he listed expansions throughout the state along with their projected capital expenditures. He mentioned for instance, Cargill meat Solutions in Wichita which he indicated was a retention, in that they could have moved back to its world headquarters in Minneapolis but chose to stay in the state, in that region, and formed a partnership with KBA.

Financial – State authorized funds as a reminder is \$581.8M, and to date they have committed \$243.6M; of the \$581M. They have received \$175.1M and the commitment remaining to be paid is \$171.8M. He also offered various charts that accompany his presentation as it relates to graphical depictions of those numbers found on pages 46 and 47.

A copy of the two booklets he referred to at the beginning of this overview, and a booklet entitled “Advancing Kansas' National Bioscience Leadership”, which was also part of his testimony, are (Attachment 1) attached and incorporated into the Minutes as referenced.

The Chair thanked Mr. Thornton and said the Committee is going to have a number of questions here about how the KBA is spending Kansas taxpayers dollars. She went on to say they have had people come forth all the time saying a return on your investment is this, this, and this. That is why the Governor is trying to develop a board to evaluate every agency by the same standards, so we really do know what our return is on the investments. This is an incredible investment that Kansas has made that we want spent to grow Kansas. And when you have little projects from Kansas investors, who have come before you for investments and they are not getting funded, then those projects come to us and they say what is going on up there, so this is why they are asking these questions.

Chairperson Wagle began questions including:

1.) Referring Mr. Thornton to the booklet that listed the Board of Directors information. She thought he explained to her, before you make an investment, the question goes before a subcommittee of the Board, and asked, can you explain to my Committee who is on that subcommittee that determines your investments? (Chaired by Dr. Ray Smilor and additional members on it would be David Franz, Bill Sanford, Dan Watkins, and there is a vacancy currently.) Is Mr. John Carlin on this subcommittee? (As Chairman, he serves as Ex-officio.) Is Ray Smilor from Kansas? (He is head of an entrepreneurial program at Texas Christian University.) Is Bill Sanford from Kansas? (His official residence is in Naples, Florida, he runs a company here in Kansas.) And David Franz? (He is from Maryland.) And Dan Watkins lives here? (Yes.) I believe Governor John Carlin has an apartment in Manhattan. Does he consider that his legal address? (Yes.) Does the 5-member subcommittee include the Chairman? (Yes.)

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2.) Does the Board typically adopt the recommendations of this investment committee? (Safe to say for the vast majority of investments, yes that is the case. There has been some examples where that it has not been the case because of questions raised, or concerns, or more work needs to be done. And I might add, even before it goes to the committee, they do not always adopt the recommendations of the staff.)

3.) Regarding your building, there are legislators who helped create the KBA and they say no where in the legislation did we say they could build bricks and mortar, what they wanted is investment and projects. So we have a building and it appears you are spending \$279 a square foot. These are our tax dollars, so can you explain why it is so expensive? (The building itself that you are referring to is the venture accelerator, it is in Olathe, Kansas. It is part of the project that KBA introduced to the City of Olathe with KSU and KBA. The City of Olathe donated 100 acres to KBA and KSU, 60% of that land is managed by the Bioscience Authority and 40% by KSU. The KBA piece is more directed towards commercialization.

The first element of the agreement was that the Bioscience Authority would move into the Kansas Bioscience Park and develop a bioscience incubator. As it relates to the building itself, it is an incubator, two-thirds of the building will be used effectively for tenants, specifically bioscience companies that require wet lab space which is canned heat and expensive to build.

He offered to turn to the gentleman who is managing the project for them who could give the Committee exact comparables, but the figure, the \$279, is comparable to wet lab space and bioscience incubators, not just here in the state Kansas but in other parts of the country. In terms of wet lab space, bioscience space is not like IT space. They do require exotic gases, fume hoods, certain types of equipment and the ready ability or that kind of space to facilitate the expansion of a company with the attraction of the state of Kansas is important.)

4.) Are you going to have contracts for the Lab? (We have initiated our marketing efforts in the last month and a half, in hiring Christine Murray here and have one tenant to date and our goal when we go into the building in June is to have that building over 50% loaded with tenants. Today we believe the total is 528 feet that has been leased, just percentage wise is 1,700 square feet lease out is 12K.) So you have 12K square feet of the building, and 1,700 has been leased, so referring to the pictures in tab 5, we have a small tenant office and a small office and if you are investing in a venture capital investment, you said the requirement, for those who "invest in that top financing," would be to have an office in the state of Kansas? (Yes.) Would it qualify, I know you are giving 6 or 8 \$5M grants to venture capital? (We have done exactly 3.) Your plan would be? (Our plan would be somewhere around 6.) Are all of these outside Kansas? (They must, as a requirement, have an office in Kansas) Could they rent a small office and meet your requirements? (It is unlikely that would be the case for several reasons, but the short answer would be no, and let me give you an example of MPM. MPM did not rent an office, they bought a building, a \$1.25M building and renovated it. It is more likely they do that. Why? The bigger issue there is, this is about investment opportunities in the State of Kansas and not sitting in a small office.)

The Chair recognized Senator Masterson who stated he had some questions of his own and a few questions from people who asked him to ask, including:

1.) Regarding being ranked number 5, what were the metrics that created this? Senator Masterson said he was provided another manual entitled from Batel, where we showed a much lower ranking, so want to make sure this is something that actually depicts what Kansas is doing. (First off, if you dig into it, you will realize that the Business Facilities Magazine does the ranking. The extent to which they use data, they also use data associated with things that wouldn't necessarily be in BATEL. So for example, it mentions prominently the NBAF.) Do you have any details on the matrix? (Yes, and if you don't mind, I will provide that data, not just for the Business Facilities magazine but also for the BATEL report.) I am trying to find the business magazine, it appears it is a paid subscription magazine. (I understand.) Chairperson Wagle asked, is that magazine subscription based, or is it a free magazine? (I would assume it is a free magazine.)

2.) Senator Masterson then asked, how many eminent scholars have we attracted? (One at WSU, one eminent scholar for animal disease at KSU, and then at the University of Kansas, I believe 7. There have been two rising stars in addition to that at the University of Kansas and there is a cluster hire there as well, and believes there were 3 researchers associated with that cluster hire.) How do we agree to engage

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contractually with them as far as money invested? (If you don't mind, there are three questions in that one question. Individuals that pursue federal research development grants or contracts, either through the foundation or the federal government, tend to get them as individuals and they are called principal investigators and as PIs. so to speak, the grants follow them. The second thing is the organization that does the recruiting is not KBA it is the University of Kansas. We actually vet to a third party evaluation process. Are they, in fact, the kind of researchers that will make a big difference here in our state? The third is with our contracts through our academic institutions, if the PI leaves the state of Kansas, the Bioscience Authority is going to stop, period.)

3.) Re: Commercialization and jobs, has there been technologies that we have been responsible for commercializing, yet and do we have examples of those commercialized technologies? (Do you mean for the eminent scholars?) No, for just the KBA in general. (Yes, a great many numbers, a wheel chair company struggling for early-stage capital, \$75K proof of consent grant, brought in a CEO, developed a clear marketing plan for the company, and they are out there using that marketing plan, hiring individuals to implement that. Also, KC Bio Medics, and some of these are in the book by the way, and In Space in Manhattan.) Mr. Thornton did explain KC Bio Medics. Senator Masterson went on to ask, could you also give me a list of technologies KBA is responsible for commercializing and I would also be curious about the validating of jobs, which jobs have been created, and get a base line for some of that?

3.) Going back to venture capital, some of the perception I am getting feedback on, is with these dollars going to venture capital, and I understand they have to put an office here in Kansas, but some of the appearances that KBA is giving taxpayer money to seize another income for the Authority. We put money out so the Authority gets the return on those capital investments and creates a secondary funding screen, how can you respond to that? (That is most definitely not our intent. Our intent is to address access to early-stage capital. Some have overcome and some have failed infamously. If you don't mind I will use a few examples that this might be helpful and I also, if you don't mind, will provide a report that reviews the various state venture capital initiatives and highlights successes and failures which may be instructive for the Committee. First is, bioscience companies are different. They do require a substantial amount of financing. The second part is we don't want to just recruit venture investors who had an MBA behind their name. We wanted to recruit the best we possibly could. Open Prairie and Cultivian are organizations with extraordinary backgrounds and extraordinary returns. And yes we do expect a return on these funds, we would not have selected them if we didn't expect a return.)

Have you seen any investments that have gone belly-up or bankrupt and have you had any that have succeeded and showed return on investment up to this point? (Inside the KBA's portfolio, one company has, it is Innovia. None of the funds have been bankrupt, it's too early though, they really just initiated those investments.)

The Chair recognized Senator Longbine who stated he would encourage KBA to look statewide for projects, KU, KSU, WSU seem to get a lot of attention in the research institutions and understandably so, but thinks it is also important to realize there are regional universities that may not be suitable for eminent scholars but certainly there are some rising stars located in those regional companies that are entrepreneur in nature that are trying to grow. Just a comment, would encourage you to look outside the KC, Wichita, Manhattan area and see if there are additional opportunities. (I appreciate that and we look forward to engaging other economic investment partners, specifically the DOC, but also regional economic development organizations as well. They can be eyes and ears for potential investment opportunities for the Authority.)

The Chair recognized Senator Lynn who asked regarding eminent scholars, what does it take to get somebody like the gentleman that was recruited a couple of years ago from Penn State, what was the package, as I recall that package was over \$1M ? (Yes, I am not finding it here right now and I will most definitely provide you with packages of all of these individuals.) We wait a long time for that research to come back to pay back what we are investing in.) We have done a 7.5% pay cut for state officers, and some of our economic development executives are making five times more. Regarding the people on the Board who are probably well educated people, we have to pay them. We have to pay you. What are salaries looking like for corporate officers? In your budget in terms of staff, what are their salaries? I would think the Committee would be interested in this, in full transparency. I am looking at your

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corporate officers and then at your operational costs. (Mr. Thornton referred them to tab 3, past the turquoise sheet, second page, the total wages and benefits of \$2,572,505.) The Chair asked for a breakdown, saying it appears wages doubled.

She went on to say, there is concern with KBA putting money in a building instead of investing in Kansas. (He feels the building is a precondition to housing these companies.) Don't our universities have wet labs? (Private companies can't use those facilities.)

The Chair then called on Senator Steineger who asked:

1.) With regard to the buildings, who are the architects and how much have they been paid? Any engineering company and how much have they been paid? Any kind of professional services, I want who they are and what they got paid to date.

2.) In looking at page 2, KBA operative expenses, contractual consulting services, you have 2 line items, one for \$511K and one for \$630K and would like to know who and how much, not just a company name like MGM, who is MGM? The same with Marketing, expenses show \$444K, who is it, a company name and an individual name?

3.) And meeting and travel expenditures I think the Committee would like to see what kind of meetings you are going to and where are they at? He cited when we travel, and he doesn't anymore because the Legislature cut our travel expenses, but when they do, they have to turn in a public report showing literally to the penny, hotel & dining expenses, airfare, taxi, and how much do we have to pay people to operate a business?

Chairperson Wagle stated she thinks there is concern beyond this morning, in that, where in this Legislation are you authorized to leave the state? As it was going on 9:30 a.m., the Chair asked Mr. Thornton if he could come another day, maybe after turn-around? (Yes.)

Adjournment

The meeting was adjourned at 9:31 a.m. The next meeting is scheduled for February 16, 2011.