

TRANSCRIPT OF GOVERNOR LINDA LINGLE'S TESTIMONY

Before the

SENATE COMMITTEE ON ECONOMIC DEVELOPMENT & TAXATION

January 30, 2007

SB 1365 – RELATING TO THE INNOVATION ECONOMY

Thank you very much, Chair Fukunaga, Vice Chair Espero, Senator Slom.

As you know, I have outlined an innovation initiative that has a variety of components. They're contained in four specific bills that are going to be considered during the legislative session.

This morning, the first bill on innovation in workforce development was taken up and passed out of committee. Tomorrow, we will have the innovation in education bill be taken up.

This one is certainly an important one and touches on a number of different issues. But they all are focused on the same thing, and that is: How do we raise the standard of living of all the people in our state while decreasing an over reliance on land development as a foundation of our economy? And how do we do it while maintaining our cultural lifestyle here in Hawai'i?

We have taken a position that it is through innovation that we will be able to achieve all these things, and innovation all across the economy is what we are focused on. Not innovation in, simply, new kinds of industries – not only new technologies, not only life sciences or marine science or optics or any one field, but innovation as a concept across the entire economy. Because it's through innovation that our existing industries will increase productivity and create higher-paying jobs.

This bill that's before you is an integrated, comprehensive plan that we feel is important to consider as a whole. I know there's always a temptation to pick and choose components of any particular proposal, legislative or otherwise, but I feel the amount of work that has gone into this from departments throughout the government, but also from the private sector, has really created a comprehensive, broadly-based approach. This particular bill has six critical components that I'd like to speak briefly about. Let me list them first, and then go one by one.

First of all, the total cost of this bill is just over \$5.7 million, and that's part of a \$30 million two-year proposal – the \$5.7 million is over a two-year period. So I feel that it is an extremely modest proposal in relationship to the ultimate benefit, and in relationship to the existing size of our general fund budget.

The six components of this bill include: the establishment of a Hawai'i Innovation Investment Fund; investing in the Technology Incubator Innovation Center that's being planned by Kamehameha Schools in Kaka'ako; the creation of a digital media center facility in order to expand the industry from one that has served too often as just a backlot for Hollywood bringing the broader-based industry here; the MELE Program – Music, Enterprise and Learning

Experience partnership between Honolulu Community College and Belmont University. The fifth component is to enhance the UH's Office of Technology Transfer and Economic Development in order to expand its ability to commercialize the research that's going on at the university. And sixth, and very importantly, a program to accurately measure the effectiveness of the overall Innovation Initiative.

I want to start with the creation of the Hawai'i Innovation Investment Fund because I think it's the most misunderstood of the six components, based on what I've heard so far since it's been proposed. And the one where there's information that's come out from a variety of sources that I don't feel is accurate. And again, I will touch on each of the six components in a brief way. We have others, including Director Liu, who will speak in more detail about the different proposals.

The creation of the Hawai'i Innovation Investment Fund (HIIF) is important because we have many companies in our state who reach the verge of profitability only to leave because they can't get the kind of financing that they need to grow.

This investment fund is envisioned to be a professionally-managed what is known as a "fund of funds." So this fund will, in fact, invest in other venture capital funds that invest in technology and creative industry companies here in our state. We also encourage the State Retirement System in this bill, as well as private investors, to invest in the Innovation Investment Fund. And we ask the retirement system to allocate \$100 million for Hawai'i venture capital investments, some of which may be made in whole or by in part through the HIIF.

The \$100 million that we are asking them to allocate for investments in venture capital funds in our state is less than 1% of the assets of the retirement system, which is now at about \$10.5 billion. It's the largest institutional investor in the State of Hawai'i, and yet invests literally nothing in our startup companies.

It is ironic that I was at a luncheon the other day in Kona with the head of a company there who was doing landmark research and now development of renewable energy using the macadamia nut husks, and they had the total financing for their project, and the financing came through the California State Employees Retirement System. California, Oregon, Pennsylvania and other states have moved very successfully to allocate some of their investments to these kinds of companies or funds in their own state, and they are realizing good returns.

And that's an important point to make because the misinformation that's out there, and partly it's just because people haven't read the proposal or really don't understand it completely – but a key bit of misinformation out there is that we are raiding the State Retirement System.

That is completely false – there is no money being taken out of the State Retirement System. Rather, it is a requirement to allocate the \$100 million, or less than 1% of their assets, to be invested in Hawai'i venture capital investments.

In addition to that requirement in the bill, we remove from the fiduciaries of the State Retirement System the liability because of investment in these venture capital funds. Some people don't think that's necessary; we're just doing it as an added incentive to make certain there's no reason or excuse not to move forward with this proposal.

Also, for investors in the Hawai'i Innovation Investment Fund – which may be not just the Hawai'i Retirement System, it may be others invested in this fund – this would exempt all taxpaying investors from state income tax and franchise taxes on their returns.

The fund will be overseen by a seven-member board, made up of four from the business community, one from the Retirement System, one from the Department of Budget and Finance and one from DBEDT.

So again, we think this fund, its creation and funding others is important to those companies that are on the verge of profitability to expand and not have to leave the state because they can't get financing. It would also increase the experience that exists here in venture capital funding and venture-type firms that could exist in a much greater degree.

Second of the six components is the state's investment in the partnership for the Technology Incubator and Innovation Center in Kaka'ako at the site of the old Honolulu Ford. It's about a five-acre site; it's planned as a three-phase development of 400,000 square feet. It would supply both wet lab space for life sciences, bioscience research, and also incubation space for other companies.

The arrangement that is being discussed with Kamehameha Schools is for a 10-year lease, 99,000 square feet. It would be between our High Technology Development Corporation (HTDC). The HTDC would provide a state guarantee, basically, of its 10-year lease for this space. We would then, in turn, HTDC would lease this space out in order to reduce the risk, the cost, of this very unique and important project. We are proposing that we pay the difference the financing costs and what we realize in the rents, and we have pegged that at about \$250,000 per year. We think its money well spent, a good investment, and its location by the medical school is important and, we believe, will provide an important boost to the life science industry.

The third component is a digital media incubator facility. As you know we've invested millions of dollars in film and television productions in the state. Millions of dollars as tax credits, through the building and then major, multi-million dollar renovations of Diamond Head Studio, the funding for the creative media program at the University of Hawai'i. All important components of an eventful industry but an important part of that that's missing – the vision of really having an industry here – is a facility, a mixed-use facility that would combine industry, government and academic entities.

In our vision, it would be DBEDT, in coordination with the University of Hawai'i, to oversee the leasing, operation and maintenance of such a facility. The kinds of work that we see being done

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there, besides the critical television and feature film, is digital visual effects, the pre- and post-production work for a feature film, the interactive video game development, computer animation, creative software design, and dynamic Web design and distribution.

The next component, and I admit to you the most exciting to me, is MELE, and it stands for Music and Enterprise Learning Experience. It's so exciting to me because I feel it's such a natural for us. As you know, the City of Nashville has created an entire industry built around two things: their distinctive music and their unique lifestyle – country lifestyle, southern/country lifestyle.

Well we have a very distinctive music, as evidenced by us having our own category now at the Grammy Awards in 2005, but we also have a very unique culture. And the visionary work being done by the Honolulu Community College to recognize this and to take the initiative to develop a partnership with Belmont University of Nashville is something we should not let pass us by.

This is an issue that has lingered for decades in our state, because we have this huge abundance of musical talent in the state. How do we leverage that to actually help our artists to be more successful and in the process create an industry? I certainly think over time it could rival the size and the importance of the Nashville sound.

This relationship with Belmont is an important one because they would collaborate with HCC on the joint use of their curriculum, technical facilities and equipment specifications, the training of faculty, dual-credit courses and internships. And what this program would be and what we're asking for is the money for the support of this program, and also for a facility, so that our musical artists could be a real industry here.

And the community college envisioned this program centering around three specific areas – the artistic creativity, the entertainment expertise and the technical production skills. HCC would award an associate's degree in music business, and those credits would be transferable to Belmont (*indistinguishable*) and the master's program as well.

Everyone who I've talked with in the music industry, the business, musicians as individuals are very, very excited about this – this focus on them and what they do and what they bring to our lives as residents, to our economy, to the visitor industry, to movies, and to have this focus on the importance of what they do for us is very exciting to all of them as well.

The next part of the package has to do with a little-known office, little-known to the general public, at the University of Hawai'i. The office is called the Office of Technology Transfer and Economic Development (OTTED). OTTED has the responsibility to the state to help to commercialize the important research that's been going on at the university.—

*Recording ended

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