

MINUTES OF THE SENATE COMMERCE COMMITTEE

The meeting was called to order by Chairperson Karin Brownlee at 8:30 a.m. on January 22, 2004 in Room 123-S of the Capitol.

All members were present.

Committee staff present:

Kathie Sparks, Legislative Research
Susan Kanarr, Legislative Research
Helen Pedigo, Revisor of Statutes
Nikki Kraus, Committee Secretary

Conferees appearing before the committee:

Tracy Taylor, KTEC
Jerry Lonergan, President, Kansas Inc.

Others attending:

See Attached List.

Mr. Taylor presented the committee with the Kansas Technology Enterprise Corporation update for January 2004 (Attachment 1). The three main areas of focus for KTEC are research, business assistance, and investments. The "3 C's" of KTEC are *Collaboration*, referring to its efforts to work with the state, universities, and private foundations, *Commercialization*, referring to innovation centers and the Centers of Excellence, and *Capital*, through capital formation companies, InvestMidwest, and local incubator seed funds. Mr. Taylor went on to outline several ongoing projects and explained the continuing efforts of KTEC to facilitate technology-based economic development in the state.

Mr. Taylor discussed additional details of funding procedures with the committee, as well as combined efforts with Kansas State University. Mr. Taylor also outlined partnerships with larger companies' product development and marketing departments, including an upcoming dairy product that could be offered as an alternative vending machine product to traditional pop and unhealthy snacks.

Mr. Taylor stated that through reinvestment in the program, there has been great progress, and he was confident it would continue.

Mr. Lonergan presented an "Informational Update on Kansas, Inc." (Attachment 2). In this, he outlined the creation and purpose of Kansas, Inc., summarizing to three main points: conducting research and develop policies geared to position Kansas to be competitive for economic growth; develop, monitor, and update the state's strategic plan for economic development; and evaluate economic development programs. Mr. Lonergan outlined the research prospects for calendar year 2004 and fiscal year 2005 through both external research programs (the economy of an aging population, bioscience collaboration, and entrepreneurship among others), internal research programs (impacts/performances of state economic development programs, coal-bed methane economic impacts, and workforce demographics, among others), and collaborative Kansas Inc.-Legislative efforts such as benefit-cost analysis of tax incentives.

In response to the committee, Mr. Lonergan stated that anytime a state raised taxes, it would be less competitive, but that there needed to be a balance that was fair in order to provide valuable services.

The committee discussed the value of "whole racing" to the state, a topic which includes everything from dogs and horses to automobiles to bicycle and track events.

Senator Barone referred to an article published by Karl Peterjohn that stated Kansas has the highest property taxes. Mr. Lonergan stated that while taxes were certainly very important, it was necessary to consider whole business cost, including factors like land values, wages, and many other factors.

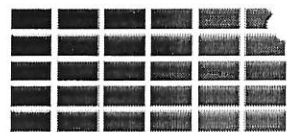
Mr. Lonergan referred to a business cost tax study currently underway, and the Chair stated that the committee would like to see that whenever it might become available.

CONTINUATION SHEET

MINUTES OF THE SENATE COMMERCE COMMITTEE at 8:30 a.m. on January 22, 2004 in Room 123-S of the Capitol.

The meeting adjourned at 9:30 a.m. The next meeting will be at 8:30 a.m. on January 23, 2004 in Room 123-S of the Capitol.

Tracy
Taylor



KTEC

**KANSAS
TECHNOLOGY
ENTERPRISE
CORPORATION**

KTEC Update
January 2004

Tracy Taylor

Sen Commerce
01/22/04
Attach #1

Senate Commerce
01/22/04
Attach #1

KTEC Areas of Focus

Research

Centers of Excellence

- HBC, *Univ. of Kansas*
- ITTC, *Univ. of Kansas*
- NIAR, *Wichita St. Univ.*
- AMI, *Kansas St. Univ.*
- KPRC, *Pittsburg St. Univ.*

Experimental Program to Stimulate Competitive Research (EPSCoR)

Small Business Innovation Research (SBIR) assistance

Business Assistance

Incubators

- MACC, *Manhattan*
- LRTC, *Lawrence*
- ECJC, *Lenexa*
- KUMCRI, *Kansas City*
- ATC, *Pittsburg*
- WTC, *Wichita*
- WKTC, *Great Bend*
- Quest, *Hutchinson*

Mid-America Manufacturing Technology Center (MAMTC)

National Institute for Strategic Technology Acquisition & Commercialization (NISTAC)

Investments

Applied Research Matching Fund (ARMF)

Technology Commercialization Seed Fund (TCSF)

KTEC Incubator Seed Funds

- Manhattan Holdings (MACC)
- Kaw Holdings (LRTC)
- Wichita Ventures (WTC)
- Prairie Investments (ECJC)
- Precede Fund (KUMCRI)
- Quest Ventures (Quest)
- Milestone Ventures (ATC)

Results Via The 3 C's

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- **Collaboration**

- KDOC / Legislature / Administration
- Stowers and Kauffman Foundations
- Kansas State, Univ. of Kansas, Pittsburg State and Wichita State
- Federal government – EDA, Department of Commerce

- **Commercialization**

- Innovation Centers/Incubators (eight locations throughout state)
- Centers of Excellence

- **Capital**

- Capital Formation Companies
- InvestMidwest
- Local incubator seed funds, KTEC Holdings Inc. and KTEC investment programs (ARMF and TCSF)

Technology-Based Economic Development Initiatives

h-1

So What?

- Emerging entrepreneurial growth companies are responsible for 67% of new jobs (more in economic downturns) and 95% of all radical innovations since WWII *
- Created 2/3 of all net new jobs in the '90s *
- Jobs created by tech companies pay about \$50,000 – two times the average salary of non-technology jobs (approx. \$26,000)
- Reduces brain drain
- Diversifies tax base
- A region's economic prosperity is closely tied to its entrepreneurial capacity *
- Entrepreneurial companies seek talent, capital, networks and infrastructure *

* National Commission on Entrepreneurship, 2001

Life Sciences Initiative

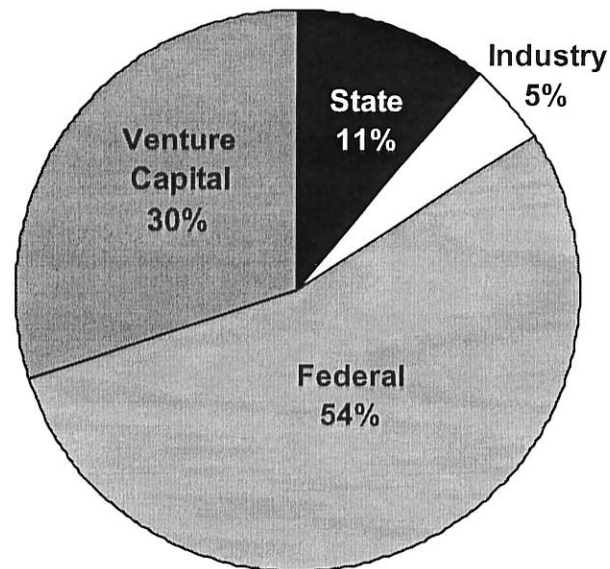
- Kauffman and Stowers foundations (collectively worth about \$5B)
 - Focused on life science and entrepreneurial habitat
- Government research funding focused on IT, life sciences and nanotechnology

KTEC Cumulative Results

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- \$1.22 billion in increased sales
 - 13,778 jobs created or retained
 - 371 company start-ups
 - 633 technologies developed
- 273 patents issued
- \$6.93 million in royalties received
- \$4.37 million in equity returns

FY 2003 Percent of Total Investment



**Total FY 2003 investment:
\$97.9 million**

Leverage: \$8.1:1

Staff Reductions

1-6

KTEC FTE Issue

FY03	19
FY04	12

Annual KTEC Salary & Wage Cuts

FY04: \$327,745

National Institute for Strategic Technology Acquisition & Commercialization

1-7

- Jointly sponsored by KTEC, Kansas State University, the KSU Foundation and Mid-America Commercialization Corporation, a KTEC incubator
- Leads the nation in acquisition and management of patent donations
- Portfolio includes nearly 600 patents in more than 30 fields of technology



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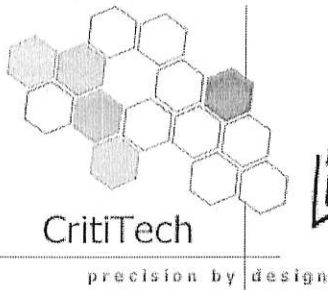
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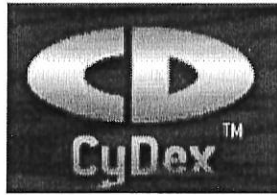
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KTEC Client Companies

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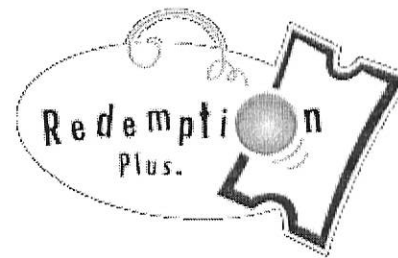
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Representative Client: Deciphera Pharmaceuticals

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- Founded by Dan Flynn and Peter Petillo
- Located in Lawrence
- Targets cell proteins to develop drugs to treat up to 200 diseases, including Alzheimer's and cancer
- KTEC invested \$200,000 in seed round
- Recently completed \$15 million round of funding from private, Kansas-based investors
- Has created 8 Kansas jobs. Expects to employ 35 people by 2006 at average salary of \$90,000
- Received assistance from Lawrence Regional Technology Center, a KTEC incubator

Representative Client: NanoScale Materials

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1-10

- Located in Manhattan
- Produces a line of reactive nanoparticle materials that improve chemical reactivity, called NanoActive materials.
- Has created 30 Kansas jobs.
- NanoActive materials have diverse applications for commercial and military use.
- KTEC invested \$200,000 in seed round
- Has been assisted by Mid-America Commercialization Corporation, a KTEC incubator in Manhattan.

Representative Client: NutriJoy

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- Based in Manhattan
- Developed a technology donated by Procter & Gamble that allows calcium to stay suspended in a fruit-based beverage.
- Has created 11 Kansas jobs.
- Has inked deals with many school districts, Nissan Motor Corp. and the Food & Drug Administration to install technology.
- KTEC invested \$200,000
- Received investment from Cargill Ventures
- Valued at \$6M

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Investment Process

- KTEC receives business plans on a continual basis
 - Web site, Networking, Referrals, Unsolicited, Previous Investment
- KTEC staff charged with reviewing plans, performing due diligence, investment analysis, market research and analysis, deal negotiation, and portfolio management
- Investment committee meets quarterly to review company presentations and vote recommendations to KTEC Board
 - All Committee are private sector volunteer members and have investment and/or entrepreneurial experience
- KTEC Board finalizes recommendations

Common Thread Success Factors

1988 - 2003

- Focus on the overall strength and weakness of the management team
- Assess ability and need to attract to follow-on investment capital
- Thorough due diligence to assess technology, market, and management team
- Assess previous and future intellectual property
- Comprehensive post-deal portfolio management
- Favorable terms for Kansas that also ensure company positioned for follow-on

Investment Trends

1991 - 1999

- KTEC invested total of \$9,685,301
- Funded 258 unique projects/companies.
- All investments were under Royalty agreements
- Total royalties returned \$1,728,170
- All investments were project based at the proof-of-concept or product development stage
- Continued focus on project potential and some assessment of management capability.

(KTEC started exercising new investment structures, i.e. equity, convertible debenture in early 2000.)

Investment Trends

2000 – June 2003

- Since 2000 KTEC invested \$3,347,210.
- A total of 47 companies
- Avg size of investment: **\$71,217** (An increase of **89%** from 1991-1999 period, where the avg investment size was **\$37,539**)
- Avg # of deals per year: **12** (A decrease of **130%** from 1991-1999 period, where the aver # of deals per year was **28**)
- More focus on the management team and company potential (versus inventor and project).
- All of the investments made in this period are still **active**.
- Out of 47 investments 5 were royalty investments, the rest were either equity or a variation.

Investment Trends

2000 – June 2003

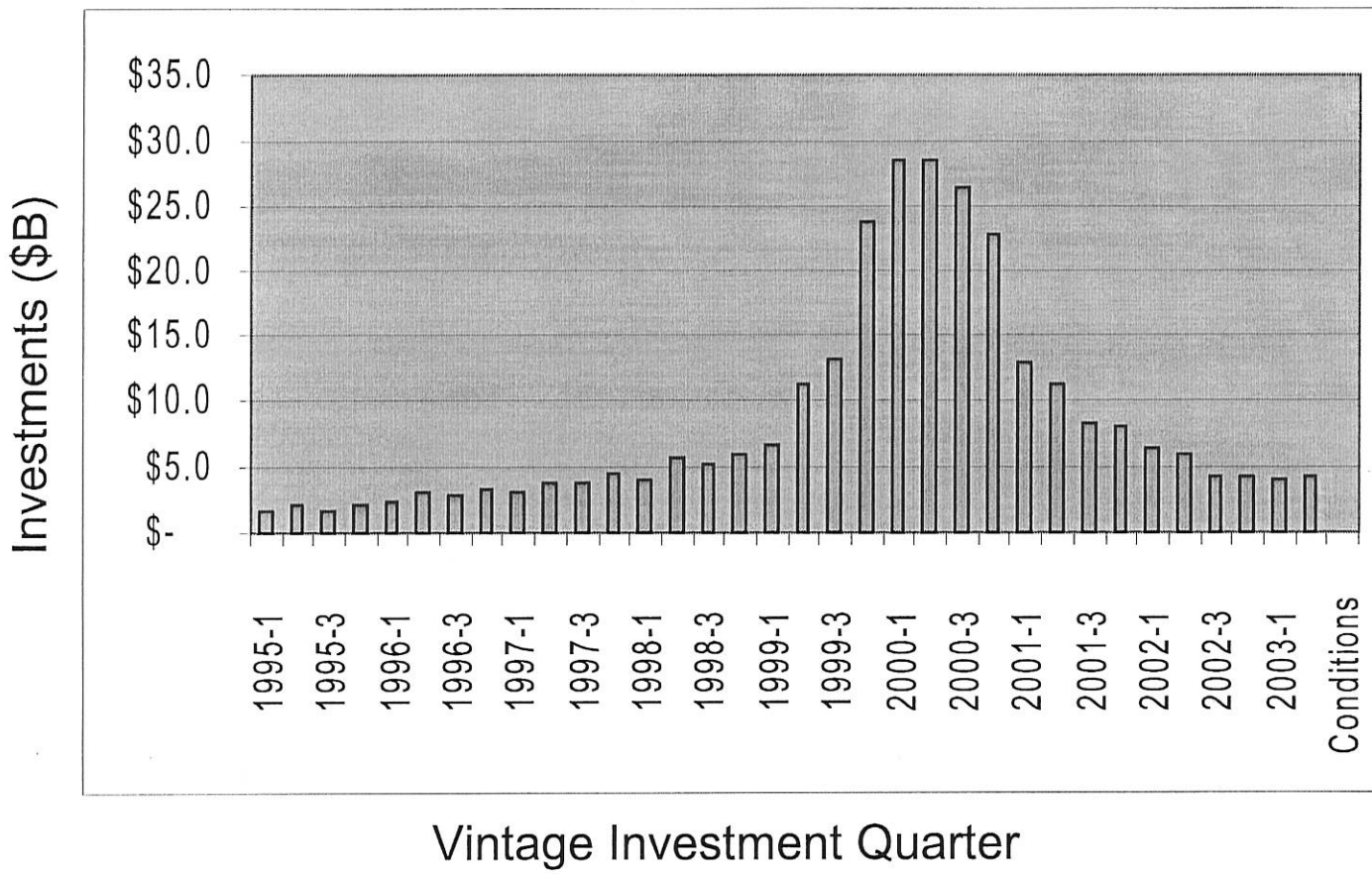
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- KTEC implemented new Technology Commercialization Seed Fund (TCSF)
 - Investments up to \$250,000
- Increased focus on disruptive innovations
- Capital formation in Kansas
- Interaction with company on a continual basis
 - Board observer position
- Requirement of a defined exit strategy
- Job creation and wealth creation
- Angel investment activity has increased

PWC MoneyTree Historical Trend (National Data)

1-17



- Highlights:**
- 1996: \$12B**
 - 1999: \$55B**
 - 2000: \$106B**
 - 2001: \$41B**
 - 2002: \$21B**



Source: National Venture Capital Assoc., PricewaterhouseCoopers Private Equity & Venture Capital Practice, Thomson Venture Economics

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Kansas Inc. Testimony
Jerry Lonergan, President
Senate Commerce Committee
January 22, 2004
Information Update on Kansas Inc.

Thank you, Senator and good morning members of the committee.

My name is Jerry Lonergan; in September of last year I accepted an invitation from the board of directors to become the fourth President of Kansas Inc. and welcome this opportunity to provide an information update on the organization.

Kansas Inc. was created as part of a set of economic development initiatives in the late 1980's. Its statutorily responsibilities have evolved to the point where they can be summed as follows:

1. Conduct research and develop policies geared to position Kansas to be competitive for economic growth;
2. Develop, monitor, and update the state's strategic plan for economic development; and
3. Evaluate economic development programs.

Recently, beyond conducting an update of the state's strategic plan, Kansas Inc. has not been particularly active and engaged in the policy arena. There are good reasons for the Legislature and Kansans to expect that to change.

- A revitalized and engaged board of directors including the active presence of both the Senate President and Minority Leader on the board;
- The Governor's office has communicated with me regularly and positively and is in the process of filling current board vacancies to insure a full board is in place;
- For the first time in quite a while there is great communication with and a strong cooperative working relationship among Kansas Inc., Kansas Technology Enterprise Corporation, and the Kansas Department of Commerce – and a commitment from leadership of those three agencies to work together as originally envisioned; and,
- As president, besides being the first born and raised Kansan in this role, I bring a proven and successful background in operating a statewide research organization that also leveraged dollars and created a multi-million dollar research portfolio (at the Kansas Electric Utilities Research Program).

I also feel our growing credibility has been recognized with the invitation from Lee Allison chair of the State Energy Resources Coordinating Council for me to serve as co-chair of the Wind Prairie Task Force which seeks to serve an advisory role to help communities and wind developers find ways to: 1) preserve a valuable and unique land infrastructure while 2) bringing economic development and jobs to rural Kansas.

Since September the focus has been – preparing the Kansas Inc. annual report for submission on October 1; completing an update of the regional comparison of state business cost and taxes in Kansas; establishing, and in some cases re-establishing, contact throughout the state with the business community, institutes of higher education, and other organizations; and, using those contacts and in-person individual visits with each member of the Kansas Inc. board of directors developing a research agenda for 2004 and Fiscal Year 2005.

Given a short time frame the agenda was developed primarily based on interviews with board members and a select set of professionals throughout the state. Additionally, the strategic plan, as well as other relevant literature, was reviewed to insure issues identified in that document are incorporated in this plan.

Future agendas will be developed with broader input, including a planned technical advisory group to the board, comprised of research professionals.

As presented to the board of directors in December, the agenda is not a list of projects fixed in stone that comprise the only things we are going to look at. But rather its purpose is to alert the research community, potential funding partners, and all interested Kansans in topic areas identified as important to the state's economic future.

To be an effective research organization, Kansas Inc. must be responsive to unanticipated issues that surface and flexible to needs of the Legislature, businesses and communities.

The agenda was presented to the Kansas Inc. board this last Thursday and I am proceeding now with efforts to find funding support and to initiate these projects.

Presented first are external research projects that will require additional outside funding and will most likely be conducted in partnership with other research organizations. The internal projects listed will use in-house staff at Kansas Inc. and there is also proposed a Legislature/Kansas Inc. cooperative project which, as I understand, has been discussed in the past.

I will not discuss each individual project but highlight just a couple and then answer questions committee members may have about the proposed projects.

We are in the process of editing a short "prospectus" which will provide an overview of each topic area. That document should be completed next week and will be distributed to Legislators among others. It will serve as our outreach to the business, foundations, and grant community to begin seeking funding support and communicate our program of research.

Kansas Inc. Research Prospectus
Calendar Year 2004 and Fiscal Year 2005

EXTERNAL RESEARCH PROGRAM

1. The Economy of an Aging Population: *Taking Advantage of a State Resource*
2. Agriculture Commodities Future: *Assessment of Competitive Threats to a Critical Component of the Kansas Economy*
3. Bioscience Collaboration: *The Economy of Tomorrow*
4. Entrepreneurship: *Understanding the Challenges, Assessing the Potential*
5. Healthcare: *Realistic Policy Options to Address Selected Issues*
6. Racing Industry: *Fastest and Best Foot Forward*

Internal Research Program

1. Impacts/Performance of the State Economic Development Programs
2. Coal-Bed Methane Economic Impacts
3. Economic Development Legislative Actions in Other States
4. Kansas, Inc Staff Skill Development
5. Local Employment Trends
6. Venture Capital/Business Finance Primer
7. Workforce Demographics

Collaborative Kansas Inc. and Legislature

1. Benefit-Cost Analysis - Tax Incentives

My hope is we have developed a research agenda that is proactive, challenging, interesting, and ultimately a valuable input to identifying policies and options available to Kansas to insure a dynamic economic future.

Thank you.