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Senate Bill 358 (Substitute S-1 as passed by the Senate)
Senate Bill 359 (Substitute S-1 as originally passed by the Senate)
Sponsor: Senator Bill Hardiman (S.B. 358)
Senator Valde Garcia (S.B. 359)
Committee: Commerce and Labor

Date Completed: 7-27-05

RATIONALE

Many people believe that a key element in fostering economic development and job creation is the availability of capital investment in early-stage small businesses, particularly high-risk, technology-based ventures such as the development of pharmaceuticals and medical equipment and devices. This life-science sector has grown dramatically in Michigan in recent years, with over \$2 billion invested in research and development each year and nearly 100 new companies since 2000, according to the Michigan Economic Development Corporation (MEDC). The MEDC also reports that the growth of Michigan's life sciences industry has exceeded that of the U.S. average, growing 27% in employment (with nearly 38,000 employees), 32% in the number of companies (over 540), and 165% in sales (\$4.8 billion). Job growth in the life-science sector also is considered important to the broader economy, as life-science occupations apparently pay about \$16,000 more annually than the U.S. mean annual wage and each dollar of output produced in the United States in that sector reportedly generates an additional \$1.70 in other sectors.

Even with the life sciences success seen in Michigan to date, some people believe that the State should do more to ensure the continued development of that sector of the economy and to place Michigan in a beneficial position to compete with other states for life science ventures and job growth. To that end, it has been suggested that Michigan create an authority to invest in early-stage life science ventures from a fund created through the sale of bonds or notes

issued by the authority; codify the Biosciences Research and Commercialization Center at Western Michigan University (WMU), which was created by a 2003 supplemental appropriation act; and require the center to establish and operate an affiliation of life science research and commercialization companies that would help facilitate the growth of the life science sector in Michigan.

CONTENT

Senate Bill 358 (S-1) would create the "Life Science Investment Authority Act" to do the following:

- **Create the Life Science Investment Authority within the Department of Treasury.**
- **Provide for the Authority to be governed by a board consisting of seven members, including the State Treasurer and the chief executive officer of the Michigan Economic Development Corporation or their designees.**
- **Require the board to contract with an investment management company to make qualified investments in qualified businesses (businesses that develop, market, or commercialize life science products, i.e., drugs or medical devices).**
- **Require the agreement between the investment management company and a qualified business to include a match requirement, conditions regarding a return on the investment and the use of members of the**

“Michigan Life Science Pipeline” (proposed by Senate Bill 359), and a condition that the investment would not be used for human cloning or stem cell research with embryonic tissue.

- Provide for the confidentiality of financial or proprietary information submitted by an applicant for a qualified investment.**
- Require the board to prepare an annual budget.**
- Allow the board to appoint a director and hire employees of the Authority.**
- Specify the powers of the Authority, including the power to promulgate rules.**
- Authorize the Authority to issue bonds and notes payable solely from revenue or funds available to it.**
- Create the “Life Science Investment Fund”, which could be administered for the general operations of the Authority and to secure its notes and bonds.**
- Exempt the Authority from certain taxes.**
- Appropriate \$100,000 from the General Fund for the Act’s initial implementation costs.**

Senate Bill 359 (S-1) would amend the Michigan Strategic Fund (MSF) Act to create the “Biosciences Research and Commercialization Center” in the MSF. The bill would do all of the following:

- Require the Center to coordinate research initiatives for scientists to establish new businesses, and promote life sciences research and commercialization in Michigan.**
- Require the Center to engage in collaborative efforts to develop novel pharmaceutical products.**
- Establish criteria for the Center to receive funding, including securing at least 25% matching funds and ensuring that a percentage of royalties or return on investments would be provided to the Commercial Development Fund.**
- Require the Center to establish and operate the “Michigan Life Science Pipeline”, which would be an affiliation of companies involved in life science research and commercialization.**
- Establish reporting requirements.**

- Require that the MEDC and the Life Sciences and Technology Tri-Corridor Steering Committee have access to the Center’s records and prescribe financial penalties for failure to provide the required information and access.**

(With the exception of requiring the Center to establish and operate the Michigan Life Science Pipeline, Senate Bill 359 (S-1) essentially would codify boilerplate language enacted in Section 381 of Public Act 173 of 2003, which made supplemental fiscal year (FY) 2002-03 and FY 2003-04 appropriations for various departments.)

Senate Bills 358 (S-1) and 359 (S-1) are tie-barred.

Senate Bill 358 (S-1)

Life Science Investment Authority

The bill would create a public body corporate and politic known as the Life Science Investment Authority within the Department of Treasury. The Authority would have to exercise its prescribed powers, duties, and functions independently of the State Treasurer, but the Authority’s budgeting, procurement, and related administrative functions would have to be performed under the Treasurer’s direction and supervision. The Authority could contract with the Department for the purpose of maintaining the Authority’s rights and interests.

The Authority’s accounts could be subject to annual financial audits by the State Auditor General. Authority records would have to be maintained according to generally accepted accounting principles.

Life Science Investment Authority Board

The Authority would be governed by the Life Science Investment Authority Board, which would consist of seven members who were Michigan residents. Board members would serve staggered terms, with two initial appointed members serving two years and three serving three years. After that, appointed members would serve four-year terms.

The board would consist of the State Treasurer and the chief executive officer of the MEDC, or their designees, and five

members appointed by the Governor by and with the advice and consent of the Senate. Appointed members could not be State employees and would have to have knowledge, skill, and experience as follows:

- At least one member in science.
- At least one member in venture capital investments.
- At least one member in business in the life science field.
- At least one member in the business of bringing life science products to market.

Members of the board (as well as the Authority's officers and employees) would be considered public servants and would have to discharge their duties in a nonpartisan manner, in good faith, in the best interests of the Authority, and with the degree of diligence, care, and skill that an ordinarily prudent person would exercise under similar circumstances in a like position.

Board members would serve without compensation but would have to be reimbursed for actual and necessary expenses.

Upon the appointment of at least five members, the board could hold its first meeting, which would have to be held within 60 days after the date the Authority was created. The board would have to comply with the Open Meetings Act.

The board could act only by resolution. A majority of the board members then in office, or of any committee of the board, would constitute a quorum for the transaction of business. A vote of the majority of the board members present at a meeting at which a quorum was present would constitute the action of the board, but a vote of the majority of the members serving at the time of the vote would be necessary to approve the issuance of bonds or to approve or amend the Authority's annual budget.

Confidential Information

A record or portion of a record, material, or other data received, prepared, used, or retained by the Authority in connection with an application for a qualified investment that related to financial or proprietary information submitted by the applicant, and that was considered by the applicant and

acknowledged by the Authority as confidential, would not be subject to disclosure under the Freedom of Information Act (FOIA). A designee of the Authority would have to determine whether the Authority would acknowledge as confidential any proprietary information submitted by an applicant. Unless considered proprietary information, the Authority could not acknowledge routine financial information as confidential. If the Authority's designee determined that financial or proprietary information was confidential, the Authority would have to release a written statement, subject to disclosure under FOIA, stating all of the following:

- The name of the person requesting that information be confidential as financial or proprietary.
- That the information was determined by the Authority's designee to be confidential as financial or proprietary information.
- A broad, nonspecific overview of the information.

The Authority could not disclose financial or proprietary information not subject to disclosure without consent of the applicant submitting the information.

("Financial or proprietary information" would mean information that has not been publicly disseminated or is unavailable from other sources, the release of which might cause the applicant competitive harm.)

Authority Annual Budget

Before the beginning of each fiscal year, the board would have to prepare a budget containing an itemized statement of the Authority's estimated current operational expenses, the amount necessary to pay the principal and interest of any outstanding bonds or other Authority obligations maturing during the ensuing fiscal year or that previously matured and were unpaid, an estimate of the Authority's revenue from all sources for the ensuing fiscal year, and other amounts necessary to further the purposes of the proposed Act. The Authority's budget would have to be funded by proceeds derived from gifts, grants, loans, appropriations, and other aids from any person or the Federal government, the State, or a local government or any Federal, State, or local governmental agency.

Director & Employees

The board could appoint a person, other than a board member, to serve as director of the Authority. The Authority could delegate any of its administrative powers to the director.

Subject to the board's approval, the director would have to supervise, and be responsible for, all of the following:

- The performance of the Authority's functions under the proposed Act.
- A regular report describing the Authority's activities and financial condition.
- The issuance of bonds, notes, or other obligations of the board.
- All other activities or functions that the board considered necessary.

The board could employ legal and technical experts, private consultants and engineers, accountants, scientists, and other agents or employees for professional and technical assistance and advice as necessary. The Authority would have to determine the qualifications, duties, and compensation of those it employed.

Investment Management Company

The board would have to contract with an investment management company to make "qualified investments" in "qualified businesses", under the terms of "qualified agreements" as determined by the board. The board would have to require the investment management company to do all of the following:

- Make early seed investments in qualified businesses for "life science products".
- Use peer review of the science involved in the life science product before entering into a qualified investment.
- Coordinate with the Michigan Life Science Pipeline to ensure that Pipeline members provided services at prices that were competitive within the industry.
- Work with the board to ensure that the proposed Act's purposes were accomplished.
- Report at least quarterly to the board, as determined by the board.
- Meet any other requirements determined by the board.

"Life science products" would mean a product that requires Food and Drug Administration (FDA) approval or registration before its introduction in the marketplace and is a drug or medical device as defined by the Federal Food, Drug, and Cosmetic Act.

"Qualified business" would mean a business entity that develops, markets, or commercializes life science products. "Qualified investments" would mean a loan or investment in a qualified business under the terms of a qualified agreement. "Qualified agreement" would mean an agreement between a qualified business and the investment management company. A qualified agreement would have to include all of the following:

- A condition that the qualified business match the qualified investment, which could not exceed 10% of the total needed to complete work on the requested round. A qualified investment could be made in follow-on rounds.
- A condition that the investment management company would ensure a return on the State's investment similar to other investors in the qualified business, as determined by the investment management company.
- A condition that qualified businesses would use members of the Michigan Life Science Pipeline to develop their life science product, if the services needed were readily available as determined by the investment management company.
- A condition that a qualified investment would not be used to engage in or support human cloning or stem cell research with embryonic tissue.

Powers of the Authority

Except as otherwise provided in the proposed Act, the Authority could do all things necessary to implement the purposes of the Act, including all of the following:

- Promulgate rules under the Administrative Procedures Act necessary to carry out the purposes of the proposed Act.
- Adopt, amend, and repeal bylaws for the regulation of the Authority's affairs and the conduct of its business.
- Solicit and accept gifts, grants, loans, and other assistance from any person or the

Federal, State, or a local government or any agency of the Federal, State, or a local government, or participate in any other way in any Federal, State, or local government program.

- Finance and otherwise aid in the development and commercialization of life science products.
- Make loans and investments; guarantee and insure loans, leases, bonds, notes, or other indebtedness, whether public or private; and issue letters of credit.
- Borrow money and issue bonds and notes to finance part or all of the costs of developing and commercializing life science products and secure those bonds and notes by mortgage, assignment, or pledge of any of its money, revenue, income, and property.
- Invest any money of the Authority, at the board's discretion, in any bond, note, or other obligation determined proper by the board.
- Contract for goods and services and engage personnel as necessary and engage the services of private consultants, managers, legal counsel, engineers, accountants, scientists, and auditors for professional financial assistance and advice payable out of any of the Authority's money.
- Charge, impose, and collect fees and charges in connection with any transaction and provide for reasonable penalties for delinquent payment of fees or charges.
- Do all other things necessary to promote and finance development and commercialization of life science products in Michigan.

The Authority also could indemnify and procure insurance indemnifying any members or employees of the board from personal loss or accountability from liability asserted by a person on the Authority's bonds or notes or from any personal liability or accountability by reason of the issuance of the bonds, notes, insurance, or guarantees; by reason of acquisition, construction, ownership, or operation of a project; or by reason of any other action taken or the failure to act by the Authority.

Bonds & Notes

The Authority could authorize and issue its bonds or notes payable solely from revenue or funds available to the Authority. Bonds

and notes of the Authority would not be a debt or liability of the State and would not create or constitute any indebtedness, liability, or obligation of the State or constitute a pledge of the full faith or credit of the State. All Authority bonds and notes would be payable solely from revenue or funds pledged or available for their payment as authorized in the proposed Act. The Authority's bonds or notes would not be general obligation of the Authority.

All expenses incurred in carrying out the Authority's ability to authorize and issue bonds or notes would be payable solely from revenue or funds provided or to be provided under the proposed Act. The Act would not authorize the Authority to incur any indebtedness or liability on behalf of or payable by the State. The Authority's bonds or notes would have to be authorized by resolution of the Authority.

Bonds and notes issued under the proposed Act would not be subject to the Revised Municipal Finance Act, but the issuance of bonds and notes would be subject to the Agency Financing Reporting Act.

The Authority could authorize and approve an insurance contract, an agreement for a line of credit, a letter of credit, a commitment to purchase notes or bonds, an agreement to remarket bonds or notes, or any other transaction to provide security to assure timely payment of a bond or note.

The Authority could not invest or otherwise approve an insurance contract, an agreement for a line of credit, a letter of credit, a commitment to purchase notes or bonds, an agreement to remarket bonds or notes, or an issuance of bonds or notes or any other transaction that resulted in a combined liability of the Authority in excess of \$50.0 million.

Any of the following could legally invest funds belonging to them, or within their control, in bonds or notes issued under the proposed Act:

- The State and a public officer, local unit of government, agency of the State or a local unit, or an intergovernmental entity created under the laws of the State.
- A bank, trust company, savings bank and institution, savings and loan association,

- investment company, or other person carrying on a banking business.
- An insurance company, insurance association, or other person carrying on an insurance business.
- An executor, administrator, guardian, trustee, or other fiduciary.

Authority bonds or notes would be authorized security for public deposits.

Life Science Investment Fund

The bill would create the Life Science Investment Fund under the jurisdiction and control of the Authority. The Fund could be administered for the general operations of the Authority and to secure any notes and bonds of the Authority. The Authority could spend money from the Fund only for the authorized purposes provided in the proposed Act.

The Authority could receive money or other assets from any source for deposit into the Fund. The Authority would have to credit to the Fund interest and earnings from Fund investments.

Money in the Fund at the close of the fiscal year would have to remain in the Fund and could not lapse to the General Fund.

Tax Exemption

The Authority would be exempt from, and could not be required to pay, taxes on real and personal property belonging to the Authority that was used for a public or governmental purpose. Property of the Authority would be public property devoted to an essential public or governmental function and purpose. The Authority's income and operation, including bonds or notes issued by the Authority or the interest and income derived from the bonds and notes, would be exempt from all taxes and special assessments of the State or a political subdivision of the State.

Senate Bill 359 (S-1)

Research & Commercialization

The Biosciences Research and Commercialization Center described in Public Act 173 of 2003 would be created in the MSF and be located at WMU in Kalamazoo. The Center would have to do all of the following:

- Coordinate research initiatives and provide an organizational home for scientists as they worked to establish new businesses.
- Obtain extramural funding to support research programs.
- Develop a center of excellence to promote life sciences research and commercialization in Michigan.
- Undertake collaborative efforts with private sector entities to develop novel pharmaceutical products in specialized therapeutic areas.
- Provide an organizational structure for research scientists and engineers, an entity to receive and license intellectual property, and a vehicle for entrepreneurial activities required for commercialization.

The Center's mission would be to discover new knowledge, generate and acquire intellectual property, commercialize intellectual property, and enrich the intellectual culture of the community.

Funding Criteria

In order to receive funding, the Center would have to submit a proposal and detailed business plan to the Life Sciences and Technology Tri-Corridor Steering Committee created by Public Act 169 of 2003 (which made FY 2003-04 appropriations for the MSF). The proposal would have to include a business plan for the Center's operations, including five-year budget forecasts; a plan for management oversight of the Center; intellectual property commercialization plans; a marketing plan; and a plan for private sector collaboration. The Center also would have to do all of the following in order to receive funding:

- Demonstrate the ability to leverage significant additional public and private investment and provide a minimum of 25% matching funds.
- Demonstrate a commitment to enter into collaborative research projects with universities or private research facilities in Michigan.
- Establish a separate governing board of directors that included the chief executive officer of the MEDC; the director of the Van Andel Institute; the Director of the Department of Labor and Economic Growth; one private sector member of the Life Sciences Steering Committee;

and other members from the public and private sectors.

- Establish and operate the Michigan Life Science Pipeline.

In addition, in order to receive funding, the Center would have to ensure that 10% of any royalties or return on investment directly related to research or commercialization activities developed by the Center would be provided to the Commercial Development Fund until the initial \$10.0 million appropriation made in Public Act 173 of 2003 was repaid.

Once the initial \$10.0 million appropriation was repaid, 3% of any royalties or return on investment directly related to research or commercialization activities developed by the Center would have to be provided to the Fund. If the Center failed to return royalties or return on investment to the Fund within five years, a plan would have to be developed between the Center and the MEDC to provide repayment of the \$10.0 million initial appropriation provided in Public Act 173 of 2003. (The Commercial Development Fund was originally created by Public Act 120 of 1999, which made FY 1999-2000 appropriations for the MSF. Public Act 120 provided that up to 10% of the funds it appropriated for the MSF could be used to support a Commercial Development Fund to support commercialization opportunities for life science research in Michigan.)

Any unspent or unencumbered balance from the funds appropriated to the Center would have to be deposited into a work project account and would be subject to the Management and Budget Act.

Life Science Pipeline

The Michigan Life Science Pipeline would have to begin operations by April 1, 2006. The Pipeline would have to do all of the following:

- Recruit Michigan-based companies involved in life science research and commercialization to affiliate themselves with the Pipeline.
- Market the services of Pipeline members to develop business for them.
- Otherwise assist Pipeline members to develop life science research and commercialization in Michigan.

- Provide that Pipeline members provide services to qualified businesses under the proposed Life Science Investment Authority Act at prices that were competitive within the industry, as determined by the Pipeline.
- Report to the Life Science Investment Authority the individuals who were Pipeline members and which services were and were not available from them.
- At the Pipeline's discretion, charge a reasonable fee to members, based on the services provided to them.

Reporting Requirements

By February 1 each year, the MEDC would have to provide a report to the Senate Majority Leader, Speaker of the House, chairs of the Appropriations Committees and members of the related subcommittees, the Senate and House Fiscal Agencies, and the State Budget Director, on the status of the Center, the status of the appropriation for it, and a listing of the Center's activities that had been paid for with any allocation from the appropriation. By February 1 and July 1, the Center would have to provide progress reports to the MEDC for the duration of the award to it.

Access to Records

The MEDC and the Steering Committee would have to have access at all reasonable times to the Center's records in order to monitor the research projects and prepare reports. If the Center failed to provide the MEDC with the information or access required under the bill, it would be liable to the State for a penalty of at least \$500 per day beginning within 10 days after the February 1 or July 1 reporting date and at least \$1,000 per day beginning 20 days after the reporting date. A penalty could be withheld from future appropriations.

Proposed MCL 125.2078 (S.B. 359)

ARGUMENTS

(Please note: The arguments contained in this analysis originate from sources outside the Senate Fiscal Agency. The Senate Fiscal Agency neither supports nor opposes legislation.)

Supporting Argument

The life sciences industry is expected to experience significant growth in the near future. Some projections indicate that

employment in this sector will grow 13% more rapidly than the average annual growth rate for overall employment in the next decade. The development of new pharmaceuticals and medical devices and technologies could help to drive Michigan's economy in the 21st century, and it is important that the State position itself as an attractive location for the development of life science business ventures. Indeed, Michigan already has committed significant resources to the development of this important business sector. In the past four years, more than \$500 million in public and private investment reportedly has been made in life sciences in Michigan. This has contributed to the launching of nearly 100 new life science-related businesses. Successful ventures in this area of the economy should lead to a significant increase of well-paying jobs in Michigan. It is important for the State to leverage the investments made to date by providing financial and developmental assistance to life science ventures. By creating a funding source and mechanism for early-seed investment in Michigan-based life science companies, Senate Bill 358 (S-1) would encourage economic growth in that sector and make Michigan an attractive place for life science entrepreneurs to pursue their goals.

In addition, Senate Bill 359 (S-1) would create the Michigan Life Science Pipeline, an affiliation of companies involved in life science research and commercialization, to provide expertise and resources for the early-stage development of more life science ventures. Pipeline companies would provide the services needed to gain FDA approval of a life science product, which could help products reach the market sooner. The Pipeline also would provide an incentive for diverse companies to collaborate for the development of the larger life sciences industry.

Supporting Argument

Financial support for high-risk ventures has been lacking in Michigan. The State is said to rank low in the amount of venture capital and "angel" investment capital available to start-up companies. (An angel investor is a private investor, often a successful entrepreneur, who provides capital and business expertise at an early stage of a venture's development.) To address the shortfall in the availability of Michigan-based

venture capital, in 2003 the State enacted the Michigan Early Stage Venture Investment Act, which provides for the creation of the Michigan Early Stage Venture Investment Fund, to which investors may contribute under agreements that provide guaranteed rates of return or tax credits. Money in the Fund is to be used for investment in venture capital firms, which will provide early-stage capital for technology, alternative energy, and health care ventures in Michigan. In addition, the Senate has passed Senate Bills 92 and 521, which would allow taxpayers to claim an income tax credit for equity investments in a qualified technology-based business or a community-based seed capital company. Senate Bill 358 (S-1) would build upon those two measures, by authorizing the proposed Life Science Investment Authority to contract with an investment management company to use revenue from the sale of bonds for seed capital investments in businesses that develop, market, or commercialize life science products.

Supporting Argument

While the Biosciences Research and Commercialization Center already has been created and is operating at WMU, establishing such an ongoing effort in the boilerplate language of a budget bill may not be the most effective way to sustain a long-term economic development function. By creating the Center in statute, Senate Bill 359 (S-1) would make that entity a more stable resource for the development of life sciences businesses in Michigan.

Opposing Argument

Article IX, Section 19 of the State Constitution prohibits the State from investing in the stock of individual companies, with certain exceptions such as for the investment of pension funds. It is unclear whether a State authority making early-seed investments in certain businesses for life science products, as proposed by Senate Bill 358 (S-1), would violate that constitutional provision.

In addition, it is unclear whether pledging money from State appropriations for the repayment of bonds issued under the bill would make them general obligation bonds rather than revenue bonds. Revenue bonds have a specified revenue source for their repayment and are not backed by the full faith and credit of the State; general

obligation bonds, on the other hand, are backed by the full faith and credit of the State and require voter approval.

Legislative Analyst: Patrick Affholter

FISCAL IMPACT

Senate Bill 358 (S-1)

The bill contains an initial appropriation of \$100,000 for implementation costs under the bill. However, actual costs would depend on future appropriations and the amount of bonds issued by the Authority. The MEDC funds life sciences projects through the appropriations for the Technology Tri-Corridor - Life Sciences line item. The following amounts have been appropriated for the program over recent fiscal years:

FY 2001-02 - \$45 million
FY 2002-03 - \$32.5 million
FY 2003-04 - \$25 million
FY 2004-05 - \$30 million

Senate Bill 359 (S-1)

The bill would have no fiscal impact on State or local government.

Fiscal Analyst: Bill Bowerman
Elizabeth Pratt

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This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.