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BILL ANALYSIS

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House Bills 5099 and 5100 (as passed by the House)
Sponsor: Representative Ed Clemente
House Committee: New Economy and Quality of Life
Senate Committee: Commerce and Tourism

Date Completed: 8-5-09

CONTENT

House Bills 5099 and 5100 would amend Sections 88k and 88b, respectively, of Chapter 8A (21st Century Investment Programs and Activities) of the Michigan Strategic Fund (MSF) Act to do the following:

- Allow the Strategic Economic Investment and Commercialization Board (commercialization board) to award grants from the 21st Century Jobs Trust Fund and recommend loans, equity investments, and warrants from the Jobs for Michigan Investment Fund (rather than requiring the commercialization board to award grants and loans from both Funds).
- Make loans, equity investments, and warrants recommended by the commercialization board subject to the approval of the MSF board.
- Remove peer-review requirements from the process for awarding grants and making loans and require use of a request for proposal (RFP) process instead.
- Require that certain factors considered in the review process be given "preference" rather than "equal weight".
- Specify that a Federal review process would satisfy the Chapter 8A review process for certain grant or investment applicants.
- Allow the MSF to establish a process of recommending investments in qualified venture capital funds to establish accelerator funds that would invest in businesses engaged in competitive edge technologies.
- Allow nonprofit directors or officers to meet certain requirements by filing an affidavit.
- Delete notification and hearing requirements regarding changes to commercialization board programs.
- Revise 21st Century program spending limitations.
- Allow Chapter 8A application fees to be used for administration costs, without being subject to restrictions on the percentage of appropriations that may be used for administration costs.

A detailed description of the bills follows.

House Bill 5099

21st Century Grants & Loans

Under Section 88k, the commercialization board must award grants and loans from the 21st Century Jobs Trust Fund and the Jobs for Michigan Investment Fund only for basic research, applied research, university technology transfer, and commercialization of products, processes, and services to encourage the development of competitive edge technologies to create jobs in Michigan.

Under the bill, the commercialization board could award grants (but not loans) from the 21st Century Jobs Trust Fund and could recommend loans, convertible loans, equity investments, and warrants from the Jobs for Michigan Investment Fund for basic

research, applied research, university technology transfer, and commercialization of products, processes, and services to encourage the development of competitive edge technologies *intended* to create jobs in Michigan. Loans, convertible loans, equity investments, and warrants recommended by the commercialization board would be subject to approval by the MSF board. The MSF board would have to establish a standard process to review investments recommended by the commercialization board before approving any investment it considered appropriate.

Currently, the MSF, as determined by the commercialization board, must establish a competitive process to award grants and make loans for competitive edge technologies. The bill instead would allow the MSF, as determined by the commercialization board and the MSF board, to establish a process to award grants for and recommend investments in competitive edge technologies.

Currently, the competitive process must include a provision requiring the applications to be peer reviewed by independent peer review experts, based on the scientific and technical merit, personnel expertise, commercial merit, and the ability to leverage additional funding of the application. Scientific and technical merit, personnel expertise, commercial merit, and the ability to leverage additional funding must be given *equal weight* in the review and scoring process.

Under the bill, instead, the process would have to include a provision requiring the commercialization board to award grants for, and recommend investments in competitive edge technologies, by issuing an RFP. The commercialization board would have to establish a standard process to evaluate proposals submitted as a result of an RFP and appoint a committee to review the proposals. The applications would have to be reviewed, in addition to other criteria adopted by the board, based on the scientific and technical merit, personnel expertise, commercial merit, and the ability to leverage additional funding of the application. Those factors, in addition to other criteria adopted by the board, would have to be give *preference* in the review and scoring process. If an applicant were seeking a grant or investment under

Chapter 8A to match Federal funds for small business innovation research or small business technology transfer programs, the review requirement would be satisfied by the review conducted by the Federal agency awarding the Federal funds.

The bill would delete a requirement that the MSF contract with independent peer review experts selected by the commercialization board to assist the board with its responsibilities under Chapter 8A.

Investments in Venture Capital Funds

Under the bill, the MSF, as determined by the commercialization board and the MSF board, could establish a process to recommend investments to the MSF in qualified venture capital funds to establish accelerator funds that would invest in qualified businesses that engaged in competitive edge technologies.

The process would have to include a provision requiring the commercialization board to select qualified venture capital funds by issuing an RFP. At a minimum, the RFP would have to require a responding entity to disclose any conflict of interest, any criminal convictions, or any investigations by the Internal Revenue Service or the Securities and Exchange Commission, or any other Federal or State taxing or securities regulatory body, or court, or pertinent litigation regarding the conduct of the person or entity. The commercialization board would have to establish a standard process to evaluate proposals submitted as a result of an RFP and appoint a committee to review the proposals. The process also would have to include a provision that a qualified venture capital fund would not be eligible to participate unless it operated or entered into an agreement for the operation of a business development office in Michigan, staffed with at least one full-time equivalent person who was actively seeking opportunities for venture capital investments in businesses located in Michigan, unless the investment opportunity requested by the qualified venture capital fund were targeted to a specific transaction involving a competitive edge technology that would not occur without the MSF's investment as determined by the commercialization board.

The process also would have to include all of the following:

- A provision that a qualified venture capital fund would not be eligible to participate unless it agreed to establish an accelerator fund (an investment fund targeted at early-stage technology companies) and collaborate with an institution of higher education.
- A preference for proposals that could contribute to the development of economic diversification or the creation of employment opportunities in Michigan.
- A provision requiring that the applicant leverage other resources as a condition of investment.
- A provision that not more than 15% of any investment awarded could be used for administrative costs or overhead, including personnel, by the awardee or its accelerator fund.
- A requirement that authorized investments include repayment provisions in the event the qualified venture capital fund or accelerator fund failed to comply with the agreement.

Spending Prohibitions

The Act requires the commercialization board to establish requirements to ensure that money spent under Section 88k is not used for certain purposes, including grants or loans to a person who has been convicted of a criminal offense incident to the application of or performance of a State contract or subcontract, or grants or loans to a person who has been convicted of a criminal offense, or held liable in a civil proceeding, that negatively reflects on the person's business integrity, based on a finding of embezzlement, theft, forgery, bribery, falsification or destruction of records, receipt of stolen property, or violation of State or Federal antitrust statutes. The bill specifies that a director or officer of a nonprofit entity could satisfy these requirements if he or she filed with the MSF an affidavit affirming that he or she had not been so convicted or held liable.

Deletion of Notification Requirement

The Act requires the commercialization board to notify the Governor, the Secretary of the Senate, the Clerk of the House of Representatives, certain legislators, and each person who requested to be notified, before adopting a resolution that establishes or substantially changes a program operated

by the board. The Act includes requirements for the notice, and requires the board to hold a public hearing and give people an opportunity to present data, views, questions, and arguments. The bill would delete these provisions.

House Bill 5100

Expenditure of 21st Century Money

Under Section 88b, money transferred or appropriated by law to the MSF for the purposes of carrying out Chapter 8A must be spent or invested by the MSF as authorized by law for the following purposes:

- 21st Century investments.
- Grants and loans approved by the commercialization board under Section 88k.
- Other programs or activities authorized under Chapter 8A.

The bill would delete the authorization for money to be spent for grants and loans approved by the commercialization board, and would refer instead to money spent for competitive edge technology loans or grants under Section 88k or for convertible loans, equity investments, or warrants from the Jobs for Michigan Investment Fund recommended by the commercialization board under Section 88k and approved by the MSF board.

Spending Limits

Currently, except for certain appropriations, the MSF board may not spend more than the following amounts each year from the 21st Century Jobs Trust Fund, for the following purposes:

- For the loan enhancement program, 25%.
- For the private equity investment program, the venture capital investment program, and the mezzanine investment program, combined, 40%.
- For competitive edge technology grants and loans under Section 88k, 70%.

Also, the commercialization board may not authorize the expenditure of more than \$100.0 million for basic research over the life of the program.

The bill would delete these provisions.

Currently, the commercialization board is *required* to authorize the expenditure of at least certain amounts in certain fiscal years, including \$25.0 million in fiscal year (FY) 2008-09 through 2011-12. The bill, instead, would *permit* the MSF board to authorize the expenditure of at least \$30.0 million in FY 2007-08 through FY 2011-12 for competitive edge technology loans or grants under Section 88k or for convertible loans, equity investments, or warrants from the Jobs for Michigan Investment Fund recommended by the commercialization board under Section 88k and approved by the MSF board. The commercialization board and the MSF board could not authorize the expenditure of more than \$50.0 million for basic research between October 1, 2005, and September 30, 2016.

Application Fees for Program Administration

Under the Act, not more than 4% of the annual appropriation from the 21st Century Jobs Trust Fund may be used for purposes of administering the programs and activities authorized under Chapter 8A. The MSF and its board may not use more than 3% of the annual appropriation for administering the programs and activities authorized under Chapter 8A unless the MSF board, by a two-thirds vote, authorizes the additional 1% for administration.

The bill specifies that application fees received for programs and activities authorized under Chapter 8A would have to be paid to the MSF and could be used by the MSF for administering the programs and activities authorized under Chapter 8A. The restrictions on expenditures for administering Chapter 8A programs and activities would not apply to the expenditure of application fee revenue.

MCL 125.2088k (H.B. 5099)
125.2088b (H.B. 5100)

Legislative Analyst: Patrick Affholter

FISCAL IMPACT

The bills would give the Michigan Strategic Fund additional flexibility in allocating appropriations from the 21st Century Jobs Trust Fund and restructure the competitive edge technology grant and loan program as an optional program that could award grants and loans or make investments.

The 21st Century Jobs Trust Fund program was created in FY 2005-06 to diversify the Michigan economy. As originally enacted, the program required an allocation of State funds of \$1.0 billion over 10 years. With the budget difficulties in recent years, this level of appropriations was not sustained as funds were transferred to the General Fund to balance the budget. The appropriation to the MSF board for 21st Century Programs is \$52,950,000 in FY 2008-09, an amount below the \$75.0 million that was anticipated by the original legislation.

House Bill 5099

The bill would revise the current competitive edge technology grant and loan program which was most recently funded at \$30.0 million in FY 2007-08, the minimum level required by statute in that year. The program would become an optional program that could award grants, loans, convertible loans, equity investments, and warrants. Investments made by the program would have to satisfy a number of criteria including establishment of accelerator funds (to invest in early stage companies) and collaboration with an institution of higher education. Approval of awards would be a two-step process requiring first recommendations by the Strategic Economic Investment and Commercialization Board, followed by approval by the MSF board, as opposed to the current structure under which the commercialization board has authority to make awards. The program would be revised to allow grants to be made from the 21st Century Jobs Trust Fund, while loans, convertible loans, equity investments, and warrants could be awarded from the Jobs for Michigan Investment Fund. The Investment Fund is the permanent fund that primarily consists of repayments and earnings from prior awards. The MSF estimates that the FY 2008-09 closing balance in the Investment Fund will be approximately \$1.7 million.

The bill would eliminate the requirement to make awards after a competitive peer review process. This would be replaced by a request for proposal process. This is expected to reduce the administrative costs of the program. The bill also would remove the requirement to provide notice to the Governor, the Secretary of the Senate, the Clerk of the House, and members of the

House and Senate Committees on Appropriations, and to hold a public hearing requiring any proposed change in commercialization board program policies or fees. This simplification of process also would tend to reduce administrative costs.

House Bill 5100

The MSF Act sets a minimum amount that is required to be allocated to the competitive edge technology grant and loan program each year. This allocation is set at \$25.0 million for each year from FY 2008-09 through FY 2011-12. The bill would eliminate this requirement. Instead, the MSF has proposed allocating remaining funds available in FY 2008-09 to loan guarantee programs that would support manufacturers and auto suppliers that are having difficulty obtaining financing in the current economic climate. Given the reduced level of 21st Century Jobs Trust Fund appropriations after reductions made by Executive Order 2009-22 and the program allocations made by the MSF board to date, it does not appear that the MSF board can meet the current law requirement to allocate \$25.0 million in FY 2008-09 to competitive edge technology grants and loans.

Other limitations on the allocation by the MSF board of annual appropriations from the 21st Century Jobs Trust Fund among various programs would be eliminated by the bill. The MSF Act authorizes the MSF board to allocate appropriated funds from the 21st Century Jobs Trust Fund within broad limits. These require that each year not more than 25% be used for loan enhancement, not more than 40% for private equity programs, and not more than 70% for competitive edge technology grants and loans. This bill also would revise the limitation on spending on basic research, reducing it from \$100.0 million over the life of the program to a total of \$50.0 million from FY 2005-06 through FY 2015-16. Eliminating these requirements would permit the MSF board to focus remaining appropriations in FY 2008-09 on loan programs, to a greater degree than is permissible under current law.

Staff of the MSF have indicated that the FY 2008-09 appropriations from the 21st Century Jobs Trust Fund would be allocated as shown in Table 1.

Table 1
Allocations from the 21st Century Jobs Trust
Fund Appropriations
FY 2008-09

	FY 2008-09
Administration	\$2,480,000
Business Marketing and Business Development	3,100,000
Loan Programs	21,070,000
Centers for Energy Excellence	24,900,000
SBIR/STTR Matching Grants	1,400,000
Total	\$52,950,000

Source: Michigan Strategic Fund

The bill also specifies that application fees for 21st Century programs would be used by the MSF for the cost of administering those programs. The fee revenue would provide funding for administrative expenses in addition to the allocation of up to 4% of appropriations for administration permitted by statute. The fees are not set by the bill. The amount of fee revenue received would depend on the level of fees established and the number of applicants.

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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.