

ACT 260

S.B. NO. 1365

A Bill for an Act Relating to the Innovation Economy.

Be It Enacted by the Legislature of the State of Hawaii:

SECTION 1. The legislature finds that Hawaii's desire for economic growth that benefits all residents depends on building our State's human resources, and in turn, applying these highly skilled resources to the creation and adoption of innovation across its economy.

The legislature further finds that economic growth and diversification throughout many communities has been enhanced by the availability of venture capital funding for entrepreneurs engaged in building innovative new ventures. Well-known regions such as Silicon Valley; Route 128 in Boston; Austin, Texas; and the Research Triangle in North Carolina have benefited greatly from the combination of scientific research, an entrepreneurial culture driving high technology growth, and funding availability for early-stage equity investments. Other areas similar in size and population to Hawaii, including San Diego, Salt Lake City, Seattle, and Boulder, have also developed strong technology-based businesses with the assistance of venture capital.

The source of this venture capital is derived in large part through employee pension funds. Of the approximately \$25,000,000,000 of venture investment in 2006, over half was provided by pension funds. Many public pension funds target investments in-state to provide enhanced returns to pensioners and support the development of high-growth businesses within local communities.

The state employees' retirement system has committed approximately \$300,000,000 to the alternative asset category, including venture capital, but none of it is invested in Hawaii. The legislature finds that this lack of investment in Hawaii venture capital by the employees' retirement system may be due to a lack of large-scale qualified investment opportunities and concerns over the possible breach of fiduciary duty and prudent investor rules related to early-stage investing. Oregon, for

example, has legislated investment by the public pension fund in local venture capital where prudent.

The purpose of this Act is to encourage the employees' retirement system to invest in Hawaii venture capital by:

- (1) Requiring the employees' retirement system to report annually to the legislature on any Hawaii venture capital investments; provided that if the board determines it is not prudent to invest in any Hawaii venture capital the board shall report the rationale for the decision; and
- (2) Requiring the employees' retirement system to develop criteria to determine the amount of funds that may be prudently invested in Hawaii private placement investments.

SECTION 2. Section 88-119, Hawaii Revised Statutes, is amended to read as follows:

“§88-119 Investments. Investments may be made in:

- (1) Real estate loans and mortgages. Obligations (as defined in section 431:6-101) of any of the following classes:
 - (A) Obligations secured by mortgages of nonprofit corporations desiring to build multirental units (ten units or more) subject to control of the government for occupancy by families displaced as a result of government action;
 - (B) Obligations secured by mortgages insured by the Federal Housing Administration;
 - (C) Obligations for the repayment of home loans made under the Servicemen's Readjustment Act of 1944 or under Title II of the National Housing Act;
 - (D) Other obligations secured by first mortgages on unencumbered improved real estate owned in fee simple; provided that the amount of the obligation at the time investment is made therein shall not exceed eighty per cent of the value of the real estate and improvements mortgaged to secure it, and except that the amount of the obligation at the time investment is made therein may exceed eighty per cent but no more than ninety per cent of the value of the real estate and improvements mortgaged to secure it; provided further that the obligation is insured or guaranteed against default or loss under a mortgage insurance policy issued by a casualty insurance company licensed to do business in the State. The coverage provided by the insurer shall be sufficient to reduce the system's exposure to not more than eighty per cent of the value of the real estate and improvements mortgaged to secure it. The insurance coverage shall remain in force until the principal amount of the obligation is reduced to eighty per cent of the market value of the real estate and improvements mortgaged to secure it, at which time the coverage shall be subject to cancellation solely at the option of the board. Real estate shall not be deemed to be encumbered within the meaning of this subparagraph by reason of the existence of any of the restrictions, charges, or claims described in section 431:6-308;
 - (E) Other obligations secured by first mortgages of leasehold interests in improved real estate; provided that:
 - (i) Each leasehold interest at the time shall have a current term extending at least two years beyond the stated maturity of the obligation it secures; and

- (ii) The amount of the obligation at the time investment is made therein shall not exceed eighty per cent of the value of the respective leasehold interest and improvements, and except that the amount of the obligation at the time investment is made therein may exceed eighty per cent but no more than ninety per cent of the value of the leasehold interest and improvements mortgaged to secure it;

provided further that the obligation is insured or guaranteed against default or loss under a mortgage insurance policy issued by a casualty insurance company licensed to do business in the State. The coverage provided by the insurer shall be sufficient to reduce the system's exposure to not more than eighty per cent of the value of the leasehold interest and improvements mortgaged to secure it. The insurance coverage shall remain in force until the principal amount of the obligation is reduced to eighty per cent of the market value of the leasehold interest and improvements mortgaged to secure it, at which time the coverage shall be subject to cancellation solely at the option of the board;

- (F) Obligations for the repayment of home loans guaranteed by the department of Hawaiian home lands pursuant to section 214(b) of the Hawaiian Homes Commission Act, 1920; and
- (G) Obligations secured by second mortgages on improved real estate for which the mortgagor procures a second mortgage on the improved real estate for the purpose of acquiring the leaseholder's fee simple interest in the improved real estate; provided that any prior mortgage ~~[does]~~ shall not contain provisions that might jeopardize the security position of the retirement system or the borrower's ability to repay the mortgage loan.

The board may retain the real estate, including leasehold interests therein, as it may acquire by foreclosure of mortgages or in enforcement of security, or as may be conveyed to it in satisfaction of debts previously contracted; provided that all the real estate, other than leasehold interests, shall be sold within five years after acquiring the same, subject to extension by the governor for additional periods not exceeding five years each, and that all the leasehold interests shall be sold within one year after acquiring the same, subject to extension by the governor for additional periods not exceeding one year each;

- (2) Government obligations, etc. Obligations of any of the following classes:
 - (A) Obligations issued or guaranteed as to principal and interest by the United States or by any state thereof or by any municipal or political subdivision or school district of any of the foregoing; provided that principal of and interest on the obligations are payable in currency of the United States; or sovereign debt instruments issued by agencies of, or guaranteed by foreign governments;
 - (B) Revenue bonds, whether or not permitted by any other provision hereof, of the State or any municipal or political subdivision thereof, including the board of water supply of the city and county of Honolulu, and street or improvement district bonds of any district or project in the State; and
 - (C) Obligations issued or guaranteed by any federal home loan bank, including consolidated federal home loan bank obligations, the Home Owner's Loan Corporation, the Federal National Mortgage Association, or the Small Business Administration;

- (3) Corporate obligations. Below investment grade or nonrated debt instruments, foreign or domestic, in accordance with investment guidelines adopted by the board;
- (4) Preferred and common stocks. Shares of preferred or common stock of any corporation created or existing under the laws of the United States or of any state or district thereof or of any country;
- (5) Obligations eligible by law for purchase in the open market by federal reserve banks;
- (6) Obligations issued or guaranteed by the International Bank for Reconstruction and Development, the Inter-American Development Bank, the Asian Development Bank, or the African Development Bank;
- (7) Obligations secured by collateral consisting of any of the securities or stock listed above and worth at the time the investment is made at least fifteen per cent more than the amount of the respective obligations;
- (8) Insurance company obligations. Contracts and agreements supplemental thereto providing for participation in one or more accounts of a life insurance company authorized to do business in Hawaii, including its separate accounts, and whether the investments allocated thereto are comprised of stocks or other securities or of real or personal property or interests therein;
- (9) Interests in real property. Interests in improved or productive real property in which, in the informed opinion of the board, it is prudent to invest funds of the system. For purposes of this paragraph, "real property" includes any property treated as real property either by local law or for federal income tax purposes. Investments in improved or productive real property may be made directly or through pooled funds, including common or collective trust funds of banks and trust companies, group or unit trusts, limited partnerships, limited liability companies, investment trusts, title-holding corporations recognized under section 501(c) of the Internal Revenue Code of 1986, as amended, similar entities that would protect the system's interest, and other pooled funds invested on behalf of the system by investment managers retained by the system;
- (10) Other securities and futures contracts. Securities and futures contracts in which in the informed opinion of the board, it is prudent to invest funds of the system, including currency, interest rate, bond, and stock index futures contracts and options on the contracts to hedge against anticipated changes in currencies, interest rates, and bond and stock prices that might otherwise have an adverse effect upon the value of the system's securities portfolios; covered put and call options on securities; and stock; whether or not the securities, stock, futures contracts, or options on futures are expressly authorized by or qualify under the foregoing paragraphs, and notwithstanding any limitation of any of the foregoing paragraphs (including paragraph (4)); and
- (11) Private placements. Investments in institutional blind pool limited partnerships, limited liability companies, or direct investments that make private debt and equity investments in privately held companies, including but not limited to investments in Hawaii high technology businesses or venture capital investments that, in the informed opinion of the board, are appropriate to invest funds of the system. In evaluating venture capital investments, the board shall consider, among other things, the impact an investment may have on job creation in Hawaii and on the state economy. The board shall report annually to the legislature on any Hawaii venture capital investments it has made; provided that if the board determines it is

not prudent to invest in any Hawaii venture capital investments the board shall report the rationale for the decision. The board, by January 1, 2008, shall develop criteria to determine the amount of funds that may be prudently invested in Hawaii private placement investments.’

SECTION 3. Statutory material to be repealed is bracketed and stricken. New statutory material is underscored.

SECTION 4. This Act shall take effect on July 1, 2007.

(Approved July 6, 2007.)