

The Florida Senate
BILL ANALYSIS AND FISCAL IMPACT STATEMENT

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

Prepared By: The Professional Staff of the Appropriations Subcommittee on Transportation, Tourism, and Economic Development

BILL: PCS/CS/SB 1314 (188068)

INTRODUCER: Appropriations Subcommittee on Transportation, Tourism, and Economic Development; Commerce and Tourism Committee; and Senator Brandes

SUBJECT: Florida Capital Formation Act

DATE: February 21, 2018 REVISED: _____

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	<u>Harmsen</u>	<u>McKay</u>	<u>CM</u>	<u>Fav/CS</u>
2.	<u>Hrdlicka</u>	<u>Hrdlicka</u>	<u>ATD</u>	<u>Recommend: Fav/CS</u>
3.	<u> </u>	<u> </u>	<u>AP</u>	<u> </u>

Please see Section IX. for Additional Information:
COMMITTEE SUBSTITUTE - Substantial Changes

I. Summary:

PCS/CS/SB 1314 creates the Institute for Commercialization of Florida Technology (institute) to increase the availability of seed and early stage investment capital in Florida without requiring an ongoing state expenditure for such support.

The institute will replace the Institute for Commercialization of Public Research (ICPR). The institute will differ from the ICPR in several ways. Namely, the institute will:

- Be operated by a private fund manager who will be paid from fees based on the institute's investment activities, rather than a professional staff;
- No longer partner with publicly supported universities or research institutes to support their commercialization efforts; and
- Not be supported by or function under the Department of Economic Opportunity (department).

Like the ICPR, however, the institute will partner with innovation and target industry businesses to foster investment funding, especially in seed-stage, startup, and early stage companies; advise companies about successful management, operations, and development processes; and provide opportunities to attract further investment.

The bill has minimal impact on state expenditures.

The bill takes effect July 1, 2018.

II. Present Situation:

Venture Capital and Early Stage Business Investments

Venture capital is money provided by investors who choose to fund young companies that have the potential to develop into profitable businesses. Venture capital is an important source of equity for startup companies because its investment does not typically require security (such as a guarantee of repayment) from the business.¹

Venture capital investments are typically made in lieu of traditional bank loans because the start-up or expansion-oriented companies they fund have a higher level of investment risk. The investor may eventually share in the risk of a failed business or the reward of a successful one. These investments are also characterized by a higher level of equity participation in the business by the investor, including mentorship or networking to assist the company with management and other obstacles.²

Investment in a technology or idea that has not yet been developed into a fully-fledged product or business is also known as “seed investing” or “early-stage investing.”³

As of September 2017, one Florida website lists approximately 38 venture capital firms in the state.⁴ Although the venture capital industry has grown in the last 20 years, it has done so only in limited geographic regions – generally limiting the investment of capital in businesses in or near those regions.⁵

Florida Capital Formation Act

In 2007, the Florida Capital Formation Act was enacted to address the need to increase the availability of seed capital and early stage venture capital for emerging Florida companies.⁶ The act created the Florida Opportunity Fund and the Institute for the Commercialization of Public Research.

The intent of the act, in part, is to “mobilize private investment in a broad variety of venture capital partnerships in diversified industries and geographies” and “mobilize venture equity

¹ National Venture Capital Association, *Funding Innovation: How Venture Funded Startups Grow, Transform and Impact the U.S. Economy*, available at <https://nvca.org/ecosystem/funding-innovation/> (last visited Feb. 16, 2018).

² *Id.*

³ Florida Office of Economic and Demographic Research, *Return-on-Investment of the Florida Microfinance Loan and Microfinance Guarantee Programs*, p. 37, (Jan. 2018), available at

<http://edr.state.fl.us/Content/returnoninvestment/MicrofinanceLoanandGuaranteeProgams.pdf> (last visited Feb. 15, 2018).

⁴ Florida Trend, *Business FLORIDA: Business Assistance and Funding, Florida’s Venture Capital Firms*, (Sept. 22, 2017) available at <http://www.floridatrend.com/article/17615/floridas-venture-capital-firms--2015> (last visited Feb. 15, 2018).

⁵ Cromwell Schmisser, *Program Evaluation of the US Department of Treasury State Small Business Credit Initiative*, p. 61 (Oct. 2016), available at https://www.treasury.gov/resource-center/sb-programs/Documents/SSBCI_pe2016_Full_Report.pdf (last visited Feb. 16, 2018).

⁶ Chapter 2007-189, L.O.F., codified as ss. 288.9621-288.9625, F.S.

capital for investment in such a manner as to result in a significant potential to create new businesses and jobs in this state.”⁷

The Opportunity Fund was created to invest in seed and early stage venture capital funds (fund of funds), focusing on opportunities in Florida, and it can also make direct investments, including loans, in individual businesses and infrastructure projects. Enterprise Florida, Inc., facilitates the fund.

Further, the Legislature intended to create an institute “to mentor, market, and attract capital to such commercialization ventures throughout the state.” The Institute for the Commercialization of Public Research (ICPR) assists in the commercialization of products developed by research and development activities of innovation businesses, publicly supported universities and colleges, research institutes, and other publicly supported organizations within Florida.⁸

Institute for the Commercialization of Public Research

The ICPR is a private-public partnership that operates as a nonprofit corporation. It administers company support services and seed capital funding programs to help early-stage businesses or ideas for businesses grow and thrive in Florida.⁹ The ICPR operates with the support of mentors, advisors, and donors, and the Division of Strategic Business Development of the department provides support for and works closely with the ICPR.¹⁰

The ICPR has two primary locations, one at the University of Florida in Gainesville and the other at Florida Atlantic University in Boca Raton. A board of directors governs the ICPR and is responsible for managing the ICPR’s funds, presenting the ICPR’s annual report, and overseeing the ICPR’s general affairs.¹¹ The board of directors is composed of the executive director of the department (or designee); the president of the university where the ICPR is located, or when the ICPR is located at multiple universities, the presidents’ agreed upon designee; and three directors appointed by the Governor.¹²

The ICPR matches commercially viable technologies with management talent and capital. Additionally, the ICPR focuses on technologies and companies that originate from publicly supported organizations across the state and companies in Florida’s innovation businesses and target industries.¹³

⁷ Section 288.9622, F.S.

⁸ Department of Economic Opportunity, *Long Range Program Plan Fiscal Year 2018-2019 through 2022-2023*, p. 21 (September 29, 2017), available at <http://floridafiscalportal.state.fl.us/Document.aspx?ID=17087&DocType=PDF> (last visited Feb. 16, 2018).

⁹ Department of Economic Opportunity, *Long Range Program Plan* at p. 21. Institute for Commercialization of Public Research, *Who We Are*, available at <http://www.florida-institute.com/who-we-are> (last visited Feb. 16, 2018).

¹⁰ Section 20.60, F.S. Department of Economic Opportunity, *Long Range Program Plan* at pp. 19 and 42.

¹¹ Section 288.9625, F.S. Institute for Commercialization of Public Research, *Who We Are: Board of Directors*, available at <http://www.florida-institute.com/about/board-of-directors> (last visited Feb. 15, 2018).

¹² Section 288.9625(4), F.S.

¹³ Sections 288.0189 and 288.106(2)(q), F.S., sets forth the innovation businesses and target industries. Institute for the Commercialization of Public Research, *Annual Report Brochure FY 2016-2017* (Nov. 22, 2017), available at <http://www.florida-institute.com/news/florida-institutes-2016-17-brochure> (last visited Feb. 17, 2018).

Before the institute facilitates a company or organization's efforts to commercialize its products, it must be accepted by the institute through an application process. Publicly supported organizations may recommend that a company attempting to commercialize its research, technology, or patents be accepted by the institute. Upon acceptance by the institute, a company receives mentoring and other services, which includes developing marketing information on the company, using institute resources to attract capital investment into the company, and other resources that may encourage effective management, growth, capitalization technology protection, or marketing or business success.¹⁴

Current law prohibits the ICPR from charging for its services unless they are provided to a private company, as compared to a state university or its affiliated organizations.

Since 2007, the Legislature has appropriated an estimated total of \$33 million in state funds to the ICPR for operating costs, grants, loans, and seed stage funds.¹⁵ The ICPR did not receive any funding in Fiscal Year 2017-2018.

Florida Technology Seed Capital Fund¹⁶

The ICPR also administers the Florida Technology Seed Capital Fund as a corporate subsidiary. The fund was preceded by the Florida Research Commercialization Matching Grant Program, which expired in 2013, and the Seed Capital Accelerator Program (SCAP).¹⁷

The fund was established to “foster greater private-sector investment funding, to encourage seed-stage investments in start-up companies, and to advise companies about how to restructure existing management, operation, or production to attract advantageous business opportunities.”¹⁸ Proceeds from sale of equity or debt repayments are returned to the fund for reinvestment.

A company at the initial seed-stage investment is eligible to receive investment from the fund only after undergoing a peer-reviewed process undertaken by the fund's investor advisory board. The ICPR will invest in a company if:¹⁹

- The company's overall health and ability for growth is strong, including its intellectual property position, management capability, paths to market or commercialization, growth-potential, and ability to leverage additional funding;
- The company was identified by a publicly funded research institution;
- The company is a target industry business;
- The company was identified by a private-sector lead investor who has performed industry-standard due diligence; and
- The advisory board and fund manager reviewed and recommended the company's proposal.

¹⁴ See Institute for Commercialization of Public Research, *For Entrepreneurs: Frequently Asked Questions*, available at <http://www.florida-institute.com/about/faq> (last visited Feb. 17, 2018).

¹⁵ Office of Economic and Demographic Research, *Return-on-Investment of the Florida Microfinance Loan and Microfinance Guarantee Programs* (Jan. 2018), p. 43-45, available at <http://edr.state.fl.us/Content/returnoninvestment/MicrofinanceLoanandGuaranteeProgams.pdf> (last visited Feb. 18, 2018).

¹⁶ Section 288.96255, F.S. Institute for Commercialization of Public Research, *For Entrepreneurs: Company Funding*, available at <http://www.florida-institute.com/programs/company-funding> (last visited Feb. 5, 2018).

¹⁷ See s. 288.9552, F.S. (2011), and s. 39, ch. 2011-76, L.O.F.

¹⁸ Section 288.26255(1), F.S.

¹⁹ Section 288.96255(3)-(4), F.S.

Through the fund, the ICPR provides seed funding in amounts of \$50,000 up to \$300,000 to qualified companies, either as debt or equity. A cumulative investment of \$500,000 is the maximum the ICPR will invest in a single company before it requires a 2:1, private sector match of the investment. The ICPR has invested in a total of 66 companies through this program.²⁰

III. Effect of Proposed Changes:

Institute for Commercialization of Florida Technology

The bill creates the Institute for Commercialization of Florida Technology (institute) as a successor to the ICPR. The institute differs from the ICPR in several ways. Namely, the institute: (1) will be operated by a private fund manager rather than a professional staff; (2) will no longer partner with publicly supported universities or research institutes to support their commercialization efforts; and (3) will not be supported by or function under the department.

Section 3 amends s. 288.9622, F.S., to evince legislative intent to permit the use of a private asset manager familiar with the seed and early stage investment industry in Florida to reduce the operational costs of the Florida Technology Seed Capital Fund (Technology Fund) and the SCAP. It is the goal of the Legislature to operate these entities without requiring ongoing state expenditures.

Section 5 amends s. 288.9655, F.S., to replace the ICPR with the Institute for Commercialization of Florida Technology. The purpose of the institute is to assist in the commercialization of products developed by innovation businesses; advise the businesses about how to restructure existing management, operations, product development, or service development to attract further business opportunities; foster greater private sector investment funding; and encourage seed stage investments in startup and early stage companies.²¹

Creation of the Institute

Section 1 amends s. 20.60, F.S. to remove management of the ICPR and promotion of the commercialization of products, services, or ideas developed in public universities or institutions from the department's duties and purposes. The bill specifies that the institute is not a direct-support organization of the department.

Section 5 amends s. 288.9625(1), F.S., to provide that the institute is not subject to the control, supervision, or direction by the department in any manner. The section also amends s. 288.9625(3), F.S., to remove the requirement that the institute's articles of incorporation be approved by the department.

Board of Directors

Section 5 reorganizes the Board of Directors to consist of three members instead of five and provides for currently appointed directors of the ICPR to finish out their terms. Going forward,

²⁰ Institute for Commercialization of Public Research, *For Entrepreneurs: Company Funding*, available at <http://www.florida-institute.com/programs/company-funding> (last visited Feb. 5, 2018).

²¹ See lines 206-213 and 415-424 of the bill.

to replace a vacant board position the private fund manager will submit three recommendations to the board for consideration. The board and the private fund manager each have a vote to select a new board member from the recommended list or “from a new list of three nominees that were not included on the previous list.” It is unclear who nominates the new list.

The board’s duties include oversight of the private fund manager’s activities; performance of duties as outlined by the institute’s bylaws; and provision of an annual report of the institute’s activities to the Governor, President of the Senate, and Speaker of the House.

The directors must have expertise in selecting and supervising early stage investment managers or in fiduciary management of investment funds and other pertinent areas of expertise.

The directors may not receive compensation for their service but may be reimbursed for expenses as approved by the private fund manager pursuant to s. 112.061, F.S. Additionally, the directors may not have a financial interest in any investment in any of the institute’s portfolio companies and are subject to any restriction on conflicts of interest as specified in the institute’s organizational documents. The institute must indemnify its directors and the private fund manager to the broadest extent possible.

Private Fund Manager

The bill states that the “purpose of the institute’s use of a private fund manager is to alleviate the state’s burden of the continued and future operational and management costs related to the [Technology Fund] and [SCAP] program.”

Eligibility

Section 5 provides that the private fund manager (fund manager) must be a for-profit limited liability company or a for-profit corporation that was formed and is governed and operated in accordance with ch. 605 or 607, F.S. Additionally, the fund manager may not be a public corporation or instrumentality of the state; is not a state agency; cannot claim sovereign immunity; is not subject to ch. 287, F.S., regarding procurement of goods and services; and is not governed by code of ethics provisions in part III of ch. 112, F.S.

The fund manager must be experienced in the field and must specifically have:

- Expertise and experience in the management and operation of early stage companies in Florida;
- Experience with early stage business ventures investments in Florida;
- Working knowledge and understanding of the institute’s investment portfolio and relevant industries of those companies; and
- Individuals in its employ who have knowledge of the institute’s investment portfolio and its companies, as well as financial, technical, and business expertise to manage the Technology Fund activity.

Duties

Section 5 provides for the fund manager’s duties as they relate to the institute; **section 6** provides for the duties as they relate to the Technology Fund. They are substantially the same duties.

The fund manager is required to manage the investment-related affairs of the institute, including management of the assets of the institute's Technology Fund and SCAP investment portfolios; and conduct activities on the institute's behalf in accordance with law.

The fund manager must also issue an annual report to the Board of Directors by November 1 each year. The annual report is a public record, and must include:

- Information on any assistance provided to an innovation business;
- Description of the benefits that accrue to the state as a result of the institute's activity; and
- Independently audited financial statements, including information related to the receipt and calculation of the net profits of the investment portfolio.

The fund manager is authorized to:

- Negotiate terms of investment, sale, and liquidation with portfolio and nonportfolio companies;
- Execute contracts and contract amendments with portfolio and nonportfolio companies;
- Seek new qualified companies to participate in the Technology Fund;
- Receive and remit investment capital from the sale or liquidation of any part of the institute's investment portfolio, loan proceeds, or other investment returns;
- Mentor, assist with the development of marketing information or business plans, and assist with attracting capital investment and other resources to a portfolio company in order to foster its growth, marketing, or business success;
- Market the Technology Fund and accelerator program to potential investors;
- Facilitate meetings between prospective investors and the institute's portfolio companies; and
- Collaborate with publicly supported organizations that may be able to provide further resources or special knowledge to the institute's portfolio companies.

The fund manager is paid reasonable fees consistent with the standard practices of the fund management industry, consisting of:

- An operational management fee, including reimbursement of expenses that is paid from the proceeds of loans repaid to the SCAP or other capital, proceeds, and returns available in the Technology Fund;
- A portfolio fee paid from proceeds of each sale or asset liquidation from the institute's investment portfolio; and
- A closing fee paid from the investment amount paid by the Technology Fund to a company at the closing of each investment.

Florida Technology Seed Capital Fund

Section 5 outlines the institute's mission, which is to develop partnerships with, in particular, "innovation businesses" as defined in s. 288.1089, F.S., relating to the Innovation Incentive Program.

Section 6 provides that the institute must also strive to invest in target industry businesses, as defined in s. 288.106(2)(q), F.S., which represent diverse and stable markets.

Section 6 amends s. 288.96255, F.S., the Technology Fund, to revise the authorized investments and requirements for investment. The institute may select a company or organization for partnership with the institute or for funding from the Technology Fund only after the fund manager, using processes modeled on the investment industry's standard practices, has evaluated whether the company meets the statutory requirements, which are similar to current law. The fund manager must complete due diligence before approving a company for investment.

The bill repeals statutory limitations on investments from the fund – specifically the current limitation of initial investments of \$50,000-\$300,000, a cumulative maximum of \$500,000, and a required 2:1 match for additional investment.

Net profits from proceeds of sale or liquidation of assets or portions of assets of the investment portfolio will be returned to the Technology Fund for reinvestment, after payment of applicable costs, professional fees, expenses, fees paid to the private fund manager, and disbursement to private investors.

Fees paid to the private fund manager include are for performing due diligence and an investment closing fee, in addition to reasonable attorney fees, the operational management fee, the portfolio fee, the closing fee, and other costs in connection with making the investment.

The institute or the private fund manager can disburse payments to private investors if the institute or the private fund manager decides to transfer any portion of the Technology Fund into a private fund or special purpose vehicle. Such private fund or special purpose vehicle can receive additional private investment. The disbursement from such private fund or special purpose vehicle back to the Technology Fund or private investors is the respective pro rata portion of any net profits from the sale or liquidation of assets in the private fund or special purpose vehicle.

Public Records and Meetings Exemption

Section 7 amends s. 288.9627, F.S., to transfer the public records and meetings exemption that previously applied to the ICPR to the institute.

This section makes the following materials held by the institute exempt from disclosure pursuant to s. 119.07(1), F.S., and s. 24(a), Art. I of the Florida Constitution:

- Documents and materials that related to a business' methods of manufacture or production, potential trade secrets, or patentable material that is provided to the institute by a proprietor;
- Information that would identify an anonymous investor or potential investor;
- Information received from another person, state, nation, or the federal government, which is confidential or exempt pursuant to the originator's laws; and
- Proprietary confidential business information.

Additionally, the bill exempts from Florida's public meetings laws those portions of the institute's meetings wherein information that is confidential and exempt according to Florida law is discussed.

Miscellaneous

Section 2 makes conforming changes to s. 288.9621, F.S., the short title for the Florida Capital Formation Act.

Section 4 provides definitions for terms used in the Florida Capital Formation Act.

Section 8 provides an effective date of July 1, 2018.

IV. Constitutional Issues:**A. Municipality/County Mandates Restrictions:**

None.

B. Public Records/Open Meetings Issues:

The bill transfers the current public records and meetings exemptions for the ICPR to the institute. The bill also expands the scope and authority of the institute to make investments in seed and early stage businesses. It is unclear if the amendments made by the bill to ss. 288.9625 and 288.96255, F.S., would be an expansion of the current public records and meetings exemptions.

C. Trust Funds Restrictions:

None.

V. Fiscal Impact Statement:**A. Tax/Fee Issues:**

None.

B. Private Sector Impact:

Depending on the financial performance of the Technology Fund and the institute, there may be a reduction in the funds available for investment in private businesses that seek investment capital.

C. Government Sector Impact:

The ICPR did not receive an appropriation in Fiscal Year 2017-2018. The bill attempts to reduce future appropriations to the successor institute for its investment, management, and related expenses, by permitting the institute to fund itself through its activities. According to the most recent independent audit of the ICPR completed in Fiscal Year 2016 filed with the Florida Auditor General, the total program expenses were

\$3,732,937.²² The fund manager will require expenditures pursuant to statute, but these will be made from profits of the institute, rather than state appropriation.

University and other publicly funded research institutes may see a reduction in funds available for the commercialization of their technologies because of the privatization of the institute.

The Department of Economic Opportunity may experience minimal cost savings by eliminating the contracting and related oversight responsibilities of the department over the institute.

VI. Technical Deficiencies:

It is unclear whether the duties outlined in s. 288.9625(5), F.S., apply to the Board of Directors or the fund manager.

VII. Related Issues:

The bill refers to the SCAP or “Accelerator Program.” The Accelerator Program expired in 2013, and therefore does not require any ongoing operational funding. The Accelerator Program, however, does have outstanding loans that will not be due until December 2019, and therefore may require actions by the fund manager for purposes of collection and reinvestment of the funds.²³

The bill provides that the institute must create the Fund; the Legislature could directly create the Fund.

The bill requires that a company or organization be “based in” Florida to receive assistance from the institute. This term may need to be defined to provide clarity in interpretation.

VIII. Statutes Affected:

This bill substantially amends the following sections of the Florida Statutes: 20.60, 288.9621, 288.9622, 288.9623, 288.9625, 288.96255, and 288.9627.

²² Florida Auditor General, *Institute for Commercialization of Public Research: 2015-16 Fiscal Year*, available at https://flauditor.gov/pages/nonprofit_forprofit%20pages/institute%20for%20the%20commercialization%20of%20public%20research.htm (last visited Feb. 16, 2018).

²³ *Id.* at p. 21.

IX. Additional Information:

- A. **Committee Substitute – Statement of Substantial Changes:**
(Summarizing differences between the Committee Substitute and the prior version of the bill.)

Recommended CS/CS by Appropriations Subcommittee on Transportation, Tourism, and Economic Development on February 21, 2018:

The committee substitute:

- Restores a portion of current law legislative intent related to the Florida Opportunity Fund;
- Adds a provision that the Institute for Commercialization of Florida Technology is not subject to the control, supervision, or direction of the DEO; and
- Corrects a grammar issue.

CS by Commerce and Tourism on February 6, 2018:

The CS clarifies the terms for directors appointed before July 1, 2018, and the succession of any director appointed thereafter.

- B. **Amendments:**

None.