

MINUTES OF THE SENATE COMMERCE COMMITTEE

The meeting was called to order by Chairperson Susan Wagle at 8:30 a.m. on March 4, 2011, in Room 548-S of the Capitol.

All members were present.

Senator Schodorf – excused
Senator Faust-Gaudeau - excused

Committee staff present:

Ms. Margaret Cianciarulo, Committee Assistant
Mr. Ken Wilke, Office of the Revisor of Statutes
Mr. Reed Holwegner, Kansas Legislative Research Department
Ms. Dorothy Noblitt, Kansas Legislative Research Department

Conferees appearing before the Committee:

Mr. Thomas Thornton, President & CEO, Kansas Bioscience Authority

Others attending:

See attached list.

Continued Overview of the Kansas Bioscience Authority

Upon calling the meeting to order, Chairperson Wagle announced they were going to continue their overview of the KBA. The Committee did have some questions from their last meeting of February 22, 2011, and the KBA has submitted a new booklet that was given to the Committee yesterday. She first wanted to point out some documents the Committee has before them, saying they had a lady by the name of Melissa Lynch, who was going to come today to testify who formally worked for the Bioscience Authority as an executive assistant.

- 1.) The first item before them is a contract where Ms. Lynch was offered a job with the KBA and worked there between 2006-2008.
- 2.) Next is a letter to the Committee from Ms. Lynch, and since she could not be here to testify because she had to work, the Chair will read the letter to them.
- 3.) The third handout is an anonymous fax the Chair received about a form and how the KBA analyzes job growth.
- 4.) Last is a scope statement from Post Audit entitled, “Kansas Bioscience Authority: Reviewing the Appropriateness of Its Expenditures.”

She then read the letter she referred to in the second handout. A copy of the above four handouts are (Attachment 1) attached and incorporated into the Minutes as referenced. A copy of the new KBA booklet dated march 4, 2011 is (Attachment 2) attached and incorporated into the Minutes as referenced.

The Chair asked Mr. Thornton if there was an insurance policy that the Board has been covering? (He would like to respond to what he has read very briefly and then will answer her question. He said Melissa Lynch was the first executive assistant at the KBA and he did in fact hire her. She and he were, in fact, the only ones in that office for quite some time. Jan Katterhenry was the next hire as our Chief Financial Officer. Ms. Lynch was terminated for just cause, amongst other things. He can't speak to specifics, but would be more than happy to speak to the specifics in writing if that is acceptable to you and the Committee. He would tell them his contract is approved by the Board of Directors and likely as I am sure, our Chairman and Vice Chairman who are here with me, I will tell you this is consistent with other employment policies and agreements with people under similar situations. The answer to the question is yes.) So there is an insurance policy that the State is paying for, a life insurance policy? (The KBA most definitely paying for a term life insurance policy. And who is the beneficiary? (My children are.) Can you address the personal bills that she was asked to pay, including the lawn service? (I believe that she would be correct in that on occasion, I would have asked her to do that. I believe on occasion, she would have access to my bank account and I will provide the reasons and cause for which Ms. Lynch was terminated.) Does the Authority pay for a car? (They do) Then you also submit mileage in addition to the car payment?

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(I do not know.) So there are personal expenses being paid for out of finances of the Bioscience Board? (Is that the question you're asking?) Yes. (What I was responding to is this, she has my personal checkbook, she paid my lawn care bill, that's what she did and I believe, if I read that correction, I'm not sure how she has stated that. If you are stating that any other way, I would say that is incorrect.)

The Chair said she thinks what we are most concerned about here is the use of taxpayers dollars and about the salaries and bonuses. We have a 2010 budget submitted, salaries and expenses in 2010, and a list of increases in salaries from 2009. We also have an audit statement that the salary totals do not equal what the Committee received in the last book. (If you don't mind Madame Chair, I would like to call upon our Chairman. The Board of Directors not only sets but is responsible for compensation reviews and performances. This Board is very well engaged and if you don't mind, I am going to call on Governor Carlin, who is our Chairman and is joined by our Vice Chairman, Dr. Ray Smilor. He then asked the Chairman, if he could please address the issues of how compensation is set, how my performance is reviewed and evaluated and just generally, the compensation process of the Board? Governor Carlin said he can assure the Committee that the Board is very actively involved, particularly on the issues they are interested in regarding the terms of compensation, in terms of bonuses for not only Mr. Thornton but the other members of the staff. You and your colleagues in 2004 gave the State of Kansas a huge opportunity in his opinion the best piece of legislation that has been passed in the State's history in terms of giving Kansas some chances they would not have had otherwise. So he commends Chairperson Wagle and your colleagues who were a part of that and who have certainly been supportive of the KBA since its inception.)

The Chair asked Governor Carlin what year he went to the Bioscience Board? (I think it would have been 2006 in the spring. I finished a term and now I am in my third year of a reappointed term. He went on to say, we recognized that in order for us to do a good job, and you have given us the opportunity to do that, we had to pay salaries to attract the talent, retain the talent to get the job done. We would be happy this morning to share with you. You have asked for specifics which rightfully you should, and we welcome this opportunity quite frankly to communicate with you. We will give you some information this morning, of comparable salaries and benefits from other organizations across the country. For example, one of them we will share with you is the State of Georgia. They have an organization, the title is a little different, but the function is very similar. You will find the salary compensation very similar to what we have here. The difference is, Georgia was one of our competitors for getting the NBAF and you will note that their person did not get a bonus in the year they lost the NBAF. Yes we did provide a bonus, it was an incredible achievement and we would not have been in that position if we had not been able to hire Mr. Thornton, who was the Policy Director for Dennis Hassert, Speaker of the House, that is the one in Washington, D.C., and who has had similar experiences with entities in the State of Illinois. We would not have gotten NBAF. You get what you pay for. I understand why you asked the question and have no problem with your asking the question. We welcome the opportunity to respond. But you cannot attract and retain talent capable of carrying out your direction, without being willing to pay. And in addition to that, we didn't just distribute money and go on to the next request. We work with people to really make projects work. We stay with those projects and monitor them. We monitor outcomes on a regular basis. We know where every single investment is on a regular basis. It takes time and talent in order to help start-up companies to really succeed. Now if we cannot hold their hands, applaud and encourage them, we have to bring advice. We have got to help them secure the additional capital that will allow them to succeed, to have the proper structure to hire the talent they need to hire. The Centers we have put together, the fourth one will be coming, we have three now, one out of Wichita, one out of Lawrence Kansas City, and one out of Manhattan. The talent they had to hire to work with the private sector, comparable salaries to what we pay Mr. Thornton, obviously a smaller project. So we are very comfortable sharing with you the philosophy that we have had, the processes, I think even shared some of the stuff we have been through. We went outside in consulting to make sure we were competitive, we just wanted to find out after the fact, they that we weren't competitive with salaries and generally speaking consultants say they are in about the 75 percentile in terms of salaries.)

Chairperson Wagle asked for questions which came from:

1.) Senator Masterson who asked Governor Carlin what types of accountability do you have in place for not only you but your employees, that you look at, not necessarily on the compensation side but what appears to be on the expense side? How often do you go through that and hold people accountable for

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that? (In terms of personal expenses, what I mean by personal, not appropriate reimbursement travel, etc. that all comes to me to sign off on. Ms. Katterhenry has gone through the specifics, so I accept responsibility for those specifics during my tenure as Chair of the KBA. But we have a total package. We have an accounting team from Wichita that comes in, that works year round with us to audit everything and to make sure everything is appropriate. And the Board spends a lot of time, on a regular basis, staying in touch with what's being done, asking the questions. Ray, our Vice Chair is with me this morning and we feel very comfortable that we are getting the attention we need, getting the information we need, we are following through and yes, accountability is key, absolutely.) The only thing I was concerned about was the class by which you travel, seeing expenses from Ritz-Carlton and limousines and things like that. Do you approve of the travel and expense for an agency like this? (We approve of that level if it is appropriate for what is being done. We deal with folks who travel in those circles and consequently from time to time, yes we have to do something that a lot of us Kansas, including myself, would say that's a little beyond what should be necessary. But the reality is we want to be successful, continue growing beyond the success we have, with the opportunity you have given us and we don't want to come back and say we did it on the cheap, it didn't work out, we're sorry, but we saved a lot of money in salaries. We didn't pay what we should have been paying, it hasn't worked out, we didn't get the return, were not getting investment, were not adding employment, but we saved a lot of money because we cut it tight. I am not surprised you asked the question.)

2.) Senator Lynn asked about the Heartland BioVenture saying in the March 4, 2011 report they have listed their salaries and so forth and the bonuses that were awarded, listed on another sheet that they got earlier, showed that they received \$36K in bonuses. Can they explain why the bonuses do not appear in the March 4, 2011 report? And if those bonuses were indeed given, and what concerns her, not so much in what salaries are, as you know state employees normally don't get compensated at a high rate, but thinks what is hard to explain is the bonuses. She has asked for some response on how those were calculated and how they were given. That's question number one. The other question is, do any of the Heartland BioVenture staff live outside the state? (Mr. Thornton answered saying, the material we provided last time was through 2011. The material provided in the book, which is the most current, which is under Tab 1, page 2, is for 2010. Heartland BioVentures is a program that the Bioscience Authority rated. It is based upon successful models in other states. Its goal is to work with very early-stage bioscience companies and in some cases, literally just entrepreneurs that can create jobs, attract capital and take products to market. It is one the Board of Directors prioritized. But it is a new program, so the figures you see under Tab 1, page 2 reflect a very basic fact at that point, the KBA had literally just hired some of these staff and grew that staff over the months to the team it is now. The second part of your question relates to, are there people who live outside the State of Kansas and the answer is yes, one. His name is Dr. Terry Osborn, an individual with a great background as an entrepreneur and who has been able to attract early-stage venture. He lives here throughout the week.) To Ms. Katterhenry, she said she just wants to make sure she understands the bonus sheet they provided, could she explain. (The bonuses that you received last time, the first part show the bonus of \$170.5K relates to FY2010. And so far as bonuses for that particular staff, what were they were based on was a formula or percentage of profit. Mr. Thornton said, first of all, these are staff that are extremely capable individuals with MBA's and most with strong pharmaceutical backgrounds. The fact that they are inside the KBA, actively engaging in these early-stage companies actively helping them sharpen their commercialization pathways is really a testament to the KBA. As it relates directly to their bonuses, each of them deals with portfolios of companies and are broken down by individuals that have expertise in bioenergy, background in animal health, etc., so are sector specific. Within those sectors, they manage a portfolio of companies. So if they have been directly associated with that company, raising private capital, getting a strategic partnership, etc or some strategic exercise that fundamentally facilitates investment in the State of Kansas, formation of jobs or a recruitment of a potential strategic partner, that's the kind of outcomes we want to see from these guys.)

Senator Lynn said she respects all of their expertise and asked, do they sign some kind of disclosure in terms, because if they are out there and experts in their field, other people want them, right? (Yes.) So what kind of operational things do you have in place and do they work for anybody else, do they consult with anybody else? And is there a reason why you need to bonus them? Are you afraid they are going to be hired away or what is the justification and what do you have in place to protect us? (Mr. Thornton said his compensation philosophy is similar to the Board of Directors which is, for example, give someone a salary say of \$1.00 and you pay them a base of \$.80 and then if they hit a performance milestone in

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metrics, they actually move the needle and substantially affect economic development in our state, they can earn up to that dollar. With respect to non disclosures, we do them at the company's election. We ask the companies to not provide us material that they deem to be confidential. Extents where they need to better understand the material that is deemed to be confidential and in the interest of the relationship we will sign confidentiality or nondisclosure agreements, whatever we are talking about there. As it relates to outside consulting, doesn't happen.) Don Colbert receives around \$4K, right? (Ms. Katterhenry said he was a new employee. Mr. Thornton explained Mr. Colbert's position saying he joined as a shared employee between the Kansas Technology Enterprise Corporation or KTECH and the KBA. His specific role is to help early-stage companies pursue approximately \$2B in Federal technology development grants, with the largest program under that is called the Small Business Innovative Research Program or SBIR and went on to explain that grant program. When are bonuses usually paid? (Mr. Thornton said our fiscal year is tied to the states Fiscal Year. The KBA puts in place prior to the beginning of each fiscal year, an annual operating plan or an AOP. This plan takes a wide variety of KBA plans, but this is something the Board puts together, they set the budget, sets the level of compensation for him for a three year contract for approximately the first year of the contract. Performances are evaluated at the end of that fiscal year so that would be typically June, July, August.)

The Chair said regarding the bonuses, she just wanted to point out in addition to the audit, numbers on the wages are different from what was given to us in the last booklet, different from the piece of paper and what is in the book. (Jan Katterhenry said what we did for you last time is give you an annualized number for 2011. On the bonuses, the difference between this time and last time for 2010, when we gave you the bonus sheet last time, we took our current employees and said what was their bonus. The one person that is missing is Chad Bettes, because he is no longer with us. So if you wanted to reconcile the differences between the two, you would need to take Mr. Bettes' wages off the 2010 page and that would give you the total and the others is what I explained before.) And how are bonuses reported to the IRS? (It goes through our normal payroll process, goes through the W2.)

4.) Senator Holland has been serving on the KTECH Board and from his perspective, does not see anything unusual regarding Mr. Thornton's salary and bonuses . He did ask Governor Carlin to talk about some of the unique skills that Mr. Thornton brings to the table and how do you find that skill set out there and why we are paying a premium. (Probably more than anything is experience. We are not an operation so large that we can start folks down below and give them 5 to 10 years to really grow into capacity, they need to hit the ground running. When we hire somebody they have to have the capacity to deliver. Mr. Thornton had Washington, D.C. experiences and also in the State of Illinois, with a comparable entity doing similar work and being successful at it. It's his combination of experience, understanding how the private sector works and relates to government, its collaboration we are working on here, and that includes universities. It helps when someone understands those different cultures and entities and how they work, and be able to pull things together. Using the NBAF specifically, he understood instantly how to put a plan together to make that possible. He did not think they had anybody else. And for Kansas to win over Texas for the NBAF, it took someone who could get in for meetings in Washington, D.C. and present a plan.) His feeling on this compensation deal is if we go back to the basics as far as looking at the ROI of the KBA, that's what we need to evaluate that staff on. He suggests the Committee go back and look at a report done by GSP Consulting Corporation in the KBA's original four years in existence and referred them to page 22 where GSP lauded the KBA and feels we need marketing literature like this to reach out to potential business customers through the nation and should be doing some advertising in some of these publications. His second comment was found on page 13 regarding monitoring the staffing as activity increases. They quote a figure for one FTE of \$5M in active investment. When he looks at what KBA's committed funds are, as of today \$250M and a staff of around 21 people and consulting outside, you are keeping up with the parameter of that one FTE and could he hear comments on this? (Mr. Thornton said the report was done on behalf of Kansas Inc. and it also stated the KBA needed to do a better job of establishing what we were doing here in Kansas. As it relates to staffing, they think it is appropriate, based entirely on their annual operating plan. Regarding equivalent organizations, a sheet that was passed out earlier listing organizations that are similar to KBA.)

The Chair said she supported NBAF, voted for the bill, was excited about KBA, and it was a collaborative effort. On the other hand, you have a budget of about \$35M a year now and have purchased a building for \$12M. She asked how it is financed? (Ms. Katterhenry explained it was a construction loan, a 10-year note over 20 year amortization, and will reprice every three to five years based on our choice, tied to the note.) Do you expect to make the payments on that out of your allotment from the legislature? (Yes,

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we have forecast it out based in our current commitments.) Do you anticipate what the payment would cost? (I have it in my forecast, but I can't tell you right off the top of my head, but I can get it to you.) From the way I read your books, we have \$177M in committed funds in the future on a diet of \$35M. In this atmosphere where everybody is taking pay cuts, the money seems extremely excessive in this environment on salaries. We do have healthcare nonprofits in Kansas where they are giving out millions of dollars that were earned in assets from sales, and their salaries aren't nearly this high.

Regarding Ms. Lynch, she said she figures there would be conflict in testimony and that you would say she had been fired and she said she gave two weeks notice. She does testify in here that she was given personal receipts to be paid and that is a concern. The Chair feels this Committee has raised legitimate concerns about how money is being spent. We are excited about your success and we want it to be successful and continue to grow but there are some problems here that taxpayers see that are lavish.

The Chair called on Senator Masterson who said in looking at these job numbers, about 75% of them were in two companies, one being mainly Quintiles and see they are in 60 countries and employ 20K employees. How do we validate what we did with them to create that? (The report Senator Holland referenced actually recognized the KBA in two regards as it relates to outcomes. First, they actually have an outcomes policy. The Board of Directors, working with staff, has actually determined what were the outcomes we actually want to track and then what is the methodology we want to employ to actually track those jobs. We provided that to the Committee as it relates specifically to jobs though. It must be a new job and must be in the biosciences so that all the other jobs it might impact are not counted. They must be attributable directly to the KBA project investment. With respect to what is not included, it was referenced in questions we were asked to provide. There is no multiplier affect associated with that. We do not track indirect outcomes associated with those jobs. We have a similar policy for: the research funds that flow back to research universities, for venture policy investment, and for capital expenditures associated with the KBA's investments. As it relates to Quintiles, the KBA diversifies.) How do you go in and validate? Do they fill out the form and we just take their word for it? (I'm sorry, I missed your point. If there was a delta between what we have seen in the past and what we see year-to-year, we do audits. Ms. Katterhenry calls for those. They are not done by the Bioscience Authority. They are done by an external third party and come back to us. And we are auditing effectively, how are the funds used, and how were the outcomes associated with our direct project.) Do they actually get into Quintiles books then? (The outcomes associated, yes.)

The Chair asked the Committee to look at the scope statement from Post Audit on a forensic audit of the Bioscience Authority. A forensic audit is where you to in and look at the payment then look at the receipt that are attached to the payment. She says they will talk about the audit next week.

Adjournment

As it was going on 9:30 a.m., the Chair announced they stand adjourned.

The next meeting is scheduled for April 1, 2011.