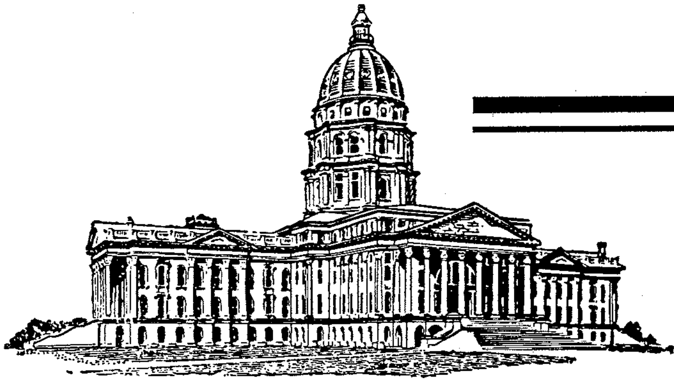

PERFORMANCE AUDIT REPORT

REVIEWING THE COMPENSATION OF EXECUTIVES OF THE STATE'S ECONOMIC DEVELOPMENT AGENCIES

A Report to the Legislative Post Audit Committee
By the Legislative Division of Post Audit
State of Kansas
September 1996

96-55

Legislative Post Audit Committee

Legislative Division of Post Audit

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September 25, 1996

To: Members, Legislative Post Audit Committee

Senator Lana Oleen, Chair
Senator Anthony Hensley
Senator Phil Martin
Senator Alicia Salisbury
Senator Don Steffes

Representative Jim Lowther, Vice Chair
Representative Tom Bradley
Representative Duane Goossen
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Representative Ed McKechnie

This report contains the findings, conclusions, and recommendations from our completed performance audit, *Reviewing the Compensation of Executives of the State's Economic Development Agencies.*

The report includes a number of recommendations for improving the State's ability to deal with conflict-of-interest situations that may arise between economic development agency employees and the companies they assist.

We would be happy to discuss these recommendations or any other items in the report with any legislative committees, individual legislators, or other State officials.

Barbara J. Hinton
Legislative Post Auditor

Question 1: How is the Compensation of Executive-Level Staff in Kansas' Economic Development Agencies Set, and How Do Their Responsibilities and Compensation Compare With Their Counterparts in Other States?

Compensation for the heads of economic development agencies is set by appointing authorities, often based on comparative information. *Their compensation is set by the Governor, the boards they report to, or the deans of the academic departments they work for. The agency heads set the compensation for their employees. Four economic development agency executives make $100,000 per year or more. Salaries generally were determined through comparisons with similar positions in other agencies. One or more employees in KTEC, MAMTC, and the commercialization corporations were eligible to receive bonuses, but they seldom received the full amount allowed.* .... page 10

Compared to other states' economic development agencies, salaries for agency heads in Kansas were near the middle of the range. *Salaries for the President of Kansas Inc. and the Secretary of Commerce and Housing fell within the middle-to-low end of salaries in other states with comparable agencies. The salary and benefits package for the President of KTEC also was in the middle of such salaries, and was comparable to salaries paid to the heads of non-profit and private entities doing similar ty pes of work. Most agency executives received benefits comparable to their counterparts in these other states.* .... page 15

Question 2: What Relationships Exist Between Economic Development Agencies and the Companies They Assist, and Are Adequate Laws and Procedures in Place to Deal With Conflicts of Interest That May Result From Those Relationships?

We identified a number of relationships between economic development agency staff and the companies they assisted. *Overall, relationships between employees and the companies they assist were relatively uncommon. Of the 680 companies in our database, we identified relationships in only about 2% of them. However, of the 61 new technology-based companies we reviewed incorporation records for, we identified relationships in 13 of them, or 21%. Not all of the relationships represented conflict-of-interest situations. Most existed between KTEC employees or the employees of the centers of excellence, and the companies they assisted. In most cases, the types of assistance these companies received was technical, rather than financial.* .... page 20

This audit was conducted by Ellyn Sipp, Laurel Murdie, and Scott Brunner. If you need any additional information about the audit's findings, please contact Ms. Sipp at the Division's offices. Our address is: Legislative Division of Post Audit, 800 SW Jackson Street, Suite 1200, Topeka, Kansas 66612. You also may call (913) 296-3792, or contact us via the Internet at: **LPA@PostAudit.ksleg.state.ks.us.**

Reviewing the Compensation of Executives of the State's Economic Development Agencies

During the 1996 legislative session, the Legislature passed House Bill 3068 prohibiting any officer or employee of the Kansas Technology Enterprise Corporation (KTEC) who receives a State-funded salary from receiving any other compensation for duties related to a KTEC subsidiary, or to a business in which KTEC has invested State funds. In addition, the bill required that before any employment contract is executed or renewed with the President of KTEC, it must be made available to the legislative economic development committees.

During discussions of the bill, legislators raised a number of questions about the compensation of executives in the State's economic development agencies, including the Department of Commerce and Housing, Kansas Inc., KTEC, the Mid-America Manufacturing Technology Center, and the centers of excellence.

Questions focused on such things as executives' salaries and other compensation, the funding sources of their compensation, who determines the compensation, how the executives are evaluated, how often they are evaluated, and how their compensation, responsibilities, and the organizational structure of their agencies compare with counterparts in comparable agencies in other states. Questions also were expressed about whether Kansas has adequate laws, policies, and procedures to address issues such as conflicts of interest, financial disclosure, and codes of ethics for economic development officials.

In addition, legislators wanted to know how many start-up companies or spin-offs are being funded or supervised by economic development agencies, and what sort of financial and contractual relationships exist between these entities and the agencies that fund them. This performance audit addresses the following questions:

1. **How is the compensation of executive-level staff in Kansas' economic development agencies set, and how do their responsibilities and compensation compare with their counterparts in other states?**

2. **Are adequate laws and procedures in place and being followed to guard against conflicts of interest for State officials responsible for administering economic development moneys?**

3. **What relationships exist between State economic development agencies and entities that come into existence as a result of funding they provide?**

For reporting purposes, questions two and three have been combined.

To answer these questions, we gathered information on employee compensation and evaluation from Kansas' economic development agencies, and from several entities affiliated with them. We reviewed State laws, policies, and procedures, interviewed economic development agency executives, and reviewed budgetary and program information. To identify relationships among agency staff and the companies they assist, we surveyed economic development agency employees, and reviewed statements of substantial interest, income tax returns, and corporation records available from the Secretary of State's Office. We also reviewed agency records pertaining to a sample of companies that had received economic development assistance from the State. Finally, we contacted a limited sample of other states to find out about their compensation and evaluation policies, and to identify any conflict-of-interest policies.

In conducting this work, we followed all applicable government auditing standards set forth by the U.S. General Accounting Office.

In general, we found that compensation for economic development agencies' executive-level staff is set through a review of salaries in comparable organizations. Most officials are evaluated annually or quarterly, and a few are eligible for bonuses based on their achievement of certain objectives. In a few cases, economic development officials served on boards or in some other management capacity for companies they were providing assistance to, but they didn't receive additional compensation from those companies. Most economic development executives in Kansas receive compensation that's comparable to what officials in other states receive.

We identified relationships between economic development agency staff and 13 start-up technology companies they assisted. Most of these relationships involved employees at KTEC or the centers of excellence. Also, the assistance most companies received from these employees' agencies was technical, rather than financial.

Although all these relationships could have had the potential for a conflict of interest, in many cases employees disclosed their relationships, or the employees or their agencies took some action to mitigate the potential conflict. In some cases, however, such actions weren't taken when they should have been.

We found that State efforts to manage conflicts of interest aren't adequate in a number of areas. State law is unclear about whether some employees are subject to the State's ethics laws. Except for the centers of excellence, most economic development agencies didn't have written policies and procedures on conflict-of-interest situations and how they should be "managed" to avoid actual conflicts. Although the State requires many employees to file disclosure forms (statements of substantial interest), the process hasn't been set up to ensure that agencies review those forms to see if potential conflicts exist. Also, university conflict-of-interest disclosure policies require employees to list their substantial interests only if the employees think a conflict exists, and don't require university employees to report financial interests at the same level as other State employees who are required to report such interests. We also found that, unlike some other states, Kansas' economic development employees aren't prohibited from having an interest in companies that receive assistance from the economic development agencies they work for.

These findings are discussed in more detail, following a brief overview of Kansas' economic development agencies.

Overview of Kansas' Economic Development Agencies

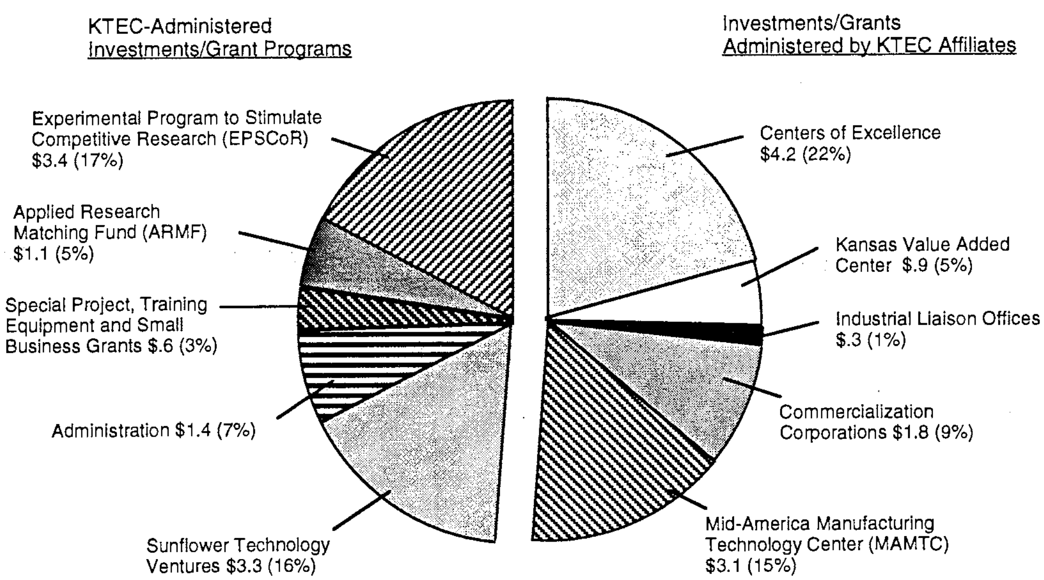
In the mid-1980s, in response to concerns about a decline in prosperity in Kansas, the Legislature commissioned two University of Kansas professors to examine the strengths and weaknesses of the Kansas economy. Based on recommendations contained in their report and made by the Legislative Commission on Economic Development, the Legislature restructured several existing economic development agencies, created several new ones, and set up the Economic Development Initiatives Fund. This Fund receives money from the sale of Lottery tickets to finance economic development activities in the State.

The primary agencies involved in economic development at the State level are described below. Because the major concerns behind the audit centered on issues relating to start-up companies, and because the Kansas Technology Enterprise Corporation (KTEC) is most closely involved with such companies, the bulk of this Overview focuses on that agency and its affiliates.

KTEC Was Created by the 1987 Legislature To Advance Science and Technology, and To Build Partnerships Between Government and Private Industry

This agency works most closely with new, technology-based start-up companies. It's governed by a 20-member board of directors made up of private and public members, including four members of the Legislature.

KTEC Operating and Program Expenditures for Fiscal Year 1996
(in millions)



KTEC's mission is to create and expand advanced technology in Kansas. In fiscal year 1996, it spent more than $20 million. About one-half its budget is used for KTEC-administered investments and programs, and the other half is for such programs administered by KTEC affiliates.

KTEC's budget for fiscal year 1996 was $20.3 million. The Economic Development Initiatives Fund, which provided more than $18 million of the agency's budget, was the primary funding source. The rest of its funds came from federal and other special revenue funds. The Corporation employed 15 full-time-equivalent staff in fiscal year 1996. The chart on page three shows how its budget is spent.

KTEC's primary activities include providing funding, equity investment, and technical expertise to develop technology-based industry. The emphasis is on developing new technologies that can be commercialized by the private sector. KTEC anticipates these investments will provide a return to the State, but over a longer-term, such as 5-10 years.

KTEC directly grants money for the following:

- to develop new products through university and business research projects
- to assist inventors, entrepreneurs, university scientists, and applicants for federal grants
- to assist entrepreneurial, technology-based businesses

One of its major programs in this area is the Applied Research Matching Fund Grant Program. Through this Program, businesses can receive grants of up to 40% of the cost of a research project to develop a product or a marketable technology. In fiscal year 1996, this Program awarded 23 businesses $1.1 million.

These awards are structured like grants, but turn into loans that are repaid by the companies if the technology "works" or the product is successfully developed. In most of the Applied Research Matching Grant agreements we reviewed, if the product was commercialized, KTEC would receive a royalty of between 1% and 3.5% of product sales to repay the amount of the grant, plus simple interest of between 5% and 10% per year. Sometimes, additional royalty payments also were negotiated. The amount to repay was larger if the product was sold to or manufactured by a company outside Kansas. The accompanying profile shows how much royalty money has been returned to the State from the Applied Research Matching Grant Program.

KTEC also created two seed capital funds—Ad Astra I and II—to make equity investments and loans to help start up companies with technology-based products. Ad Astra I was established in fiscal year 1988 with $1.8 million in Economic Development Initiatives Fund moneys, and an additional $800,000 from private investors. Ad Astra II was established in fiscal year 1994 with $1.4 million in Economic Development Initiatives Fund moneys. It received a second State appropriation of $1.5 million in fiscal year 1995. The State's investment in Ad Astra II was matched with almost $990,000 in private funds.

Investments made from these funds range from $20,000 to $250,000 each, and can be repaid with royalties or with stock in the companies. These funds are managed by a private fund manager, Campbell-Becker, Inc., in Lawrence, Kansas. The profile also shows how much the State has realized from its Ad Astra fund investments.

In 1995, the Legislature also set up Sunflower Technology Ventures as a new venture capital fund for economic development purposes. This new fund was created in part because essentially all the moneys in the Ad Astra funds already have been in-

Since 1993, KTEC Has Received Almost $600,000 From Companies Receiving Grants and Investments

KTEC can receive royalties through its Applied Research Matching Fund Program (ARMF). It also can receive dividends or other payments from its equity investments in companies it invests in through the Ad Astra venture capital funds. The following table shows how much has been awarded to companies and committed to the Ad Astra funds, and the amounts KTEC has received in fiscal years 1993 through 1996 from Applied Research Matching Fund grantees and Ad Astra portfolio companies.

Royalties Paid to KTEC From Companies that Received Money Through ARMF Grants			Money Received From Equity Investments in Companies made by Ad Astra I and II		
Fiscal Year	Funds Awarded	Royalties Received	Fiscal Year	KTEC Funds Committed	Earnings Received
1988	$731,471				
1989	450,512				
1990	1,001,772		1990	$1,799,340	
1991	1,378,552		1991		
1992	1,322,802		1992		
1993	1,119,317	$ 5,628	1993		
1994	1,202,703	14,781	1994	1,400,000	
1995	1,238,613	51,980	1995	1,500,000	$371,000
1996	1,115,292	151,339	1996		0
Totals	**$9,561,034**	**$223,728**		**$4,699,340**	**$371,000**

The money KTEC receives is turned over to its holding company, KTEC Holdings. According to the President of KTEC, the money will be reinvested in similar programs. By KTEC Board policy, priority will be given to reinvesting funds earned from a KTEC program in the same or a similar programs. The Legislature reduced its appropriation to the ARMF program from the Economic Development Initiatives Fund by $200,000 in fiscal year 1997. That amount will be replaced by royalties that have been collected from companies that received ARMF grants. The earnings from Ad Astra investments have not been reinvested.

Through fiscal year 1996, KTEC has received royalties from 13 companies that received ARMF grants. Before 1993, KTEC didn't enter into royalty agreements with companies that received such grants.

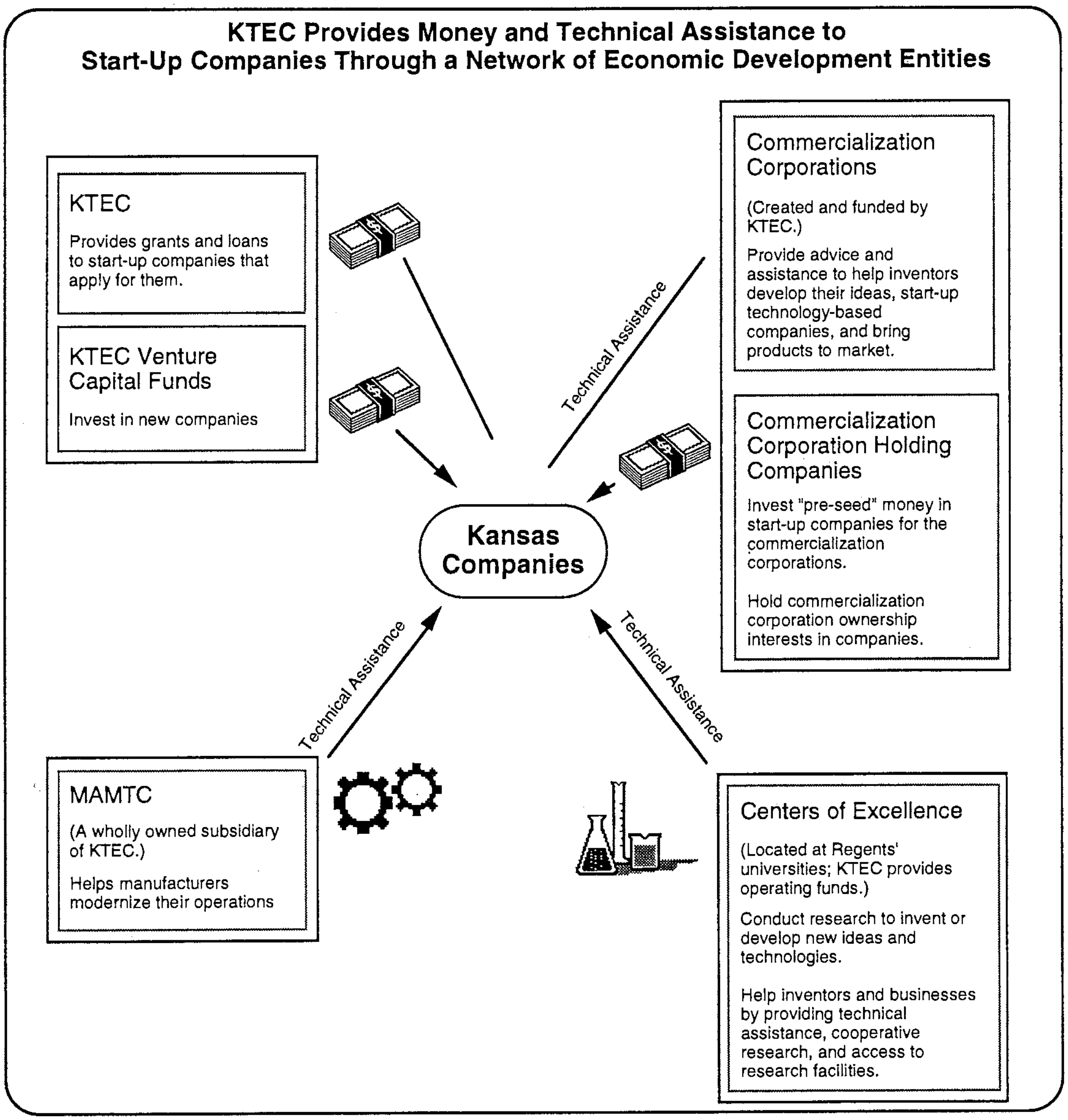
Ad Astra I invested in a total of 11 companies between 1991 and 1995. The investments in three of those companies have been written off, and one company has paid royalties back to Ad Astra I. Ad Astra II invested in 15 companies from 1993 through 1996. One of the investments has been written off, and two companies have paid royalties back to Ad Astra II.

Appendix A lists all the companies that have received Ad Astra Fund monies since fiscal year 1990. Appendix B lists all the companies that have received Applied Research Matching Fund monies since fiscal year 1988, and lists the royalties these companies have paid to KTEC.

vested, and there was a perceived need for more venture capital financing to be available to Kansas companies.

More than $3 million in State funds will be matched by nearly $7 million in private investments. With a pool of $10 million, Sunflower will apply to become a federal Small Business Investment Company, which is a venture capital firm that can package loans and other investments for new businesses. If Sunflower Technology Ventures receives that designation, it will become eligible for $20 million in federal funds.

Sunflower will make substantially larger investments in companies than the Ad Astra funds have made. According to the incorporation document, Sunflower will focus its investments on companies ready to start production, or on follow-up investments in more mature companies. The President of KTEC will manage Sunflower himself, with the help of a co-manager hired through a national search. By federal law, if Sunflower is granted a small business investment company designation, the President must resign from KTEC to run Sunflower.



Over the years, KTEC has created or funded a "network" of entities or affiliates to help it accomplish certain economic development objectives. The major affiliates are described on the facing page:

Centers of Excellence. KTEC helps fund the five Centers of Excellence the Legislature established at State universities between 1988 and 1990. They are as follows:

Advanced Manufacturing Institute	Kansas State University
Higuchi Biosciences Center	University of Kansas
Center of Excellence in Computer-Aided Systems Engineering	University of Kansas
National Institute for Aviation Research	Wichita State University
Center for Design, Development, and Production	Pittsburg State University

Primary clients and purpose: The centers primarily serve as research organizations to develop and transfer technology to industry, and to market university-developed technology. They also serve new or existing businesses that need help researching or developing their ideas or products into something that's marketable. They can provide technical services that are available only at a university-based research center.

Services provided: The centers provide basic and applied research, training, seminars, and technical consulting. For example, a company might come to a Center with an idea for a computer software program, and the Center's employees would help develop that software using advanced development techniques. Or, a company may come to a Center to help it develop a prototype of a product using highly advanced technical equipment.

Mid-America Manufacturing Technology Center (MAMTC). In fiscal year 1992, KTEC established MAMTC as a wholly owned non-profit subsidiary. MAMTC operates under a cooperative agreement between the National Institute of Standards and Technology (U.S. Department of Commerce) and KTEC. The agreement includes federal funding of about $13 million over the six-year period beginning in fiscal year 1991, and requires an annual State match of $1 million. MAMTC is based in Overland Park, but has five regional offices in Kansas, which generally are co-located with the centers of excellence. MAMTC also serves companies in Missouri, Colorado, and Wyoming. In all, 53 similar centers exist across the country.

Primary clients and purpose: MAMTC primarily helps small manufacturers modernize their operations.

Services provided: It provides technical training, engineering expertise, demonstration of equipment, and consulting services. For example, a company may come to MAMTC to get help modernizing its assembly line, and MAMTC field engineers will help identify how best to redesign that process.

Innovation and commercialization corporations. KTEC has set up three such corporations:

Kansas Innovation Corporation	Lawrence
Wichita Technology Corporation	Wichita
Mid-America Commercialization Corporation	Manhattan

These corporations were set up to help entrepreneurs market their technology-based ideas and products. According to KTEC officials, it originally was thought that the centers of excellence would be able to commercialize many of these ideas and products. However, because the centers' emphasis was on basic and applied research, they didn't have the skills or expertise needed to successfully commercialize new technologies. These non-profit corporations are private/public partnerships between KTEC, the universities, and the local private sector. Each corporation also has one or more affiliate organizations to provide assistance in other parts of the State. Each also is associated with a for-profit "holding company" that may provide the initial capital ("pre-seed" money) to get a company started. The presidents of the commercialization corporations, who aren't State employees, serve as the presidents of their associated holding companies. KTEC plans to fund the commercialization corporations for 10 years, at which time they are expected to become self supporting through the fees or other payments the corporations' clients pay.

Primary clients and purpose: The commercialization corporations primarily serve new technology-based companies in their very early stages of development; they take an active role in getting these companies started.

Services provided: These include writing business plans, conducting market research, doing engineering problem-solving, and locating sources of financing. For example, if someone invents a new type of electric motor, a commercialization corporation could help him or her obtain a patent, determine the potential market for the motor, write a business plan, locate investors, and start a company to manufacture and sell the motor. The corporation also could help negotiate the sale or license of the motor to an existing manufacturer.

Technology companies that enter formal technical assistance projects with these various entities pay for the services they receive with a fee based on a percentage of product sales, a cash fee, or stock in the fledgling company.

KTEC's Mission Is To Create and Expand Kansas Enterprises Through Innovation

KTEC is a quasi-public corporation established by the Kansas Legislature in 1987 to foster the creation, growth, and expansion of Kansas enterprises through technological innovation.

According to the President of KTEC, the agency also has the goal of providing a return on the State's investment in such technology. To help it achieve its mission, KTEC has been structured much like a private company. For example, KTEC has the authority to sue and be sued; borrow money; make contracts; acquire, own, hold and dispose of real or personal property; enter into agreements with public agencies and with entities involved in applied research and technology; invest funds; trade, buy or sell qualified securities; own and take license in patents and copyrights; negotiate royalty payments, and generally exercise any powers necessary to fulfill the mission of KTEC.

To accomplish its mission, the State has consolidated all science and technology programs within the KTEC network, which includes government, universities and private industry. According to the President of KTEC, such partnerships are key to achieving the agencies' success.

Also, much like a private company, KTEC is governed by a 20-member board of directors, made up of both public and private members as follows.

- The Governor or the Secretary of Commerce and Housing
- The Secretary of the Board of Agriculture
- Four legislators
- Four private-sector directors appointed by the legislature representing the following Kansas industries: oil and gas, aviation, telecommunications, computer software, information services and research services.
- Ten directors appointed by the governor, including six from the private sector, representing small Kansas enterprises in the following industries: oil and gas, aviation, telecommunications, computer software, information services and research services. One director must have experience in high-risk venture investments and one must have commercial banking experience. Four of the ten directors appointed by the governor are engineers or scientists with extensive experience in managing basic or applied scientific and technological research at Kansas educational institutions.

The Department of Commerce and Housing Attempts to Create New Jobs and Expand the Kansas Economy By Helping Existing Businesses and Trying to Attract New Businesses to the State

The Department comprises six divisions: Administration, Business Development, Community Development, Housing, Trade Development, and Travel and Tourism. During fiscal year 1996, it employed 138 full-time-equivalent staff, and had a budget of about $73 million.

About $16 million of the Department's funding came from the Economic Development Initiatives Fund, and $1.7 million from the State General Fund. The remainder came from federal funds for the Community Development Block Grant Program.

The Department provides most of its direct assistance to businesses through its Business Development and Community Development Divisions. The Business Development Division provides technical and financial assistance to existing businesses, conducts marketing activities to attract new businesses, and provides grants to businesses for employee training. The Community Development Division provides professional advice, grants, and loans to cities and counties for capital improvements and local economic development.

Kansas Inc. Was Created by the 1986 Legislature To Oversee, Evaluate, and Plan Economic Development Activities in Kansas

It's governed by a 15-member board of directors. Members of the board include the Governor, four legislators, a member of the State Board of Regents, the Secretary of Commerce and Housing, a labor representative, and seven members from key industrial sectors.

Kansas Inc.'s budget for fiscal year 1996 was about $450,000. Its funding sources were the Economic Development Initiatives Fund, the State General Fund, and private sources—which by law must make up at least one-third of the agency's budget. The agency employs five full-time equivalent staff. Its primary activities include the following:

- formulating and studying economic development policy
- conducting strategic planning
- evaluating the State's tax, regulatory, and expenditure policies
- coordinating economic development activities by public-and private-sector organizations in Kansas

Kansas Inc. doesn't provide any funding—such as loans, grants, or the like—to outside entities, nor does it offer technical assistance to businesses.

How Is the Compensation of Executive-Level Staff in Kansas' Economic Development Agencies Set, And How Do Their Responsibilities and Compensation Compare With Their Counterparts in Other States?

Compensation for these officials is set by the Governor, the boards they report to, or the deans of the academic departments they work for. The heads of the various agencies then set the compensation of their employees. For the most part, officials told us they determined appropriate salary levels by making comparisons with similar positions in other agencies, or—in the case of professors—with faculty at peer institutions. A few officials were eligible for bonuses based on their achievement of certain goals. In a few cases, economic development officials also served on the boards or in management positions for companies their agencies were providing assistance to, but they didn't receive additional compensation.

Based on the limited comparative information we were able to obtain, it appears the salaries of the heads of Kansas Inc. and the Department of Commerce and Housing are fairly comparable to the salaries of economic development officials with similar duties, qualifications, and responsibilities in other states. The President of KTEC's salary also was comparable to the salaries of similar officials in the other states we were able to get information from, and was in-line with salaries paid to non-profit or private entities performing similar jobs. These and related findings are discussed in the sections that follow.

Compensation for the Heads of Economic Development Agencies Is Set by Appointing Authorities, Often Based on Comparative Information

We contacted officials from the Department of Commerce and Housing, Kansas Inc., KTEC, the centers of excellence, and the Mid-America Manufacturing Technology Center to obtain information about salaries and other compensation of their executive staff, including how those salaries are set, what benefits employees receive, and how employees are evaluated. Based on the information they provided, it's apparent that compensation for the chief executives are determined in several ways.

- The salary for the Secretary of Commerce and Housing, who is a cabinet-level appointee, is set by the Governor.
- In some cases, boards of directors set executive salary levels. Kansas Inc., KTEC, the Mid-America Manufacturing Technology Center, and the commercialization corporations all have boards of directors who have the authority to establish the compensation of their agency heads. Agency officials told us their boards generally did salary surveys of similar private and non-profit agencies when establishing salary levels.
- For the centers of excellence, executive salaries are set by department deans. The directors of two centers—Advanced Manufacturing Institute, Center of Excellence in Computer-Aided Systems Engineering—have faculty appointments in specific departments at each of the universities. The deans of those departments approve their salaries. According to information provided by Center officials, these salaries are set through a comparison of peer institution

salaries, and consideration of the faculty member's teaching, research, and service activities. The director of Higuchi Biosciences Center has both a faculty appointment and an administrative appointment within the Center. His faculty salary is set by his dean and his administrative salary is set by the Vice Chancellor for Research and Public Services, based on a review of professional expertise and job responsibilities. The director sets the salary for the executive director, a member of the unclassified university staff who handles the day-to-day operations of the Center. That salary also is based on a review of professional expertise and job responsibilities. The salary of the director of the National Institute for Aviation Research is set by the Vice-President for Research, Governmental, and Industrial Programs, based on a review of salaries for similar positions. The salary of the executive director of the Center for Design, Development, and Production, who also serves as executive director of the Business and Technology Institute, is set by the Vice-President for Academic Affairs. These last two positions also are unclassified university staff.

Salaries for other high-level officials at the agencies usually were set by the agency head with the concurrence of the Governor, applicable board, or appropriate academic official.

The table on the following pages shows the fiscal year 1996 salaries for executive-level officials in each of these agencies. (It does not intend to show the sources of funding for these salaries.) The table also provides information about bonuses and performance evaluations.

Some of the major points of interest or comparisons we identified in the area of compensation, benefits, and evaluations are as follows:

- Four economic development agency executives make more than $100,000 per year. In addition, the three presidents of the commercialization corporations make $100,000 per year. These individuals aren't State employees, but the corporations are part of the KTEC network and are under contract with KTEC.

- One or more employees at KTEC, MAMTC, and the commercialization corporations were eligible to receive bonuses, but they seldom received the full amount allowed.

- Through his employment contract, the President of KTEC also can receive compensation from other sources. For instance, he can participate as a general partner in a venture capital company (such as Sunflower Technology Ventures), or work as a consultant elsewhere for up to one day a week. He told us when he agreed to be President he had other business obligations, and this provision allowed him to meet those other obligations. The President of KTEC told us he only worked eight days on other business during the past year.

- Most economic development agency executives received health insurance, leave, and retirement benefits similar to other State or Board of Regents' employees. However, some employees who work at the Center of Excellence in Computer-Aided Systems Engineering can accrue 176 hours of leave per year after one year of service. This policy is the same as the Board of Regents'

Fiscal Year 1996 Compensation and Evaluation Information

	Salary	Bonus: Amount Eligible	Bonus: Amount Received	Who Evaluates?	Examples of Evaluation Criteria	Frequency
Department of Commerce and Housing						
Secretary	$90,672	none allowed		Governor	No formal criteria	At the discretion of the Governor
Director, Business Development Division	60,708	none allowed		Secretary	Increase the number of jobs created and retained Number of new client companies Satisfaction of client companies	qtrly/annually
Director, Community Development Division	54,864	none allowed		Secretary	Develop a strategic planning process in each county Provide technical and financial assistance to community projects	qtrly/annually
Kansas, Inc.						
President	87,975	none allowed		Kansas Inc. Board of Directors	No formal criteria	annually
KTEC						
President	$126,000	$31,500 (up to 25% of salary)	$24,000	KTEC Board of Directors	Manage the budget process Increase return on investments Monitor outcomes of programs Obtain new venture capital and other sources of funding	annually
Vice-President-Operations	46,920	none allowed		KTEC President	Prepare annual budget Serve on Board of Directors of commercialization corporation Manage information technology, accounting, human resources, and graduate intern programs	annually
Vice-President-Applied Technology	55,308	none allowed		KTEC President	Manage the applied research matching fund and industrial agriculture programs Collect $150,000 in new royalties Commercialize 30 new projects	annually
Vice-President-Innovation Research	54,756	none allowed		KTEC President	Assist in commercializing 4 new products Manage the SBIR, SSBIR, and IDAP grant programs	annually

Vice-President-University/Federal Programs	56,316	none allowed		KTEC President	Provide oversight to centers of excellence, MAMTC, and the commercialization corporations Develop policies and procedures, establish performance measures, and monitor performance of these entities	annually
Mid-America Manufacturing Technology Center						
Chief Executive Officer	$124,000	$24,800	$22,076	MAMTC Board of Directors as part of annual contract renewal		
Vice-President-Marketing	57,000	11,400	8,994	CEO	All collect performance data on the number of companies contacted, initial site visits, informal engagements, technical assistance projects, amount of project revenues, and customer satisfaction	annually
Vice-President-Operations	76,992	15,384	3,105	CEO		annually
Regional Director-Great Bend	58,000	11,600	9,647	CEO		annually
Regional Director-Manhattan	83,964	none (a)		CEO		annually
Regional Director-Overland Park	67,650	13,530	11,361	CEO		annually
Regional Director-Pittsburg	68,009	13,602	12,610	CEO		annually
Regional Director-Wichita	84,400	none (a) (MAMTC bonuses are up to 20% of salary)		CEO		annually
<u>Centers of Excellence</u>						
Advanced Manufacturing Institute						
Director	$82,143(b)	none allowed		KSU Dean of Engineering	Performance on administrative duties and technology development.	annually
Center for Design, Development, and Production						
Director	$85,622	none allowed			no formal evaluation required until FY 1997	
Center of Excellence in Computer-Aided Systems Engineering						
Director	$80,653(b)	none allowed		Director, Engineering Management Program	Performance on research, teaching, and service duties.	annually

(a) These regional directors are tenured faculty members; as a result, they aren't eligible for bonuses.
(b) These are 9-month salaries.

(continued)

Fiscal Year 1996 Compensation and Evaluation Information

	Salary	Bonus: Amount Eligible	Bonus: Amount Received	Who Evaluates?	Evaluation Criteria	Frequency
Higuchi Biosciences Center						
Director	$117,122	none allowed		Vice Chancellor for Research, Graduate Studies and Public Service	Formulate budget targets Change administrative structure to meet the goals of the Center Monitor conflicts of interest	five-year cycle
Executive Director	93,907	none allowed		Director	Manage day-to-day operations of the Center	annually
National Institute of Aviation Research						
Executive Director	$101,500	none allowed		Vice President for Research and Governmental and Industrial Programs	Assist faculty with development and research Organize labs to benefit faculty and business clients Identify possible colaborative projects	annually
Innovation and Commercialization Corporations						
Kansas Innovation Corporation						
President	$100,000	$25,000 (up to 25% of salary)	$0	Corporation Board of Directors	Performance of the corporation The employee's contribution to the growth and profitability of the corporation	annually
Mid-America Innovation Commercialization Corporation						
President	$100,000	$25,000 (up to 25% of salary)	$0	Corporation Board of Directors	Performance of the corporation The employee's contribution to the growth and profitability of the corporation	annually
Wichita Technology Corporation						
President	$100,000	$25,000 (up to 25% of salary)	$0	Corporation Board of Directors	Performance of the corporation The employee's contribution to the growth and profitability of the corporation	annually

leave policy for unclassified staff, but it's more than the 168 hours of leave other State employees can accrue per year after 20 years of service. The Presidents of Kansas Inc. and KTEC receive fully paid family health insurance plans. The President of KTEC also has a $270 a month car allowance, and a fully-paid $200,000 group life insurance policy.

- Annual evaluations were required for most economic development officials; our review for a sample of officials showed they received them. In general, their evaluations included a review of how well they met pre-established goals and objectives.

In a few cases, economic development officials served on boards or in some other management capacity for companies they were providing assistance to, but didn't receive additional compensation from those companies. One of the concerns raised when this audit was requested was that economic development officials were receiving outside compensation from some companies their agencies were providing financial or technical assistance to.

We found that some officials who work for economic development agencies do serve as members of the boards of directors—or in some other management capacity—for companies that received assistance from their agencies. These situations are as follows:

- the presidents of the commercialization corporations frequently serve on the boards of the companies they assist. They may even serve as presidents of those companies while the companies are getting started.
- employees of KTEC serve on the boards of the commercialization corporations.
- the President of KTEC serves on the boards of the pre-seed capital funds run in association with the commercialization funds.

In all these cases, these responsibilities are seen as part of the jobs of the economic development employees, and they don't receive additional compensation for this work. The primary reason for having them in these positions is to safeguard the State's investments.

We also identified instances where economic development agency employees served on the boards of some companies their agencies assisted—where this service <u>wasn't</u> part of their normal job responsibilities. These relationships will be discussed in question two.

Compared to Other States' Economic Development Agencies, Salaries for Agency Heads in Kansas Were Near the Middle of the Range

One of the audit concerns was how economic development executives' salaries and responsibilities in Kansas compared with executives' salaries in similar agencies in other states. Comparisons are somewhat limited by the fact that economic development agencies in other states are so varied. By talking with State economic development officials and reviewing the literature, we identified eight states that had

State	Agency	Budget	Employees	Directors Qualifications	Agency Responsibilities	Salary	Bonus	Benefits: Health Ins.	Benefits: Life Ins.	Benefits: Retirement	Benefits: Other
Kansas	Kansas Inc.	$451,501	5	PhD in Public Policy	•Analyze and coordinate KS economic development activities •Strategically plan to identify economic opportunities, set objectives for State economic development programs, and improve tax and regulatory policy •Evaluate Kansas economic development programs in other agencies, including establishing benchmarks and performance objectives	$87,975	n/a	fully paid health for employee and dependents	state benefits	state retirement	n/a
Rhode Island	Economic Development Council	$425,000-$450,000	3	PhD in economic development planning, 10 to 12 years of government and consulting experience	•Analyze the economy of Rhode Island •Make policy recommendations to improve Rhode Island's economy to the Legislature and Executive Agencies •Administer the selection process and provide oversight for University Centers of Excellence	$95,000	up to 20 % of salary	private plan (about $100 month paid by employer)	n/a	Council matches 50% of contributions, up to 6% of salary	n/a
Indiana	Economic Development Council	$455,000	7	PhD, 20 years experience in economic development. Some consulting, but also worked in government.	•Strategically plan and conduct research for state economic policy •Evaluate economic development tools and incentives	$88,200	possible, but never awarded. Amount at the discretion of the Board	private plan b/w $100-$400 a month	employer paid for; twice of annual salary	Private plan, employer contributes 10% of gross salary	n/a
Kansas	Department of Commerce and Housing	$73,757,449	138	Bank Vice-President and community development experience	•Facilitate growth, diversification, and expansion of existing enterprises and basic industries, and the creation of new enterprises by Kansans •Provide loan guarantees and other assistance to encourage the export of value-added goods and services nationally and internationally •Provide grants to companies to increase employee training opportunities •Provide assistance to local governments about strategic planning and local economic development programs •Provide financial and technical assistance to increase the availability of affordable housing •Provide information about resources and economic opportunities, existing industry and business, and technological innovations in Kansans •Promote and provide grants to encourage travel and tourism in Kansas	$90,672	n/a	state benefits	state benefits	Can have deferred compensation plan instead of state benefits	n/a
Arkansas	Industrial Development Commission	$52,978,401 (FY 96-97)	107	Worked in Commission's community development and industrial recruitment offices. Became director of Industrial recruitment. Worked for Little Rock Chamber of Commerce	•Work with existing industry expand current operations and recruit new capital investment •Provide technical services to communities and counties for strategic planning •Promote the sale of AR agricultural and manufactured products and encourage foreign investment •Design and implement programs that help AR industries identify ways to increase efficiency	$84,149	n/a	state benefits	state benefits	state benefits	n/a

					and productivity •Provide financial, technical, and training assistance to AR cities and counties •Provide intensive pre-employment training and retraining for manufacturing workers •Promote the state and its industries through advertising, publications, and special events						
Iowa	Department of Economic Development	$21,862,578 (FY 97)	123	didn't provide information	•Develop a 20-year and 5-year strategic plan for Iowa's economic development programs •Coordinate job training and employment programs •Foster technology transfer from universities to the marketplace •Provide financial assistance for economic and community development projects •Provide technical assistance to communities and regional economic development organizations •Promote and market Iowa and Iowa products	$76,700-$108,700	n/a		didn't provide information		
Minnesota	Department of Trade and Economic Development	$36,579,000	234	didn't provide information	•Provide assistance to communities through grants and loans for housing rehabilitation, public facility improvements, and economic development projects •Assist small- and medium-sized businesses export products internationally •Provide grants to organizations and communities to promote tourism in MN	$67,000	n/a	state benefits	state benefits	state benefits	n/a
Virginia	Economic Development Partnership	$32,969,000 (FY 97)	145	20-25 years of marketing and economic development experience in another state. MS in Econ, JD	•Improve the livelihood of Virginians and increase the tax base in VA •Increase domestic and international industrial development, capital development, and tourism in VA	$117,000	up to 25% of salary	state benefits	state benefits	state benefits	n/a
Kansas	KTEC	$20,312,997	15	Ran a private venture capital firm for more than 5 years; has more than 10 years experience running companies or major divisions of companies, including president and chairman of a hospital turnkey computer systems company	•Provide matching grants to encourage development of innovative technologies •Make quality seed capital investments in start-up companies through the Ad Astra investment pool •Fund 3 commercialization corporations to provide business assistance and seed capital to start-up businesses •Increase the award of federal research and development grants to Kansas universities •Assist companies in obtaining federal funds •Finance basic research, applied research, and technology transfer at KS universities •Finance MAMTC to provide manufacturers with technical and engineering problem solving.	$126,000	$24,000 (up to 25% of salary)	fully paid for employee and dependents	state benefits and fully paid $200,000 group policy	state benefits	vehicle lease allowance
Connecticut	Connecticut Innovations, Inc.	$12,000,000	25	J.D. and M.S. in managment. 10 years experience running venture capital firms	•Provide grants for cooperative research between universities and industry •Fund 2 Advanced Technology Centers at universities •Provide matching funds for federal grants to	$93,476-$120,074	flat amount determined by Board of Dir.	state benefits	state benefits	state benefits	n/a

(continued)

					businesses •Provide loans, investments, and grants for product development and marketing in high technology businesses						
Florida	Enterprise Florida Innovation Partnership, Inc.	$4,806,724	10	Former president of KTEC	•Provide manufacturing, engineering, technical, and business services to small manufacturers •Support 4 commercialization corporations to provide entrepenurial assistance and technology transfer from universities •Fund applied research and product development in companies •Allocate federal and state funds to defense-related industries •Assist companies in obtaining federal funds	$150,000	$30,000 (amount determined by Board of Dir.)	private plan	part of retirement benefits	split dollar retirement plan	n/a
Indiana	Business Modernization and Technology Corporation	$10,000,000	54	Appointed by governor. Came from manufacturing business with experience in the Corporate investment division of BMT	•Manage a product development loan fund to help conduct research and develop prototype products •Manage a loan fund to support commercialization of a product •Finance manufacturing and business support services through 14 regional Manufacturing Extension Centers •Fund 8 Centers of Technology Development and Service to assist in technology transfer and offer technical assistance to industries	didn't provide information	n/a	state benefits	state benefits	private annuity Corporation contributes 15% of salary up to $40,000, 19.4% over $40,000	n/a
Minnesota	Minnesota Technology, Inc.	$10,000,000	80	M.S. in Economics, Director of Pennsylvania Office of Technology Development, Executive Director, Ben Franklin Research Partnership, Int'l Trade and Investment company.	•Provide assistance with modernization, job training, and technological assistance through a division of MN Inc., the Upper Midwest Manufacturing Technology Center •Work with industries in defense conversion •Provide start-up capital financing to small, technology-related manufacturers through an equity fund •Help companies apply for federal dollars through MN Project Innovations	$93,600	n/a	state benefits	state benefits	state benefits	n/a
Virginia	Center for Innovative Technology	$8,200,000	27	Community college president	•Co-fund grants for research and innovative technology projects business at public universities •Establish and fund 13 technology development centers at research universities in fiber optics, composite materials, advanced computer technology, biotechnology, and wireless communications •Provide engineering and problem solving through the Manufacturing Action Program to small manufacturers •Contract with 11 individuals at community colleges to perform technology transfer assistance projects, including linking entrepreneurs with other CIT programs	$110,000-$189,000	up to 25% of salary	fully paid	fully paid	defined contribution TIAA/CREF	vehicle provided; housing allowance

economic development agencies similar to those in Kansas. In all, 11 agencies in those states could be used for comparisons.

For each comparison agency, we contacted officials to identify the responsibilities of these executives and their compensation (including salaries and fringe benefits). We also tried to get information on how the compensation was set, and how the evaluation process worked in other agencies, but found that most states didn't have formal criteria or were unwilling to provide it. The information we obtained is summarized in the table on the following pages.

We focused on agency heads because analyzing the duties of all upper-level economic development staff in Kansas and other states would have taken more time than was available for this audit. In looking at these agency heads, we focused primarily on their background qualifications, the size of the agencies they were responsible for—both in terms of budget and number of employees—and the general types of activities they were responsible for.

Salaries and benefits for the President of Kansas Inc. and the Secretary of Commerce and Housing fell within the middle-to-low end of salaries in other states with comparable agencies. As the table shows, the President of Kansas Inc. is paid about the same as the head of the Indiana Economic Development Council, and somewhat less than the head of the Rhode Island agency. However, he isn't eligible for a bonus, as are officials of both other states (although a bonus has never been awarded in Indiana).

The Secretary of Commerce and Housing is paid in the middle of the range of salaries of the other states used for comparison purposes. With the exception of Virginia, these state economic development officials weren't eligible for bonuses, and received their states' fringe benefit packages.

The salary and benefits package for the President of KTEC appears to be in the middle of the range of salaries of top officials in technology-based economic development agencies in other states. We contacted five other states with agencies similar to KTEC. All these agencies are quasi-public or private entities. According to the Executive Director of the State Science and Technology Institute, KTEC has one of the most comprehensive programs in the country. He told us the states set up most like Kansas are Virginia, Florida, and Connecticut. He said Indiana and Minnesota have less comprehensive programs than KTEC, although they do many of the same things KTEC does. The table shows that the President of KTEC's salary and benefits fall in the middle of the range of the salaries and benefits of the heads of similar agencies in the other states.

We also reviewed information from a salary survey prepared for KTEC, which reviewed the compensation levels of state science and technology program officials from other technology programs, non-profit organizations, and universities. The salaries for the president of such organizations ranged from $111,000 to 189,000, as of April 1995.

What Relationships Exist Between Economic Development Agencies And the Companies They Assist, and Are Adequate Laws and Procedures in Place to Deal With Conflicts of Interest That May Result From Those Relationships?

Overall, relationships we identified between economic development employees and the companies they assist were relatively uncommon. However, of 61 start-up companies we reviewed incorporation records for, we identified employee relationships in 13 of them, or 21%. Most of those relationships occurred between employees of the centers of excellence and the companies they assisted. In most cases, these companies received technical assistance, rather than financial. The relationships we found generally involved employees who either owned stock in start-up companies, served in a management capacity in those companies, or both, or employees or their spouses who owned or worked for companies that sought assistance from the employee's agency.

Not all relationships we found represented conflict-of-interest situations. When conflicts existed, it was because the employees generally were in positions to decide which companies would receive State funds or other resources from their agencies. Employees didn't disclose their relationships about half the time; in these cases, the employees worked at the centers of excellence.

We found that State efforts to manage conflicts of interest aren't adequate in a number of areas. State law is unclear about whether some employees are subject to the State's ethics laws, while other employees clearly aren't covered. Except for the centers of excellence, most economic development agencies didn't have written policies and procedures on conflict-of-interest situations and how they should be "managed" to avoid actual conflicts. Although the State requires many employees to file disclosure forms (statements of substantial interest), the process hasn't been set up to ensure that agencies review those forms to see if potential conflicts exist. Also, university conflict-of-interest disclosure policies require employees to list their substantial interests only if the employees think a conflict exists, and don't require university employees to report financial interests at the same level as other State employees who are required to report such interests. We also found that, unlike some other states, Kansas' economic development employees aren't prohibited from having an interest in companies that receive assistance from the economic development agencies they work for. These and other findings are described in more detail in the sections that follow.

We Identified a Number of Relationships Between Economic Development Agency Staff And the Companies They Assisted

One of the concerns behind this audit was whether relationships existed among economic development agency staff and the companies that received assistance from the agencies they worked for. In such relationships, conflicts of interest can occur when agency employees are in a position to give State funds or other resources to entities in which they or their families have a personal stake.

Obviously, if the people who are making such decisions own a stake in—or receive any compensation from—the companies involved, it's more difficult for them to be objective and to separate their personal interests from the best interests of the State. Conflicts of interest also can occur if State employees use information they obtain in the course of their work to further their personal financial interests.

The appearance of a conflict of interest can be as detrimental to the public trust as an actual conflict. At a minimum, employees should disclose any relationships they have so potential conflict-of-interest situations can be avoided or appropriately managed.

To determine the types of relationships that exist between economic development agency officials and the companies they assist, we developed a database of companies that received economic development assistance in fiscal years 1995 or 1996 from KTEC, the Department of Commerce and Housing, the centers of excellence (including any companies that got MAMTC services through a center), and the commercialization corporations. In addition, we were able to include some companies that received assistance from the industrial liaison offices.

We reviewed statements of substantial interest for all economic development agency employees and board members, and reviewed income tax records for a subsample of these individuals to see whether they had any financial interests in any of the companies that received economic development assistance. Because of time constraints, we didn't review incorporation records for all 680 companies in our database. Such a review could disclose relationships that exist (such as an employee owning stock in a company or serving on its board of directors) that wouldn't show up otherwise if the employee didn't disclose them or receive any financial earnings or compensation from them. Because of the focus on start-up companies, we reviewed incorporation records from a sample of 61 new technology-based companies that received assistance from the State in fiscal years 1995 or 1996. Finally, for the companies where we identified relationships, we examined company files at the economic development agencies in more detail.

Overall, relationships we identified between employees and the companies they assist were relatively uncommon. Of the 680 companies in our database, we identified relationships in only about 2% of them. However, of the 61 new technology-based companies we reviewed incorporation records for, we identified relationships in 13 of them, or 21%. Not all these relationships represented conflict-of-interest situations. Most of them existed between employees of the centers of excellence and the companies they assisted. And in most cases, the types of assistance these companies received from the agency where the relationship existed was technical, rather than financial. Where relationships existed, they tended to group into the following four areas:

- employees in economic development agencies who <u>own stock</u> in start-up companies that have received or are receiving assistance from the agencies these employees work for

- employees in economic development agencies who <u>serve in a management capacity</u> for these companies, either on the board of directors or in an operating position

- employees in economic development agencies who <u>both own stock and serve in a management capacity</u> in start-up companies that have received or are receiving assistance from the agencies these employees work for

- employees of economic development agencies or their spouses who either own companies or work for companies that seek assistance from the agencies these employees work for (in many cases, the employee has developed a marketable technology or idea, and is starting a new company to try to produce or market it)

The following sections describe the relationships we identified in some detail, together with our assessment of whether the relationship appears to be a conflict of interest. When a conflict-of-interest situation existed, it generally was because the employees were in positions to decide which companies would receive State funds or other resources from their agencies. Employees didn't disclose their relationships to their employers in about half the cases. All these instances involved centers of excellence employees.

It's important to remember that this isn't an exhaustive list of all the relationships that might exist. Because of the number of companies that have received economic development assistance from the State over the years, we were able to look at only a sample of companies involved.

In 3 of the 13 start-up companies where we found relationships, economic development employees owned stock in those companies at the time they were receiving assistance from the State. One of these relationships involved the President of KTEC and a company called Janus Biomedical.

- **Before he took his current position, the President of KTEC and his wife** had invested in Janus Biomedical as part of the venture capital firm he managed. After he came to KTEC, one of KTEC's venture capital funds (Ad Astra II) invested about $152,000 in Janus Biomedical. Besides owning stock in Janus Biomedical, the President also was on the company's board of directors, and was receiving consulting fees from the company. Conflict-of-interest concerns were raised at the time this investment was made.

  Steps taken to manage the potential conflict of interest: In an attempt to avoid a conflict of interest, the President of KTEC quit receiving consulting fees from Janus Biomedical. He also disclosed his interest in the company on the State's financial disclosure form.

The other relationships we identified in this area involved employees of the State's centers of excellence. Those two situations are described in the paragraphs that follow:

- **The Director of the Center of Excellence for Computer-Aided Systems Engineering (CECASE)** owns stock in Data Discovery, Inc., a company that received technical assistance from the Center. At one point, the Director also was on the company's board of directors. These relationships represent potential conflicts of interest. (The Director returned to full-time faculty duties September 1, 1996, and no longer has any administrative duties at the Center.)

  Steps taken to manage the potential conflict of interest: University of Kansas officials indicated they were aware of these relationships, and required the Director to relinquish his role as a board member of the company because it conflicted with his duties as a faculty member. The University allowed him to retain his stock. However, the Director didn't disclose his ownership interests with this company, as required by University policy. The Associate Director (who didn't own any stock in the company) was appointed to fill the vacant board position.

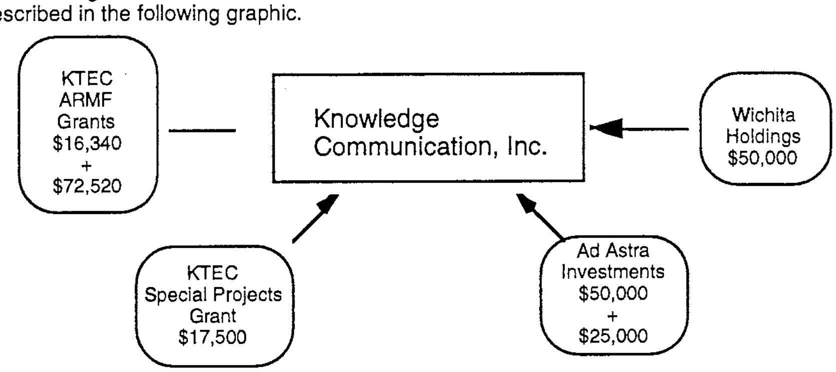
- As part of his research activities at Higuchi Biosciences Center, **a lab director at the Center** invented a molecule that would allow otherwise insoluble products to be dissolved in water, with potential applications in the cosmetics and pharmaceutical industries. Because it was his invention, University policy allowed him to share in any proceeds the University received from it. In 1992 and early 1993, the Executive Director and the lab director, along with other members of the University's staff, attended meetings with a consultant who recommended that a private company—Cydex—be formed to market this new technology. During January 1993 through May 1993, the Executive Director corresponded with KTEC asking permission to use part of the Center's core research and commercialization funding to pay for legal and consulting expenses relating to commercializing the molecule. In July 1993, the company was formed. Both the Center's **Executive Director and lab director** purchased stock in the new company through a private offering. Although the University's general counsel said the Executive Director had never been involved in the decision-making process for any of the funds controlled by the research centers within Higuchi Biosciences Center, the equity ownership still appears to us to represent a potential conflict-of-interest situation.

Steps taken to manage the potential conflict of interest: Both employees disclosed their stock interests in Cydex. The lab director took additional steps to ensure that an oversight advisory committee would be responsible for making decisions at the Center involving the company. In addition, according to University policy, the

Start-Up Companies Often Receive Financial Assistance from Several Economic Development Programs

Companies can receive assistance through several of the programs offered by KTEC, its network of economic development entities, and the Department of Commerce and Housing. In all, 121 of the 680 companies we identified as receiving assistance in fiscal years 1995 or 1996 received money or technical assistance from two or more economic development programs during those years.

For instance, Knowledge Communication, Inc., a Wichita-based company that designs CD-ROM software for corporate training, has benefitted from several KTEC programs. Through December 1995, Knowledge Communication received $231,360 from various programs funded by KTEC. These are described in the following graphic.



To-date, the State hasn't realized any returns on its investment in Knowledge Communication. However, if the company is successful, the State could earn some returns. For example, to repay these grants plus 10% interest, the company will pay the State a royalty of 2.5% of gross sales. Once the grant is paid off, the company will continue to pay the State royalties. For one product, it will pay 1% of gross sales up to $32,680. For a second, it will pay 1% of gross sales for the life of the product. In addition, the Ad Astra investments represent an ownership of 11.3% of the company.

University prohibited the employees from simultaneously having a management role at both the University and the company.

Employees from three different economic development agencies served in management capacities for one company we reviewed. That company was Biosciences Innovations, and the relationships are described below:

- **The president of the Kansas Innovation Corporation** (a commercialization corporation) is also president of Bioscience Innovations, Inc. and serves on its board of directors. Biosciences is a client of the corporation. In addition, **a vice-president of KTEC** serves on the company's board of directors, as does the **Executive Director of Higuchi Biosciences Center.** These relationships would be conflicts of interest if these individuals were paid by the company for their services.

  Steps taken to manage the potential conflict of interest: None of these individuals receive any compensation from the company; therefore, no conflict of interest existed. In addition, the KTEC employee disclosed his interests in the company.

In 4 companies we reviewed, employees of economic development agencies both owned stock and held management positions in companies that got assistance from the agencies they worked for. All of these relationships involved employees of the centers of excellence:

- **The Director of Research and Development at the National Institute of Aviation Research (a center of excellence)** owns a small amount of stock (which he got at no cost) and serves on the board of directors of Impact Dynamics, Inc., which uses the Center's test facilities. This company was formed to commercialize a technology developed by a faculty member working in the Center. The faculty member has agreements with the company and with Wichita State University that allow him to share in any royalties that result from the technology. The faculty member also serves on the company's board of directors. These relationships represent potential conflicts of interest.

  Steps taken to manage the potential conflict of interest: The Director of Research and Development disclosed his interests in the company on the University's disclosure form, but the faculty member didn't. In addition, the Center has designated another employee to make decisions affecting the company's use of the Center's facilities. Another Center employee became president of this company and resigned from the University to avoid a conflict of interest.

- **The Associate Director of CECASE** owns stock in Hanuman II Corporation, a company that received technical assistance from the Center. **The Director** serves on the company's board of directors, and **another CECASE employee** owns stock in and serves on the company's board as well. Each of these relationships represents a potential conflict-of-interest situation.

  Steps taken to manage the potential conflict of interest: Even though the University was aware of these relationships, the employees in this case didn't disclose their interests in Hanuman II Corporation. They told us the company no longer exists. The company has forfeited its corporate status; however, it still existed at the time the employees filed conflict-of-interest forms with the University.

- **Two management-level employees of CECASE** own stock in and are directors of the Lawrence Applied Research Corporation. According to annual reports the Center filed with KTEC, this company received seminar services and consulting services from the Center. Both the Director and the Associate Director said they questioned whether the company really had received any services from CECASE. The Director said this company was included in the report based on instructions provided by KTEC. If services were provided, these relationships represent potential conflict-of-interest situations.

  Steps taken to manage the potential conflict of interest: We couldn't tell whether services had been provided. The employees didn't disclose their interests in Lawrence Applied Research Corporation. The Director received University approval to consult with the company, but the consulting form doesn't disclose his personal interests in the company.

- **While an Associate Director of the Advanced Manufacturing Institute (a center of excellence)**, an employee owned stock in and was Vice-President of the Electric Hybrid Vehicle Corporation (EHV), which received consulting and core research services from the Center. Although the Executive Director of the Institute said the Associate Director doesn't make decisions relating to providing core research support, this relationship still appears to us to represent a potential conflict-of-interest situation.

  Steps taken to manage the potential conflict of interest: This employee disclosed his interests in the company on the State's statement of substantial interest form.

In 5 of the companies we reviewed, employees of economic development agencies or their spouses either owned companies or worked for companies that got assistance from the agencies they worked for. Two of those cases involved an employee and board member of KTEC:

- **A Vice-President of KTEC** started a company called Free Spirit Enterprises with her husband. The Vice President, who also served on the board of the Mid-America Commercialization Corporation as a representative of KTEC in an unpaid capacity, went to that commercialization corporation for assistance. A conflict of interest would exist if the Corporation took that company on as a client. To date, that hasn't happened, so no conflict of interest exists.

  Steps taken to manage the potential conflict of interest: The employee disclosed her interest in the company on the State's financial disclosure form.

- **A board member of KTEC**, who also was a KU faculty member associated with a research center now housed within Higuchi Biosciences Center, founded a company called Cypress Systems. He was president of the company and owned stock in it. The company received assistance from KTEC through a loan and an investment from one of KTEC's venture capital funds, Ad Astra Fund I. Because board members can influence KTEC investment decisions, this situation represents a conflict of interest.

  Steps taken to manage the potential conflict of interest: The board member disclosed his interests in the company, and abstained from any votes relating to KTEC investments in his company.

Three other cases we identified in this area involved relationships between employees of the centers of excellence and the start-up companies they assisted.

- **The employee who coordinates technology transfer activities for CECASE** is married to a professor who developed a software product he wanted to bring to market through a company he founded, Ambler Software Engineering. That software company received technical assistance from the Center. Although this employee isn't in a decision-making role at the Center, this relationship poses at least the appearance of a conflict of interest.

  Steps taken to manage the potential conflict of interest: The employee disclosed her spouse's interest in the company to the University. To deal with the conflict, the University had a third party write the licensing contract. The University's general counsel told us the employee wasn't involved in the discussions or negotiations regarding the licensing agreement.

- **The wife of the Director of CECASE** is an employee of Cadence Design Systems. Cadence received core research and consulting services from the Center. This relationship represents a potential conflict-of-interest situation.

  Steps taken to manage potential conflicts of interest: None. The Director didn't disclose his wife's employment with Cadence, as required by University policy. He told us his wife wasn't in a management position with the company, and maintained that no conflict of interest existed.

- **Three employees of CECASE** formed a company, Fast Lane Communications, to provide Internet and World Wide Web homepage services. The employees are sole owners and operators of Fast Lane. Fast Lane has received some services from the Center and from KTEC's commercialization corporation in Lawrence, in exchange for internet access and maintaining the Innovation Corporation's web homepage. Although none of these employees were in a management position at CECASE, there is at least an appearance of a conflict of interest.

  Steps taken to manage potential conflicts of interest: These employees didn't disclose their involvement with this company, as required by University policy. In addition, even though the Center's annual report says this company received assistance from the Center, the Director told us the company received only informal advice, and that no documentation existed to show what services the company actually got.

The preceding information shows the types of relationships that exist among economic development agency employees and the companies their agencies assist. As we noted, sometimes these relationships represented a real or potential conflict of interest, or at least the appearance of a conflict. Appendix C lists these companies and the assistance they have received from economic development agencies. The rest of this question examines whether the State has adequate policies and procedures in place to guard against such situations.

State Efforts To Manage Conflicts of Interest Aren't Adequate in a Number of Respects

To determine whether the State and its economic development agencies have adequate policies and procedures to manage any conflicts of interest that may arise, we identified good practices that should be in place to reasonably reduce problems with conflicts of interest. We developed this list through a review of relevant literature and interviews with a business and tax law expert at Washburn University's Law School.

We also talked to officials in other states about their conflict-of-interest policies and procedures, reviewed State laws and agency policies and procedures, surveyed staff, and talked to agency officials to find out what policies and procedures currently are in place. We then compared those existing policies to our list of good practices.

Based on our reviews, we concluded an adequate system to deal with conflicts of interest in economic development agencies generally would include laws or formal written policies or procedures to do the following:

- prohibit employees from having a substantial financial interest in companies their agencies do business with, OR have an effective way of managing those conflicting situations (such as requiring employees to abstain from any decisions where they would have personal financial interests in the outcomes of those decisions)
- require employees to fully disclose potential conflict-of-interest situations
- ensure that someone at the economic development agencies reviews the financial disclosure information employees provide, so that agencies are aware of potential conflicts and can act accordingly
- ensure that employees are informed about what conflicts of interest are, and what's expected of them when such conflicts arise
- have the ability to independently investigate violations of policies and enforce penalties.

In general, we found that State law and some agency policies have a number of provisions to deal with conflicts of interest, as follows:

- K.S.A. 46-285 requires State agencies to designate certain employees who must file statements of substantial interest with the Commission on Governmental Standards and Conduct. For the most part, designated employees are in management-level positions, or positions that can influence policy decisions. On these statements, employees are required to list their financial interests in any business that amounts to $5,000 or 5% of the business, whichever is less.

- K.S.A. 46-241 prohibits employees from using confidential information gained during the course of their employment to further their own financial interests.

- K.S.A. 46-233 prohibits employees from making decisions to contract with companies they have financial interests in.

- K.S.A. 74-8101(e) requires KTEC board members to declare any potential conflicts of interest, and to abstain from voting on any matter in which they have potential conflicts of interest.

- House Bill 3068, passed during the 1996 legislative session, prohibits KTEC employees from receiving compensation for services they provide to companies that receive KTEC assistance.

- The Board of Regents requires all full-time unclassified faculty and staff to file a university conflict-of-interest disclosure form each year.

Although current laws are a good start, some are unclear or don't go far enough, in our opinion, to address the real or potential conflict-of-interest situations that we discussed in the previous sections. We also found that, at the time of our audit, many economic development agencies don't have formal written policies and procedures addressing conflicts of interest. Our findings in these areas are discussed in more detail in the sections that follow.

State law is unclear about whether some employees are subject to the State's ethics laws. In opinions issued by the Commission on Governmental Standards and Conduct in 1987 and 1993, the Commission ruled that employees and board members of Kansas Inc. and KTEC weren't State employees as defined in the ethics laws, and therefore weren't subject to the State's ethics laws.

Changes to State law in 1995 made employees of Kansas Inc. and KTEC members of the "unclassified" service under the Kansas Civil Service Act. Thus, it appears they now fit the definition of a "State employee," and would be subject to the State ethics laws. One thing that's still not clear, however: State law designates "State agencies" as the entities responsible for identifying who should file statements of substantial interest. Because neither Kansas Inc. nor KTEC are State agencies, it's uncertain whether they're required to designate employees to file disclosure forms. The Commission hasn't been asked to issue a new ruling on this subject; but during this audit Commission staff told us they thought employees of both entities <u>should</u> be covered.

KTEC officials told us they think they <u>are</u> subject to State ethics laws, and have designated certain officials to file statements of substantial interest with the Secretary of State. Kansas Inc. officials, on the other hand, said they weren't sure whether their employees and board members were subject to the State's ethics laws. Kansas Inc. hasn't designated any employees to file statements of substantial interest, and none have. Most of its board members have filed, either because their appointments were subject to confirmation, or because they held other positions that required them to do so.

The presidents of the commercialization corporations and the State's venture capital fund managers aren't subject to the State's ethics laws because these individuals aren't State employees. However, they are involved in making economic development decisions regarding their client companies, and conflict-of-interest situations could arise. To deal with these situations, KTEC could require, through its contracts with these entities, the types of limitations, disclosures, or prohibitions it thinks are necessary to ensure that potential conflict-of-interest situations are known and managed.

Excluding the centers of excellence, most economic development agencies don't have formal guidelines for handling conflict-of-interest situations. Because of concerns about the potential for conflicts of interest and the need for universities to meet federal grant application requirements, the Board of Regents established formal conflict-of-interest policies in 1995. The centers follow those written policies. The other agencies' situations are described below:

- KTEC, Kansas Inc., and MAMTC. These agencies don't have written policies or procedures for managing conflicts of interest and guiding employees' actions regarding such conflicts, although the President of KTEC indicated his agency is in the process of developing such policies. Without formal guidance, there's a greater risk that conflict-of-interest situations that occur won't be identified and managed appropriately.

- Department of Commerce and Housing. In August 1996, after our audit was started, the Department established a written conflict-of-interest policy prohibiting employees from receiving compensation from private companies for work that's part of their regular job duties (reiterating K.S.A. 46-235). This new policy also prohibits employees from recommending the purchase of goods, services, or property if they or a family member have a financial interest in the company that is selling goods to the State. In addition employees must notify their division director in writing if they are knowingly participating in any aspect of a review for granting funds to an entity in which they or a family member have a financial interest.

- Commercialization corporations. The presidents of the three commercialization corporations told us that, although they didn't have written policies in this area, it was "understood" that a corporation board member would abstain from voting on a matter in which he or she had a substantial interest. The presidents also said they would never have a financial interest in any company they do business with.

  In August 1996, the Mid-America Commercialization Corporation was planning to get formal board approval for a conflict-of-interest policy requiring management staff to avoid conflicts between personal and company interests. And, unless the board gives explicit written approval, management staff can't have personal investments in or consult for the corporation's client companies, or provide services to any businesses if those services would be in direct competition with any services provided by the corporation. In addition, the new policy includes an internal review process to manage conflicts.

Although the State requires many employees to file disclosure forms, the process hasn't been set up to ensure that agencies review those forms to see if real or potential conflicts of interest exist. Employees who were required to file statements of substantial interest with the Commission on Governmental Standards and Conduct did file them. However, that information generally is filed directly with the Commission and isn't reviewed by agency officials who would need to know about individual employees' substantial interests and potential conflicts.

After they're filed, one individual within the Commission reviews the nearly 6,000 statements of substantial interest received, primarily to ensure they were filed as required. In most cases, this employee wouldn't be in a position to know whether a State employee's financial interests represented a conflict of interest.

Just as in the absence of formal policies and procedures—in the absence of some agency-level review of employees' substantial financial interests, there's a greater risk that conflict-of-interest situations that occur won't be identified and managed appropriately.

The Board of Regents' policies don't require full disclosure of university employees' financial relationships. Board policies require faculty and full-time unclassified staff to file a disclosure form with the heads of their departments. (University employees also may have to file State statements of substantial interest if they are designated to do so by their employers.)

The Board's form is designed to identify substantial interests that employees or their families may have that constitute a conflict of interest. According to the Board's attorney, employees were to identify any real or apparent conflicts on the forms. The appropriate department heads then would review these forms to determine whether the employees had a real conflict of interest—or just the appearance of a conflict—and would take any actions needed to manage the conflict.

Our review showed that the language on the form allows the employee to decide whether a substantial interest is in conflict with his or her university activities. If an employee decides a substantial interest isn't a conflict, the employee doesn't have to report anything. As described earlier, we found several examples in companies we reviewed in which university employees owned stock in a company that got assis-

Controls Have Been Built Into the Agreement With the State's Venture Capital Fund Manager To Minimize Some Potential Conflict-of-Interest Situations

The managers of the State's venture capital funds (Ad Astra I and II) also manage two venture capital funds that were in existence before the State established its funds. Some of the investments made by the Ad Astra funds were in companies that the fund managers had invested in through their other venture capital funds. We were concerned that these "add-on" investments could pose conflict-of-interest situations, so we reviewed the fund agreements to identify what controls were in place to ensure problems didn't arise.

One area of particular concern related to how the fund managers were compensated. If they were paid on the basis of how much their portfolio companies were worth, the fund managers could have an incentive to shore up poorly performing companies by making add-on investments from the Ad Astra funds. In fact, the managers were paid a flat amount, with an additional percentage available based on the amount of money initially committed to the funds. This arrangement seemed to reduce the risk that they would throw good money after bad.

We also were concerned that the fund managers would be more likely to invest the Ad Astra funds in companies they already had invested in, rather than in new technology-based companies. Although this could certainly happen, the investment agreement establishes investment criteria for each Ad Astra investment. The Ad Astra advisory committee (which is made up of representatives of the limited partners and not the fund managers) is required to review all investments—including add-on investments made in companies the fund manager has invested in through other venture capital funds—to ensure they meet the Ad Astra investment criteria.

tance, or a family member worked for the company, or the employee was a director of the company, and this information wasn't disclosed on the form.

Under Board policies, university employees don't have to report financial interests at the same level as other State employees. The Board of Regents has defined the threshold for faculty and full-time unclassified staff to report substantial interests at $10,000, or 5% of an entity, whichever is less. That figure was based on federal requirements, which specify a $10,000 threshold before substantial interests need to be reported. The State's threshold for employees filing a statement of substantial interest is $5,000, or 5%.

We also found that individual university practices on reporting substantial interests varied. Kansas State University follows the Board's policy, while both the University of Kansas and Wichita State University used a $5,000 threshold. (This year, both schools have gone to the $10,000 threshold.) Pittsburg State University apparently hasn't required its employees to file these disclosure forms yet, although the Executive Director of the Center for Design, Development, and Production did file a State disclosure form. (We didn't look at whether employees at Emporia State or Fort Hays State were required to file financial disclosure forms because neither university had a center of excellence.)

Many economic development agency employees we surveyed didn't know what their agencies' policies were regarding potential conflicts of interest. We sent a survey to employees of all the economic development agencies—including the centers of excellence—to determine whether they were aware of their agencies' formal or informal policies to disclose financial interests and prohibit conflicts of interest, and whether they thought those policies were adequate. We received responses from 87 of the 351 people we sent surveys to (25%). (Appendix D contains the complete survey results.)

In all, nearly 30% of the employees who responded didn't know whether their agencies had any policies requiring disclosure of any financial interests employees had, and 38% didn't know whether their agencies prohibited employees from having financial interests in companies their agencies provided assistance to. These figures suggest not only that many employees don't know what agencies' policies are, but, more importantly, that they don't know what their own responsibilities might be for disclosing—or refraining from—relationships with certain companies or businesses.

Agencies in Some States Prohibit Employees From Holding Any Sort of Financial Interest In Companies They Do Business With

We contacted six other states about their conflict-of-interest statutes, and found that economic development agencies in several of them have stricter conflict-of-interest prohibitions than Kansas. The agencies described below have responsibilities similar to those of KTEC. Those prohibitions are as follows:

- Iowa's Wallace Technology Transfer Foundation prohibits its employees from having any interests in any company the Foundation does business with.

- The Center for Innovative Technology in Virginia prohibits its officers and employees from acquiring an interest in an entity that receives funding from the Center.

- Minnesota Technology Inc. doesn't have a blanket prohibition on such ownership, but if an employee owns 5% of a company, or has a management position in the company, the company can't receive assistance from the agency.

- The Arkansas Science and Technology Authority is prohibited by state law from investing in any company an employee owns or is a director of.

The Kansas Legislature acted in 1996 to tighten up some of the laws relating to economic development employees and their financial relationships. As noted earlier, House Bill 3068 prohibits KTEC employees from receiving any compensation from any client companies. However, it doesn't specifically prohibit stock ownership.

Conclusion

Clearly, the development of high-technology companies and capacity in Kansas is an area that poses a lot of opportunities, both for economic development in the State and for conflicts of interest between these companies and employees of the State's economic development agencies. As more and more new products and technologies are developed, and as long as the "pool" these companies can tap into for economic development assistance and venture capital funding remains relatively limited and intertwined, there are bound to be even more such opportunities.

To address potential conflict situations, economic development agencies in some other states have instituted total bans on employee investments in the companies they assist. Others have taken a less strict approach. In Kansas, the emphasis has been on requiring disclosure of such interests, and allowing the agencies and employees involved to decide how to best manage those potential conflicts. As this audit has shown, that approach has been only partially effective at ensuring that relationships are disclosed and properly managed.

Looking towards the future, the Legislature will need to determine whether any appearance of a conflict of interest should be eliminated, or whether that is an inevitable by-product of economic development that should be managed. Given the Legislature's increasing commitment to fund new start-up technologies, it will need to walk a fine line between ensuring that employees don't benefit as a result of their State jobs, and not stifling entrepreneurship and innovation. The Joint Committee on Economic Development would be the legislative committee most likely to be involved in making the initial decisions for legislative consideration.

Whatever decision is reached, the Legislature should, at a minimum, strengthen State laws to make sure they cover employees of all State economic development agencies. In addition, agencies will need to develop formal guidelines or clarify existing policies—taking into account any changes the Legislature requires in this area—and should ensure their employees know what is expected of them so they can make the right decisions in this important area.

Recommendations

1. To ensure that all appropriate economic development officials are subject to the State's ethics laws, we recommend that the Commission on Governmental Standards and Conduct should review recent changes in State law to determine if it needs to revise its opinions on whether employees and board members of Kansas Technology Enterprise Corporation and Kansas Inc. are subject to the State's ethics laws. The results of its review—including any revised opinions it issues—should be reported to the Joint Committee on Economic Development and the Legislative Post Audit Committee. If the Commission concludes these employees aren't subject to the State's ethics laws, the Joint Committee on Economic Development should consider introducing legislation to specifically make them subject to those laws, and should make any changes needed to ensure that these agencies are required to designate employees to file statements of substantial interest.

2. To help ensure that potential conflict-of-interest situations are identified and managed appropriately, we recommend the following:

   a. KTEC, Kansas Inc., the Department of Commerce and Housing, and MAMTC should develop written policies and procedures regarding conflicts of interest. These entities, as well as the centers of excellence, should make their employees aware of the requirements that affect them. As part of these policies, agencies should, as applicable, consider having a written statement included as part of the documentation for each investment or technical assistance arrangement that indicates a review was made for conflicts of interest, and the results of that review.

   b. The State's economic development agencies should develop some method for reviewing their employees' substantial interests. One way would be to review employees' statements of substantial interest before they are filed with the Commission on Governmental Standards and Conduct, and to maintain a list or database showing those interests to help agencies manage conflicts as they arise. Other methods may be more efficient or effective, depending on the agencies' situations. For example, if employees are required to disclose potential conflicts of interest as part of each investment or technical assistance project (as noted in 2a. above), agency officials could review that information on a case-by-case basis, without having to keep track of their employees' substantial interests over time.

c. Through its contracts with the commercialization corporations and the venture capital fund manager, KTEC should require the types of limitations, disclosures, or prohibitions it thinks are necessary to ensure that potential conflict-of-interest situations are known and managed.

d. The Board of Regents should work with the universities to reword the financial disclosure form used by center of excellence employees, so that the expected information regarding those employees' substantial interests is provided. Employees should not be allowed to decide whether they think a substantial financial relationship represents a conflict of interest; that decision should be left to the employer.

e. Employees of the Center of Design, Development, and Production at Pittsburg State University should file the annual financial disclosure form, as required by Board of Regents' policy.

For all these recommendations, the agencies involved should report to the Joint Committee on Economic Development and the Legislative Post Audit Committee by the start of the 1997 legislative session regarding the actions they have taken or plan to take.

3. To ensure that its financial disclosure policy is consistent with the State's definition of substantial interests, the Board of Regents should reduce the threshold for requiring reporting of substantial interests to $5,000, or 5%. It should work with the Regents' universities to ensure this policy has been implemented at each school. Alternatively, the Board could require that all Regents' institutions designate individuals involved in economic development activities as needing to submit the State's disclosure form to the Commission on Governmental Standards and Conduct.

4. To ensure that the State has adequate laws and procedures in place to deal with conflicts of interest, the Joint Committee on Economic Development should review the kinds of relationships we identified in this audit. If it thinks a potential conflict of interest—or even the appearance of a conflict—is damaging to the public trust, it should consider whether further restrictions could be placed on economic development employees without hindering the agencies' ability to accomplish what they were set up to do. Among the options available for the Legislature's consideration are the following:

a. If the Legislature wants to eliminate any conflicts of interest entirely, the Joint Committee could consider introducing legislation prohibiting economic development employees from having any interest or any role—whether compensated or not—in any companies their agencies do business with. If this option is considered, the Committee should examine the pros and cons of prohibiting employees from serving on boards of directors, at no pay, when they are doing so to protect the State's interests.

b. If the Legislature wants to ensure that potential conflicts of interest are managed, but it is concerned about making restrictions so stringent that they might stifle the development of new technology-based companies, the Joint Committee could consider introducing legislation allowing employees to have interests in the companies their agencies assist, but requiring them to disclose those relationships and abstain from making any decisions relating to those companies.

c. If the Legislature wants to ensure that potential conflicts of interest are managed, but it wants to leave those decisions entirely up to the agencies involved, it need not act in this area. As long as the State's economic development agencies develop and follow appropriate policies and procedures in this area, as recommended in this report, those conflicts may still occur, but agencies will be aware of them and can manage them accordingly.

APPENDIX A

Companies Receiving Investments From Venture and Seed Capital Funds

Two venture capital funds and three seed capital funds operate within the KTEC network of programs and commercialization corporations. This appendix lists all companies that have received investments from the two Ad Astra funds, Kaw Holdings, and Wichita Holdings. The amount of the Ad Astra Funds invested in each company are current as of February 1996, and for the Holding Companies as of June 1996. For investments that have been written off or companies that are out of business, the amount invested is the original investment made by the Ad Astra funds. Based on documents we reviewed, Manhattan Holdings has not invested in any companies. The amount of royalties received represents KTEC's share of royalties from companies. This was calculated based on the percentage KTEC funds originally contributed to the Ad Astra funds (68% in Ad Astra I and 73% in Ad Astra II).

Fund	Company	Amount invested	Investment status	Royalties received
Ad Astra I	3D Biomedical Imaging, Inc.	$262,241		
	BioCore, Inc.	250,000		$27,350
	BioVet, Inc.	0 (a)		
	Crescendo Systems, Inc.	130,835	written off	
	Cypress Systems, Inc.	197,250		
	Diagnostic Concepts International, Inc./ Janus Technologies, Inc.	300,982		
	Interactive Concepts, Inc.	312,498	written off	
	Midwest Superconductivity, Inc.	45,600		
	Novatech, Inc.	259,264		
	NovaTech Railroad Services, L.C.	10,112		
	Oread Holdings, Inc. (Oread Labs)	23,333		
	Sitback Technologies	211,273	written off	
Ad Astra II	AeroComm, Inc.	183,000		
	Allen Information Systems	100,000	out of business	4,557
	Agri-Technology, L.P.	205,000		339,304
	Cydex, Inc.	115,000		
	EHV Corporation	67,000		
	Fluid Solutions	10,155	written off	
	Hybrids International, LTD	250,000		
	IEM, Inc.	240,000		
	Impact Dynamics, Inc.	250,000		
	Janus Biomedical, Inc.	152,338		
	Knowledge Communication, Inc.	75,000		
	MacroDyne, Inc.	141,000		
	QuVis, Inc.	120,000		
	Rubber Recovery Technologies, Inc	75,000		
	Star Transportation Products	145,000		
Kaw Holdings	H.E.L.P Innovations, Inc.	50,000		
	The Coach's Edge	50,000		
	BioScience Innovations, Inc.	30,000		
Wichita Holdings	Impact Dynamics	105,000		
	Pelleting Concepts International	15,000		
	ReLight America	70,000		
	Innovative Ideas, Inc.	20,000		

(a) This investment was received as part of the Biocore, Inc. investment. Ad Astra I did not directly invest funds in BioVet, Inc.

APPENDIX B

Companies Receiving Applied Research Matching Grants and Royalties Paid By Those Companies

As mentioned in the Overview, KTEC provides grants to technology-based businesses to help them conduct scientific research and testing of new technologies and products. Applied Research Matching Grants pay up to 40% of the company's research costs. The following table lists all of the companies that have been awarded ARMF grants since the program began in fiscal year 1988, and the amounts of those grants. Those companies that have paid royalties back to KTEC through fiscal year 1996 are denoted with an *. The total amount of royalties paid by those companies through fiscal year 1996 is shown on the last page of this appendix.

1988

Cypress Systems, Inc.	$8,000
Odontex, Inc.	100,000
Ametek, Inc.	60,000
Boeing Military Airplane Company	16,601
Olathe Manufacturing, Inc.	29,978
Center for BioAnalytical Research	5,800
Physio Technology, Inc.	45,885
Marion Laboratories, Inc.	32,880
NCR Corporation	14,849
Boeing Military Airplane Company	26,525
Osborne Industries, Inc	8,000
National Cooperative Refinery Assoc.	4,665
Shimadzu-Kansas Research Laboratory	110,000
Kansas Wheat Commission	160,000
Oread Laboratories	80,000
Sogetal, Inc.	9,725
Hills Pet Products	18,563
	$731,471

1989

Groundwater Management, Inc.	$5,333
Kraft TeleRobotics, Inc.	120,000
Precision Pattern, Inc.	7,878
Beech Aircraft Corporation	13,623
Beech Aircraft Corporation	8,000
Cypress Systems, Inc.	32,000
Boeing Military Airplane Company	21,305
Boeing Military Airplane Company	13,494
Boeing Military Airplane Company	13,774
Boeing Military Airplane Company	15,066
Boeing Military Airplane Company	13,333
Dubbert Industries, Inc.	2,852
Pitt-Plastics, Inc.	4,178
Wiseda Corporation	73,930
American White Wheat Producers Asso,c.	37,337
Boeing Military Airplane Company	10,510
Hay and Forage Industries	9,332
Agri-Technology L.P.	14,114
Boeing Military Airplane Company	24,493
K-VET, Inc.	9,960
	$450,512

1990

Fuel, Inc.	$3,969
COMDISCO Systems, Inc.	11,487
World Wood Recycling, Inc.	15,163
NCR Corporation	33,063
Ametek, Inc.	75,532
Cessna Aircraft Company	35,088
Aquaculture Engineering, Inc.	14,108
Kansas Wheat Commission	168,000
Dispensing Technologies	12,960
Interface Consultants	14,520
Kraft Telerobotics, Inc.	100,000
American White Wheat Producer Assn.	20,632
Surfaces Research and Applications	2,667
EEC Corporation	14,650
Kantronics, Inc.	6,666
On-Track Corporation	39,058
Catalytic Industrial Group, Inc.	12,656
Great Bend Manufacturing Company	48,308
Quad Recovery Systems, Inc.	47,513
Martin-Logan, Ltd.	10,404
Shimadzu-Kansas Research Laboratory	85,300
Aerotech Engineering and Research	40,616
Boeing Military Airplane Company	48,407
McPherson Manufacturing, Inc.	19,061
Hybrids International, inc.	40,666
Oread Laboratories, Inc.	11,303
Beech Aircraft Corporation	9,075
McPherson Manufacturing, Inc.	60,900
	$1,001,772

1991

Agri-Technology L.P. *	$56,236
Mobay Corporation	48,683
Kansas Wheat Commission	60,000
Plant Bioregulator Technologies, Inc.	2,223
Cessna Aircraft Company	1,840
TouchFax Information Systems	80,140
Advanced Video Technology, Inc.	51,472
Terra Sanctuary, Inc.	27,678
Restaurant/Water Technologies	2,401
DewEze Manufacturing, Inc.	59,400
Osborne Industries, Inc.	8,000
Continental Exploration, Inc.	12,087
COMDISCO Systems, Inc.	18,409
Beech Aircraft Corporation	14,900
Oread Laboratories, Inc.	24,900
Interface Concepts, Inc.	37,090
American White Wheat Producers Assn,,.	34,498
Crust Buster/Speed King, Inc. *	65,752
Beech Aircraft Corporation	8,000
Mobile Care, Inc.	14,823
BioCore, Inc.	15,000
George Martin Morris	14,990
Coleman Outdoor Products, Inc.	7,953
Ctr for Design Development and Production	250,000
Preco Industries, Inc.	14,984
Midwest Superconductivity, Inc.	75,000
Mobile Care, Inc.	35,279
Kantronics, Inc.	12,068
Kantronics, Inc.	5,359
Komala Classic	6,000
McPherson Manufacturing, Inc.	15,000
Hybrids International Ltd.	46,025
BioCore, Inc.	9,833
United Telecommunications, Inc.	10,400
BioCore, Inc.	15,000
Wilch Manufacturing, Inc.	15,000
Oread Laboratories, Inc.	10,660
BMC America	14,000
George Martin Morris	14,600
Osborne Industries, Inc.	9,980
Cypress Systems, Inc.	14,000
Magic Visions, Inc.	12,000
On-Track Corporation	55,090
Kraft TeleRobotics, Inc.	26,025
RUF Corporation	14,950
Terra Sanctuary, Inc.	2,010
Oread Laboratories, Inc.	13,974
Mobay Corporation	14,840
	$1,378,552

1992

M-PACT Worldwide Management Corp,.	$93,500
American Water Purification, Inc.	34,115

Aerotech Engineering and Research	42,440
Aerotech Engineering and Research	11,500
Cardwell International, Ltd.	9,676
Briggs Manufacturing, Inc.	14,926
Agri-Technology/Kincaid Equipment *	100,000
Radiant Systems, Inc.	25,509
AeroComm	99,500
Midwest Superconductivity, Inc.	52,118
Oread Laboratories, Inc.	19,992
Innovative Material System	14,880
Wilch Manufacturing, Inc.	13,500
Abrasive Cleaning Systems *	8,400
Cypress Systems, Inc.	15,000
American Marine Drives, Inc. *	15,000
Mobile Care, Inc.	5,900
EHV Corporation	54,000
Kanamak Hydraulics	10,256
Gradient Force, Inc.	14,000
Bremson Data Systems, Inc.	6,066
A-S-K Associates	15,000
AgriPro Biosciences, Inc.	13,000
Midwest Biofuels, Inc.	15,000
Agtech, Inc.	12,520
BMC America	2,154
Crust Buster/Speed King, Inc. *	15,000
Hall Medical Laboratories, Inc.	45,000
Turbine Specialties, Inc.	23,692
Royal Tractor Company, Inc. *	43,924
Midwest Superconductivity, Inc.	14,218
Gradient Force, Inc.	86,000
McPherson Manufacturing, Inc.	11,000
American Marine Drives, Inc. *	56,496
Janus Technologies	15,000
BioCore, Inc.	50,000
Midwest Biofuels, Inc.	85,000
TouchFax Information System *	85,000
CrustBuster/Speed King, Inc. *	69,000
Abrasive Cleaning Systems *	5,520
	$1,322,802

1993

Data Discovery, Inc.	$100,000
Valley Audio Products, Inc. *	39,138
P-AYR Products	32,000
Bioanalytical Systems	20,000
Hybrids International Ltd.	92,950
ETG, Inc.	87,740
The Phoenix Group, Inc. *	100,000
BioCore, Inc.	50,000
Cypress Systems, Inc.	15,000
On-Track Corporation	15,000
Aerotech Engineering and Research	9,500
RUF Corporation	14,998
MedVantage, Inc.	67,000
The Smith Truss Company	41,868
Overhead Camera Systems, Inc. *	14,969
Aerotech Engineering and Research	5,500
GMC Electronics	13,700
Rosinante', Inc.	15,000
Osborne Industries, Inc.	7,500
Logic Data Systems	10,000
EHV Corporation	40,000
Jenkins Motorsports, Inc.	37,634
AeroComm	97,000
AgriPro Biosciences, Inc.	10,000
Driver Alert Systems, Inc.	7,780
Aero-Ceramics Company	12,500
Advanced digital Audio Company	14,750
Moss Sales and Service, Inc. *	84,000
Sprint Corporation	29,750
Sutherland Engineering, Inc. *	14,040
Polaris Electronics Corporation	15,000
Devore Systems, Inc. *	5,000
	$1,119,317

1994

Fiber Dynamics, Inc. *	$13,659
Agri-Technology, L.P. *	20,000
The Smith Truss Company	34,987
Arcola Enterprises	54,000
Bioanalytical Systems	34,970
P-AYR Products	40,000
MedVantage, Inc.	99,700
EVAC Systems, Inc.	10,762
LithoCraft Printing Systems	7,283
Data Discovery, Inc.	75,411
Crystal Plains Manufacturing, Inc.	34,726
Xymax 2001, Inc.	73,500
Gutenberg Development Group, Inc.	95,500
Portson, Inc.	82,000
Marc Medical, Inc.	62,254
EntraCare Corporation	31,700
Research Concepts, Inc.	19,500
Fluid Solutions, Inc.	6,784
Kansas Geological Survey	31,007
Felton Medical, Inc.	26,288
BioFoods, Inc.	80,000
Mega Manufacturing, Inc.	100,000
Cardwell Manufacturing, Ltd.	100,000
X-Flex Corporation	4,422
Managed Data Solutions Corporation	19,850
The Phoenix Group, Inc. *	20,000
TensorTech Systems	20,000
Driver Alert Systems, Inc.	4,400
	$1,202,703

1995

3D Biomedical Imaging	$87,000
Aeromotive	19,200
Cypress Systems	11,832
Cytech	14,250
Cytech	49,313
Data Discovery	25,000
DCI	100,000
DEBSOFT/MicroQuest	19,000
DT Collectibles	95,000
Erwin Business Investment	13,400
Fluid Drag Research	19,600
GrapeVine Interactive	100,000
Gutenberg Development Group	20,000
H.E.L.P Innovations L.C.	19,320
Hanuman II Corporation	10,000
Hutterer Aircraft	5,000
ID, Inc.	14,000
Impact Dynamics	70,660
Impact Dynamics	19,957
JACAM Chemical Partners, LTD	35,000
Knowledge Communication	16,340

Knowledge Communication	72,520
Marlborough Scanner Systems	1,319
Medi-Flex Hospital Products	98,800
Meetech Corporation	24,510
Millennium Corporation	20,000
Multinational Trading Company	12,000
P-AYR Products	20,000
Pelleting Concepts International	31,667
Pharmedic Co.	56,103
Physio Technology	20,000
Precision Built Systems	19,602
Precision Built Systems	79,020
ReLight America	19,200
	$1,238,613

1996

Addiction Research Corp, Inc.	$20,000
ARCLASER Technologies LLC	20,000
Audio Communications, Inc.	20,000
COMPROSE	60,530
DT Collectibles, Inc.	30,000
EHV Corporation	100,000
Impact Dynamics	76,608
Intelligent Wireless Systems, Inc.	20,000
International Software Systems, Inc.	19,700
Leaton Industries, Inc.	12,000
Logic Data Systems	2,000
Millennium Corporation	45,000
Mobile Care, Inc.	20,000
Mobile Care, Inc.	50,000
NANTEK	100,000
O'Mara Enterprises	20,000
Pelleting Concepts International	99,604
Prairie Innovations, Inc.	20,000
Precision Built Systems, Inc.	90,000
QuVis, Inc.	100,000
SafeTech International, Inc.	85,000
Surfaces Research & Applications	50,000
The Coach's Edge	34,850
Wright Associates Limited	20,000
	$1,115,292

Companies That Have Paid Royalties to KTEC and the Amount of Such Royalties

Company	Royalty Amount
Abrasive Cleaning Systems	$ 4,589
Agri Technology	135,713
American Marine Drivers	28
Crustbuster/Speed King	32,140
Devore Systems	5,000
Fiber Dynamics	13,876
Moss Sales and Service	2,025
Overhead Camera	300
Phoenix Group	1,140
Royal Tractor Company	9,000
Sutherland Engineering	5,352
TouchFax Information System	1,885
Valley Audio	12,680
	$223,728

APPENDIX C

Assistance Received by Companies Identified as Possible Conflicts of Interest

We identified thirteen companies that had relationships with economic development agency employees that could represent conflicts of interest. This appendix describes the types of assistance the companies received from economic development agencies, primarily KTEC and KTEC-related programs or centers.

Ambler Software Engineering	• Services from Center of Excellence in Computer-Aided Systems Engineering
BioScience Innovations, Inc.	• Commercializes technologies from Higuchi Biosciences Center • Client of Kansas Innovation Corporation • Kaw Holdings investment ($30,000)
Cadence Design Systems	• Services from Center of Excellence in Computer-Aided Systems Engineering
CyDex, Inc.	• Client of Higuchi Biosciences Center • Ad Astra II investment ($115,000)
Cypress Systems	• Client of Higuchi Biosciences Center • Applied Research Matching Grants from KTEC ($95,832) • Ad Astra I investment ($197,250)
Data Discovery, Inc.	• Applied Research Matching Grants from KTEC ($200,411) • Services from Center of Excellence in Computer-Aided Systems Engineering
EHV, Inc.	• Services from Advanced Manufacturing Institute • Applied Research Matching Grants from KTEC ($194,000) • Ad Astra II investment ($67,000)
Fast Lane Communications	• Services from Center of Excellence in Computer-Aided Systems Engineering • Client of Kansas Innovation Corporation
Free Spirit Enterprises	• Services from Mid-American Commercialization Corporation
Hanuman II	• Client of Kansas Innovation Corporation • Applied Research Matching Grant from KTEC ($10,000) • Services from Center of Excellence in Computer-Aided Systems Engineering
Impact Dynamics, Inc.	• Applied Research Matching Grants from KTEC ($167,225) • Client of Wichita Technology Corporation • Wichita Holdings Investment ($105,000) • Ad Astra II investment ($250,000) • Services from National Institute for Aviation Research
Janus Biomedical	• Ad Astra II investment ($152,338)
Lawrence Applied Research	• Services from Center of Excellence in Computer-Aided Systems Engineering

APPENDIX D

Summary of Survey of Economic Development Agency Employees

On July 8, 1996, we mailed surveys to all full-time employees of the State's economic development agencies: the Department of Commerce and Housing, KTEC, Kansas, Inc., Mid-America Manufacturing Technology Center, and the Centers of Excellence. In all, we mailed 351 surveys to agency employees. We received 87 completed surveys from employees, giving us an overall response rate of 25%. This appendix is a summary of the responses from the surveys.

Legislative Division of Post Audit
Survey of Employees of the State's Economic Development Agencies

The Legislative Post Audit Committee of the Kansas Legislature has directed the Legislative Division of Post Audit to review certain aspects of the State's economic development agencies. To help us determine whether present conflict of interest policies and procedures are adequate, we are asking economic development agency personnel to answer the following questionnaire.

Please take the time to answer the following questions. The results will be tabulated and reported in such a way that you cannot be personally identified, but questionnaires will be included in the audit working papers which will become public once the audit is completed. Please return the completed questionnaire in the enclosed, self-addressed, postage-paid envelope by **Friday, July, 12 1996**. If you have questions, please contact Laurel Murdie at the Legislative Division of Post Audit, 800 S.W. Jackson, Topeka, Kansas, 66512, or call 913-296-3792. Thank you for your assistance.

---

1. What is your official job title? ________________________________

2. Does your agency have policies that would prevent you or your spouse from owning an interest in, receiving a salary from, or accepting gifts from businesses or entities that receive moneys from your agency?

[34] Yes [20] No [33] Don't know

3. Does your agency have policies that would require you to disclose that you or your spouse have an interest in, receive a salary from, or have accepted gifts from business or entities that receive moneys from your agency?

[56] Yes [5] No [26] Don't know

4. If your agency has such policies, have they been clearly explained to you?

[52] Yes [20] No [4] Don't have such policies

5. If your agency has such policies, do you think those policies are adequate?

[52] Yes [1] No (please explain below) [2] Don't have such policies [27] Don't know

Require too much paperwork. Business culture prevents conflicts from occuring.

6. Are you aware of anyone in your agency who has a financial interest in or who has benefitted financially from a company that your agency deals with? (For example, a company that your agency has a contract with, has loaned moneys to, or has equity in.)

[9] Yes (If yes, please describe, and if known, include the company involved.) [76] No

Conflicts are inherent in technology transfer, but we follow Board of Regents policies.

Mentioned CyDex (2), Impact Dynamics (2), Free Spirit Enterprises, and Astra Technologies.

Comments on disclosure of Rich Bendis's holdings (3) and Ted Kuwana.

APPENDIX E

Agency Responses

On September 10th, we provided copies of the draft audit report to the Kansas Technology Enterprise Corporation, Kansas Inc., the Department of Commerce and Housing, the University of Kansas, the Mid-America Manufacturing Technology Center, the Advanced Manufacturing Institute, the Center for Design, Development, and Production, the National Institute for Aviation Research, the Mid-America Commercialization Corporation, the Kansas Innovation Corporation, the Wichita Technology Corporation, the Kansas Board of Regents, and the Kansas Commission on Governmental Standards and Conduct. Their responses are included as this appendix.

After carefully reviewing the responses, we have made changes to the report to clarify certain issues. In addition, we expanded our Recommendation 3 to incorporate the Board of Regents' comments.

KTEC
KANSAS TECHNOLOGY ENTERPRISE CORPORATION

KTEC's mission is to create, grow and expand Kansas enterprises through technological innovation.

September 23, 1996

RECEIVED
SEP 23 1996
LEGISLATIVE POST AUDIT

Barbara J. Hinton
Legislative Post Auditor
Legislative Division of Post Audit
Mercantile Bank Tower
800 S.W. Jackson St., Suite 1200
Topeka, KS 66612-2212

Dear Ms. Hinton:

Thank you for the opportunity to review and comment on the performance audit Reviewing the Compensation of Executives of the State's Economic Development Agencies.

In our response we have included an Addendum which includes comments from KTEC staff, directors of the Centers of Excellence, MAMTC, and the presidents of the Innovation and Commercialization Corporations.

If I or my staff can be of any further assistance to you please do not hesitate to contact us.

Best regards,

Richard A. Bendis

Richard A. Bendis
President

Enclosure

214 W. 6th, First Floor ■ Topeka, KS 66603-3719
Phone: 913 / 296-5272 Fax: 913 / 296-1160
E-mail: ktec@ktec. com EOE

THE KANSAS TECHNOLOGY ENTERPRISE CORPORATION
RESPONSE TO THE LEGISLATIVE DIVISION OF POST AUDIT REPORT

REVIEWING THE COMPENSATION OF EXECUTIVES OF THE STATE'S ECONOMIC DEVELOPMENT AGENCIES
September 1996

INTRODUCTION

The audit was performed on Kansas Inc., the Kansas Department of Commerce and Housing (KDOCH), and on the Kansas Technology Enterprise Corporation (KTEC).

KTEC is pleased with the following audit results:

- **The compensations for KTEC executive-level staff are within the ranges of their peer groups both within Kansas and nationally; and**

- **No instances of conflict of interest occurred which were not managed consistent with K.S.A. 74-8101(e) and in no case was there any evidence or suggestion of self-dealing.**

The audit makes specific recommendations relative to its findings and KTEC is taking the following actions:

- **KTEC concurs that steps should be taken to formalize written conflict of interest policies with its own staff and has already taken steps to do so. Additionally, we are addressing this issue with our contracted programs.**

- **KTEC more clearly understands the role of the Commission on Governmental Standards and Conduct and has taken steps to develop our own policy to review Statements of Substantial Interest which are submitted annually to that office. We have requested copies of the most recent forms on file for our review.**

KTEC and its program directors and subsidiaries have carefully reviewed the audit and consolidated the responses to the various individual issues throughout the report. Accordingly, the term "KTEC" as used throughout this response refers to staff, board of directors, and other affiliated programs and entities, unless clearly indicated to the contrary.

While the report is fair, KTEC does find its presentation style, in some instances, to lend the actual findings to misinterpretation. While bolded headings may be true, the explanation which follows often sheds a clarifying light on the statement which, if taken alone, is subject to misinterpretation. For example, the statement on page 22 that in "In 3 of the 13 start-up companies where we found relationships, economic development employees owned stock in those companies at the time they were receiving assistance from the

State" could be construed to imply that individuals had made or were in a position to make funding decisions which impacted their own personal gain. But if one reads further in the report, it is noted that in each case the *potential* for conflict was properly managed - a finding which could not have been inferred from the bolded heading, which a casual reader might assume to be a complete summary of the findings.

With regard to the KTEC president's compensation, it was within the peer group's range and, even though it was at the high end of that range, the report notes that: "The President of KTEC's salary was higher than similar officials in the other states we were able to get information from, but was in-line with salaries paid to non-profit or private entities performing similar jobs." (Page 10)

Concerning the compensations of the presidents of MAMTC and the ICCs, it should be remembered that these are private corporations with governing boards of directors. While KTEC is surely an investor in each of these organizations, in no case is KTEC the sole authority or funding source. In the case of the Centers of Excellence, the directors are employees of their respective universities, their salaries are for the performance of faculty duties in addition to management of the Center, and their salaries, for the most part, are not paid with KTEC/EDIF funding.

With regard to conflict of interest, the relative absence of even questionable relationships attests to the integrity of the people involved and the safeguards in place. In none of the cases where the *potential* for a conflict of interest existed had anyone been allowed to make a funding decision involving a company in which they had a financial interest. In a few isolated cases, however, individuals had inexcusably failed to disclose that such a potential existed.

The potential for conflict of interest is naturally inherent in return-minded technology transfer. The challenge then is to manage the conflict properly through distancing individuals from funding decisions involving their own interests and making full disclosure of those potentials for conflict of interest. To this end, KTEC endorses all of the audit recommendations with the exception of 4a, which would eliminate the possibility of a potential conflict of interest by eliminating all interest. Within these guidelines, KTEC could be no more than another granting agency with no means for the state to share in a client's success or to oversee the state's investment responsibly.

OVERVIEW

KTEC feels that it is appropriate to provide some background information and historical perspective. In fiscal year 1986, a bi-partisan task force consisting of legislators and other leaders around the state evaluated the economic development efforts then in effect throughout the state of Kansas. That task force made numerous recommendations, some involving the (new) concept of public/private partnerships and quasi-public agencies.

Out of the desire to get away from the state doing "business as usual," KTEC was created through legislation to have the powers, abilities and responsibilities of a traditional corporation, even though we receive operations and base program funding from the state.

KTEC is unique within the state of Kansas, as well as within the United States. KTEC performs investment and program portfolio management functions. This statutorily-created mandate brings with it its own challenges: how to be accountable to the State (both in management of the "investment" of the State's funds and in the results obtained from the investments) and at the same time operate as an independent agency with the statutory ability and responsibility to be innovative, competitive, aggressive and return-on-investment oriented. This dual mission includes traditional economic development, which includes the creation of jobs and new companies and the generation of tax dollars, as well as the non-traditional "financial return on investment" which, if successful, can eventually decrease KTEC's dependence on legislative appropriations.

Many states, having struggled for years to address these same issues and develop effective and successful technology economic development programs, are now modeling their programs after KTEC. KTEC has a reputation nationwide as one of the most innovative and successful economic development agencies to ever be created. One key factor which is difficult to duplicate, however, is the bi-partisan support KTEC has received in Kansas from governors, the legislature, congressional leaders, community economic development organizations, and the private sector. That support has contributed to KTEC's success.

Since its inception, the success of KTEC has been measured by many standards. There are many definitions of "economic development," just as there are varying opinions as to how state funds should be used. KTEC has always been responsive to the state and participates through the formal budget process, appears before many legislative committees, and responds to all requests for information.

The majority of KTEC's budget is from the Economic Development Initiatives Fund (EDIF). All state and federal monies are initially deposited into the state's accounting system and payments are processed accordingly. KTEC also has other income sources through royalties and fees, which we return to the programs which generated the income. By statute, KTEC has the ability to award grants, engage in seed and venture financing, create for-profit and not-for-profit subsidiaries, receive royalties, hold equity interests, borrow and loan money, and enter into contracts. KTEC "invests" the state's money in "clients," each of which is closely monitored.

Key to any success is the caliber of the people doing the work and the long-term continuity of staff, board members and program managers. Throughout our development process, KTEC has tried to associate the most qualified individuals with its programs, individuals who have the skills and experience to work successfully in economic initiatives combining public and private interests. We have some employees who have significant experience in public sector organizations and who provide oversight and management of KTEC's programs. Other individuals with extensive private sector experience were hired by private entities, in which KTEC has invested, to operate those entities in an innovative and competitive manner in order to achieve a significant return on investment for their stockholders.

In this regard, KTEC's board of directors hired a president who had the necessary public **and** private sector experience to manage both the state's "investments" as well as all stages of the more traditional private sector investment practices. The president's compensation, while fair, is less than what is offered in the private sector for comparable skills. For that reason, individuals possessing the necessary qualifications generally do not want to become state employees.

KTEC's president is Richard A. Bendis. Through serving on the KTEC board from 1987-1993, serving as its first board chair, working as a consultant for KTEC to establish the Innovation and Commercialization Corporations in 1993, and serving as acting president in 1994, he had the public sector experience to effectively work with state and federal government. His private sector business experience, which includes working for large corporations, taking a private technology corporation public, and managing his own investment company, provided him with the necessary background to work with KTEC's seed and venture capital programs as well as its portfolio of economic development programs.

The KTEC board of directors recognizes that the accepted forms of compensation for private sector executives may be different than that of public sector executives. The legislature recognized KTEC's need for a president with diverse skills and experience and by statute gave the board the authority to enter into the appropriate employment agreement with the president who would direct and supervise the administrative affairs and general management of the corporation. The legislature has determined that KTEC should be involved in seed and venture capital investments and management, and authorized KTEC's board of directors to compensate KTEC's president in order to attract an individual possessing the experience in those industries.

The legislation requires the president and staff of KTEC to report to a board of directors composed of private sector and legislative appointments by the Governor and legislative leadership, certain cabinet secretaries, and university representatives. Through quarterly meetings, the board makes decisions regarding budget, grants and other issues. Additionally, by statute, KTEC employees are considered unclassified employees, and their salaries are determined by the board. We annually review job descriptions, perform position evaluations, and establish annual performance indicators which we measure on a quarterly basis. Each spring the president makes recommendations to the KTEC executive committee and board based on the outcomes of this review process. Comparisons of salary levels are also done as needed.

The staffs of KTEC's contracted programs are not considered to be KTEC employees. The directors of the five Centers of Excellence are employees of either the University of Kansas, Kansas State University, Wichita State University, or Pittsburg State University. Some of the directors of the Centers of Excellence are tenured professors. The employees of the two Industrial Liaison Offices (which are independent 501(c)3 corporations) are private employees who report to their individual private sector boards of directors. The three Innovation and Commercialization Corporations (ICC's) are also independent 501(c)3 corporations and each one has invested in a privately organized and operated for-profit seed capital fund. The private managers of the ICC's, too, report to their individual boards of directors. KTEC intentionally has legislators serve on the boards of its granting entities to ensure that the ICC's accountability to KTEC and conflict of interest issues as they relate to KTEC are appropriately managed.

While the KTEC board determines the grant amounts it will award to the ICCs' programs, the ICC's all receive funds from sources other than KTEC. KTEC awards a grant to them through a contractual agreement. The KTEC board does not control salary issues related to the personnel of ICC entities. This arrangement is similar to other state agencies which award grants of state or federal monies to private groups to carry out specific programs or tasks. While those agencies monitor the awards, they do not become involved with the salary issues of those private groups.

KTEC concurs with the Post Audit recommendation 4(c) which states: "If the Legislature wants to ensure that potential conflicts of interest are managed, but it wants to leave those decisions entirely up to the agencies involved, it need not act in this area as long as the State's economic development agencies develop and follow appropriate policies and procedures in this area, as recommended in this report. Those conflicts may still occur, but agencies will be aware of them and can manage them accordingly."

K.S. A. 74-8101(e) regarding conflicts of interests involving the KTEC board of directors is already in place. KTEC has already taken steps to formalize written conflict of interest policies with its own staff and is addressing this issue with its contracted programs.

Attached is an Addendum which summarizes the audit responses from the KTEC affiliate program managers.

ADDENDUM

SUMMARY OF INDIVIDUAL KTEC'S AFFILIATE PROGRAM MANAGERS' RESPONSES TO THE POST AUDIT REPORT

The focus of the audit involves two separate issues, Compensation of Executive-Level Staff and Conflict of Interest. We will respond individually to each one.

I. Compensation of Executive-Level Staff in Kansas' Economic Development Agencies:

♦ **Pages 11, 13 & 14**

ICC's: The ICC presidents are not paid only from state funds. They receive a grant from KTEC, but also receive funding from private sources.

MAMTC and the ICC's are independent 501(c)3 not-for-profit corporations. The money from the state goes into them, but the state gets something back. They are outside the state auspices.

MAMTC: The Chief Executive Officer **is** formally evaluated annually by the MAMTC board of directors. The MAMTC Regional Directors in Manhattan, Overland Park, Pittsburg and Wichita are University employees. The Vice President of Operations and the Regional Director in Great Bend are **not** state employees.

Centers of Excellence -The salaries listed for the center directors do not indicate that the majority of their money comes from the University for performance of faculty duties. The largest part of their salaries is not paid from KTEC or EDIF money.

♦ **Pages 12, 16 - 18**

Two of the oldest and largest technology economic development entities, namely the Ben Franklin Program and the Ohio Edison Program were not included in the comparison.

Duties of KTEC President and Vice Presidents should include:

> "President: 10 years of venture capital experience; former President of an entrepreneurial public computer systems company, former President of $90 million national health care services firm, 20 years executive level management experience, 9 years of experience with KTEC."
>
> "Vice President of Operations: Manages Information Technology, Accounting, Human Resource and Graduate Intern Programs. Responsible for writing, submitting and oversight of Agency budget."
>
> "Vice President of Applied Technology: Manages the Applied Research Matching Fund and Industrial Agriculture programs."
>
> "Vice President of Innovation and Research: Manages SBIR, SSBIR and IDAP programs."
>
> "Vice President of University/Federal Programs: Provides oversight to Centers of Excellence, MAMTC, and ICCs. Develops policies and procedures, establishes performance measures and monitors performance of programs for all three entities."

II. Conflict of Interest

<u>Post Audit has stated to us that the focus of this portion of the audit was on start-up rather than established companies.</u> Most of the scope of KTEC is to assist start-up, technology-based companies. This is not an area which Kansas Inc. has any involvement. Similarly, KDOCH focuses more on retention, recruitment and training for existing companies and improvements in community-wide and housing areas of economic development.

- **Pages 20, 27, 28, & 29**

  Reviewing and filing conflict of interest forms: KTEC thought these documents were confidential. All forms state that they are to be completed by the employee and mailed directly to the Governmental Standards and Conduct Office (GSCO). KTEC thought that GSCO would be responsible for compliance and cross-checking to see if conflicts exist and would notify KTEC accordingly. KTEC has already requested copies of the current forms on file for individuals from the GSCO.

  Also, while it may not appear in writing that certain KTEC employees are required to fill out SSI forms, KTEC has always cooperated with the GSCO annually in supplying lists of board members and current staff. They have always made the determination as to who would receive an SSI form.

  Since this audit, KTEC has developed a written policy for staff. The ICCs have, or will, implement a policy as well. The centers of excellence fall under the Board of Regents policy.

  KTEC adopted the Governor's Ethics Policy at its June 1996 board meeting.

- **Pages 22, 25, & 27**

  KTEC Staff and Board Issues: The current president of KTEC has submitted Statements of Substantial Interest since 1987 in his capacity as a board member for KTEC and as the president. He was appointed to the KTEC board originally to represent the financial sector in the area of high-risk venture investments. His personal investment in Janus Biomedical was through his venture capital company and took place before his appointment. Per K.S.A. 74-8101(e), he did not vote on issues regarding Janus Biomedical.

  The individual mentioned has not served on the KTEC board since 1994; however, he observed K.S.A. 74-8101(e) and filed the Statements of Substantial Interest. (page 25, para 8)

  K.S.A. 74-8101, which deals directly with the KTEC board of directors, was omitted from this list of conflict of interest provisions. (page 27)

  (K.S.A. 74-8101(e) states: "Members of the board of directors, in their dealings with enterprises that may receive financing through the corporation, shall declare any potential conflict of interest and abstain from voting prior to taking any actions relating to that transaction."

  The KTEC Vice-President discussed her company with MACC staff and the potential conflict was disclosed in order to assess what the relationship would be. The Vice-President was not on the MACC board at the time. A relationship between her company and MACC was not developed and she does not plan to pursue it any further.

- **Pages 22, 24, 25, 31**
  Universities and Centers of Excellence: It was not mentioned that in several of the potential conflicts the university employee received his-her shares as an inventor or co-inventor, which is sound business practice and university policy. When a university spin-off company went back to the university for services, which are available to any company, the spin-off company paid the same fees as anyone other company would have been charged.

  CECASE: The University of Kansas is submitting a separate response to the Legislative Division of Post Audit.

  HBC/CyDex: The university led the discussions regarding business formation for CyDex and asked the Center's Executive Director and Lab Director to participate to provide technical information about the compound and the pharmaceutical industry in general. The decision to form a company was taken after about two years of exploration of various ways to commercialize the technology. The KTEC funds referred to were a grant to pay for initiating the international patent filings to ensure the value of the technology. This grant is currently being repaid to KTEC (two payments have been made to date). There was also a small grant to HBC to allow them to hire a consultant to examine the various routes for commercialization.

  It is stated that the Executive Director is not involved in the decision-making process for funding projects within the Center for Drug Delivery Research (CDDR). That is the responsibility of the CDDR Director and the Core Faculty Advisory Board. In the case of projects relating to cyclodextrin funding, only the Core Faculty Advisory Board decides so that there can be no undue influence of the CDDR Director not the HBC Executive Director.

  AMI/EHV: The Advanced Manufacturing Institute (AMI) has not made any direct contribution to EHV Corporation. The contribution has been to Jim Hague, who at the time was a faculty associate of AMI doing research on the Department of Energy's Electric Vehicle Site Operator Program. The decision for support to the faculty is made by the AMI Director and not the Associate Director.

  It is stated that the AMI Associate Director did not disclose his interests in the company; however, he has reported this on the SSI forms since he has been associated with the company. AMI has copies of the forms from 1993. His association with the company ended in December 1994 and he does not hold a position or stock with the company.

  WSU: The threshold for WSU is actually $10,000, which is consistent with Board of Regents policy.

- **Pages 24, 30, & 31**
  Innovation & Commercialization Corporations: The ICC presidents are employed by private corporations. They make investments on behalf of their shareholders and it is prudent (and standard practice) for representatives of the shareholders to serve on the boards of the companies for no additional compensation. KTEC is one of those shareholders, and likewise is represented on the board by a staff member to represent KTEC's interests.

  Directors represent stockholders and serve on key committees where officers would have a conflict of interest (e.g., compensation committee). Officers run the day-to-day operations of the company on a full-time basis. University professors and employees should be able to serve as directors but not as officers. As long as the stock is not material such a role should not be a conflict of interest.

The statement is correct that the ICC presidents and seed/venture fund managers aren't state employees. However, they are not necessarily paid from state funds. KTEC awards grants to the ICCs and they also leverage that funding with other sources. Compensation could occur from any of those funds. One ICC president **was** compensated through the state system in FY96; however, KTEC reduced the grant which was directly awarded to that ICC by the amount of the salary and benefits. That person will go off the state payroll system in FY97. The seed/venture fund managers no longer receive any state funding and employee compensation is through their various income sources.

The ICCs and their for-profit holding companies are considered private companies. The ICC presidents were hired based upon their private sector investment backgrounds and were provided small profit participation incentives as part of their compensation package.

WTC/IDI: The Report states that the individual resigned from the university because of concerns over her employment in IDI. The IDI board informed her that she could not be president of IDI and remain with the university, due to the fact that being the president of the company would be a full-time job and no other employment activities would be allowed. Given that choice, she chose IDI as she felt it would provide a better long-term career path.

- **Page 30, information box**
  Seed/Venture Capital Fund: The seed/venture capital fund is not owned by the State of Kansas. It is owned by private investors of which the State, through KTEC, is a limited partner investor. It is privately organized under the Revised Uniform Limited Partnership Act, and privately managed.

- **Pages 34 & 35**
  Conclusion: Examples were not given indicating that disclosure and abstention failed. The legislature chose the method of disclosure and abstention and KTEC has followed it. The only instances that presented "perceived" conflict of interest occurred at a university where written policies are in place but a potential conflict of interest was not disclosed.

KTEC intentionally has legislators serve on all of the boards of its granting entities to ensure that accountability and conflict of interest issues are managed.

Option "a" would greatly hamper or limit the university's role in serving Kansas. Professional schools, such as engineering, strive to recruit the best experts as faculty and research staff. Outstanding faculty and research staff are expected to be called upon by industry and government agencies for their expertise, and occasional conflicts of interest are inevitable. Attempting to eliminate any **interest** by staff to serve on boards in an oversight but non-compensatory role would put KTEC in the position of investing/granting state money but preventing us the opportunity to safeguard that investment and would run counter to the issue of accountability which is desired by all involved.

Options "b" and "c" recognize this fact, and provide mechanisms for addressing conflicts. Option "c" retains authority and primary responsibility at the agency level, providing maximum efficiency.

KANSAS, INC.

Charles R. Warren, President

632 S.W. Van Buren, Suite 100, Topeka, Kansas 66603
(913) 296-1460 · fax (913) 296-1463

September 17, 1996

RECEIVED
SEP 18 1996
LEGISLATIVE POST AUDIT

Barbara J. Hinton
Legislative Post Auditor
800 S.W. Jackson Street
Suite 1200
Topeka, Kansas 66612-2212

Dear Ms. Hinton:

I want to thank you for the opportunity to review the draft report of the performance audit, Reviewing the Compensation of Executives of the State Economic Development Agencies. I believe that Legislative Post Audit has produced an important report that contains significant recommendations regarding potential conflicts of interests and relationships between business clients and the agencies and staff that serve them. Implementation of the recommendations contained in the report should increase the credibility and integrity of the state's economic development activities.

I agree that employees of Kansas, Inc. should be subject to state ethics laws. As you are aware, the Kansas, Inc. Board of Directors has adopted by formal motion the Governor's Executive Order No. 96-1 as a code of conduct for its employees. I also agree that the President of Kansas, Inc. should file a statement of substantial interest with the Commission on Governmental Standards and Conduct. Members of the Kansas, Inc. Board are currently required to file annual statements of substantial interest.

Although I agree generally with the recommendation that written policies and procedures regarding conflicts of interest be adopted by state economic development agencies. I would point out that Kansas, Inc. does not provide grants or loans to businesses, make equity investments, or provide technical assistance. This is clearly stated on page 9 of the report. Kansas, Inc. employees are not in a position to engage in activities that could lead to their direct and individual financial gain, as are employees of other state or state funded agencies. I should also note that your report does not cite any examples or make any suggestions that Kansas, Inc. employees have engaged in activities that would involve any conflict-of-interest.

Board of Directors

Governor Bill Graves, *Co-Chair* John E. Moore, *Co-Chair*

Barbara Allen · Jay Anderson · Joe Bauman · John Farmer, III · Greg Jones · Gerald Karr · John Prather
Alicia Salisbury · Warren Schmidgall · Deryl Schuster · Gary Sherrer · Jack Wempe · Larry Williams

While written policies and procedures are advisable, I would suggest that some entity other than the economic development agency, itself, recommend the form and content of such written policies. This is an area where professional guidance and "model" policies would be highly appropriate. I believe firmly in policies and practices that would provide full disclosure of financial involvement with entities outside of the employing agency.

While I believe that heads of economic development agencies should be fairly and adequately compensated for their duties and performance, I would also affirm that public service is a distinquished calling that yields rewards and satisfaction far beyond those of monetary compensation.

Sincerely,

Charles R Warren

Charles R. Warren, Ph.D.
President

KANSAS
DEPARTMENT OF COMMERCE & HOUSING

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SEP 24 1996
LEGISLATIVE POST AUDIT

September 23, 1996

Bill Graves, Governor
Gary Sherrer, Secretary

Ms. Barbara Hinton
Legislative Post Auditor
800 SW Jackson, Suite 1200
Topeka, KS 66612

Dear Ms. Hinton:

We appreciate the opportunity to comment on your recent audit, Reviewing the Compensation of Executives of the State's Economic Development Agencies. We agree with those findings and recommendations that relate to this agency. We fully intend to follow through on your recommendations with respect to conflict-of-interest procedures and believe the policy we have already established is a good foundation for the other steps you recommend.

We firmly believe that avoiding potential conflicts of interest, or the appearance of such, is an important aspect of our mandate. The study also highlights the potential salary inequities that exist between the various state economic development entities. This raises important questions relating to staff morale, good management practices and recruitment issues.

You and your staff are to be commended on a thorough study of issues that deserve our careful attention.

Sincerely,

Gary Sherrer
Lt. Governor/Secretary

GS:SB:sb

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KANSAS BOARD OF REGENTS
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GENERAL ADMINISTRATION - 913 296-3421 • STUDENT ASSISTANCE - 913 296-3517 • FAX 913 296-0983

September 20, 1996

RECEIVED
SEP 20 1996
LEGISLATIVE POST AUDIT

Barbara J. Hinton
Legislative Post Auditor
Legislative Division of Post Audit
Mercantile Bank Tower, Ste. 1200
800 S.W. Jackson St.
Topeka, Kansas 66612-2212

Dear Ms. Hinton:

Thank you for sharing a copy of the draft performance audit report, Reviewing the Compensation of Executives of the State's Economic Development Agencies. I appreciate having the opportunity to respond on behalf of Board of Regents institutions and the Board. I also appreciate your willingness to accept my response after my return from the Board meeting in Hays. It is the strong belief of the Regents institutions that potential conflicts of interest be disclosed. Failure to report and manage potential conflicts may bring discredit to research and development efforts as well as limit future public support and acceptance of such efforts. To reduce support for economic development activities is to reduce opportunity for students and citizens of the state to reap the benefits of those activities. The universities and the Board of Regents are committed to disclosure of potential conflicts of interest.

Evidence of this commitment to disclosure can be seen from the fact that the Board of Regents first adopted a policy on conflicts of interest in 1974. While there have been periodic revisions, by far the most extensive revision was the 1995 adoption of the Kansas Board of Regents of the policy on "Commitment of Time, Conflict of Interest, Consulting and Other Employment." This policy is intended, among other purposes, to educate members of the University community about conflict situations and to provide a framework within which potential or apparent conflicts may be managed. Another important purpose of the current policy is to enable the universities to verify that applicants for federal grants are not in violation of federal regulations prohibiting conflicts of interest. This policy, for the first time, requires annual reporting by all faculty of substantial interests and potential conflicts.

Officials in the Regents institutions appreciate being apprised of the information discovered in the course of the audit. However, we would call your attention to the fact that the first year of implementing this policy has barely concluded. An assessment process will be initiated soon by our Council of Chief Academic Officers. It would seem that revisions in the policy or related procedures prior to an internal evaluation would be premature.

Emporia State University • Fort Hays State University • Kansas State University

Responses to specific recommendations included in the report are as follows:

2.b. The Regents policy requiring the disclosure and management of conflicts would appear to be reasonably successful considering the fact that the disclosure component of the policy has only been in place for one year.

2.c. Whether employees may decide whether they think a substantial financial relationship represents a conflict of interest could be considered by the Regents institutions as part of the assessment of this policy (See 3 below).

2.d. We appreciate having been advised that Pittsburg State University has not implemented the Board's policy. Clearly, employees of the Center of Design, Development, and Production at Pittsburg State University should file the disclosure form required by the Board so long as they are Regents unclassified employees.

3. It is not self-evident that inconsistency between the Board of Regents definition of substantial interests and the definition used by the Commission on Governmental Standards and Conduct is problematic. In fact, if employees of Regents institutions who are involved in economic development activities are expected to disclose information required by the Commission on Governmental Standards and Conduct it would make sense to require those individuals to file that disclosure. This would appear to be more straight forward and efficient than making modifications in the Regents' policy. The Chancellor and Presidents of the institutions, as agency heads, could be asked to consider designating individuals involved in economic activities as persons required to submit disclosure forms to the Commission on Governmental Standards and Conduct. This requirement might also be adopted by entities disbursing economic development funds.

4. The Regents institutions are subject to a policy and a set of procedures which are intended to serve the purposes of educating Regents employees about the necessity of disclosing potential conflicts of interest so that they may be appropriately managed. The thorough investigation by Legislative Post Audit staff turned up only a handful of circumstances in which relationships appeared to present conflicts of interest. At least half of those relationships which posed potential conflicts were disclosed and managed. When one considers that the total pool is larger than the sixty-one start up companies mentioned in your report, one could conclude that the Regents policy is working rather well.

I would like to express one general concern about an assumption which underlines the audit report. The existence of a relationship which may present a conflict is treated as though such a relationship is inherently wrong. We do not concur with this assumption. The failure to disclose and manage potential conflicts is clearly a different manner. The institutions are strongly motivated to manage such potential conflicts because failure to do so endangers the integrity of research as well as continued public support. The Board has consciously chosen the disclosure and management approach because historically students, the institutions, and the general public all benefit when members of the faculty are actively involved in research and in efforts to transfer research results into useful applications.

Related to the above concern, I ask your indulgence in commenting on the style in which the audit report is presented. In the author's effort to introduce and close each section with a summary, and to use headings to organize the paper, it is emphasized that employee relationships existed in a significant percentage of the sixty-one start up companies. There is only one mention of the fact that some of these do not present conflicts at all. Indeed, a review of each of the instances of potential conflicts reveals that in most cases actual conflicts did not exist or were appropriately managed. Reading only the summary headings and paragraphs leaves the reader with the impression that conflict situations are more extensive and serious than they are. This is particularly troublesome since the report could just has easily have concluded that thirteen relationships, some of which do not constitute conflicts of interest and some of which have been successfully managed, out of 462 companies is an admirable record.

There are a few additional minor points I would like to make. I have been informed that the University of Kansas and Wichita State University now use the $10,000 threshold for substantial interests. Also, all unclassified employees in the Regents system with twelve month appointments earn twenty-two leave days per year commencing with the initial appointment. This is not unique to employees of the Centers of Excellence.

Thank you for the opportunity to respond to the efforts of the Legislative Post Audit staff in addressing an issue of considerable importance to the State of Kansas as well as to research and economic development in the state. The Regents institutions remain committed to disclosure as a first step to addressing potential conflicts of interests and we will work to improve upon our efforts thus far. I hope these comments will be useful.

Sincerely,

Stephen M. Jordan
Executive Director

cc: Members, Board of Regents
Members, Council of Presidents

WICHITA STATE UNIVERSITY

National Institute for Aviation Research

September 17, 1996

Barbara J. Hinton
Legislative Post Auditor
Merchantile Bank Tower
800 Southwest Jackson Street, Suite 1200
Topeka, KS 66612-2212

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SEP 23 1996
LEGISLATIVE POST AUDIT

Dear Ms. Hinton,

Re: Your letter of September 10, 1996

Here are my comments in response to your request.

On page 31, the first paragraph, reference is made to a $5,000 threshold for reporting substantial interest for Wichita State faculty and staff. In fact, the WSU threshold is $10,000, consistent with the Board of Regents policy.

With respect to the options which you present under recommendation #4 (page 34), I believe that option a, eliminating conflicts entirely, would in fact greatly hamper or limit the university's role in serving Kansas. Professional schools such as engineering strive to recruit the best experts as faculty and research staff. Outstanding faculty and research staff are expected to be called upon by industry and government agencies for their expertise, and occasional conflicts of interest are inevitable. Options b and c recognize this fact, and provide mechanisms for addressing conflicts. Option c retains authority and primary responsibility at the agency level, providing maximum efficiency. I recommend retaining option c.

Thank you for giving me the opportunity to respond to the draft of your report.

Sincerely,

William H. Wentz Jr.

William H. Wentz Jr.
Executive Director

Copy: Fred Sudermann
Ted Ayres

Wichita State University, Wichita, Kansas 67260-0093 Telephone: (316) 689-3678 Fax: (316) 689-3175
The National Institute for Aviation Research is a KTEC Center of Excellence

STATE OF KANSAS

Administration of
Campaign Finance,
Conflict of Interest
& Lobbying Laws

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KANSAS COMMISSION ON GOVERNMENTAL STANDARDS AND CONDUCT

September 16, 1996

RECEIVED
SEP 17 1996
LEGISLATIVE POST AUDIT

Barbara J. Hinton
Legislative Post Auditor
Mercantile Bank Tower
800 SW Jackson, Suite 1200
Topeka, Kansas 66612-2212

Dear Ms. Hinton:

Thank you for sending the Commission a draft copy of the audit concerning the economic development agencies in Kansas. After having reviewed the report, and discussing its contents with our Executive Director, Carol Williams, we wish to make the recommendations/suggestions found in this letter.

No matter the outcome of the recommendations your agency makes to the Legislative Post Audit Committee, the Commission will review the changes in the law. Specifically, the question of whether or not certain individuals employed by economic development agencies are "state officers or employees". If it is determined that the law has indeed changed, and our former advisory opinions are no longer accurate, then a new opinion will be issued.

The Commission will also look into asking the Attorney General's Office for an opinion on whether or not these "public instrumentalities" are "state agencies". In light of AG Opinion No. 93-135, the Commission will probably seek an opinion no matter the outcome of this particular audit.

If recommendations are made to require members of these "instrumentalities" to file financial disclose forms, it would follow that the members should also be subject to the rest of the conflict of interest laws under the Commission's jurisdiction (K.S.A. 46-215 et seq.). Specifically, the enforcement provisions in those laws would allow the Commission to help ensure that conflicts of interests did not occur.

If you have any questions or need additional information, feel free to contact me.

Sincerely,

W. Charles Smithson

W. Charles Smithson
Attorney for the Commission

Pittsburg State University

KTEC Center for Design, Development and Production

1701 S. Broadway, Pittsburg, KS 66762 • 316/235-4114

September 18, 1996

RECEIVED
SEP 27 1996
LEGISLATIVE POST AUDIT

Ms. Barbara J. Hinton
Legislative Division of Post Audit
Mercantile Bank Tower
800 SW Jackson St., STE 1200
Topeka, KS 66212-2212

Dear Ms. Hinton:

Thank you for allowing us to respond to the draft copy of your audit, Reviewing the Compensation of Executives of the State's Economic Development Agencies. Below are our corrections and clarifications.

Page 11, Paragraph 1.	The Director of the Center for Design, Development and Production reports to and is reviewed by the Academic Vice President. He also serves a dual role as the Executive Director of the Business and Technology Institute.
Page 13, CDDP Section.	Performance evaluations of all unclassified staff will be done in FY 1997.
Page 31, Paragraph 1.	Pittsburg State University does require its employees to file the disclosure forms according to the Unclassified Personnel Handbook, 2.7.10.4, "Reporting Requirements" and also as stated in the letter to Laurel Murdie - Legislative Post Audit, dated July 12, 1996.

If you need further clarification, please don't hesitate to call.

Sincerely,

E.W. Hollenbeck

E.W. Hollenbeck
Director

cc: Rich Bendis