

HAWAII EXCHANGE FOR LOCAL INVESTMENT

REPORT TO THE TWENTY-SIXTH LEGISLATURE

**Prepared by the
Department of Commerce and Consumer Affairs**

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HAWAII EXCHANGE FOR LOCAL INVESTMENT REPORT TO LEGISLATURE

I. INTRODUCTION

A. SUMMARY OF SCR NO. 134 S.D. 1

The Twenty-sixth Legislature of 2011 adopted Senate Concurrent Resolution (SCR 134 SD1), to form a work group to investigate the feasibility of a locally-focused, Hawaii based stock exchange. It would be chaired by the Commissioner of Financial Institutions, and include the Securities Commissioner and representatives from the investor community.

The Hawaii based stock exchange was envisioned to be a nonprofit corporation, to be known as the Hawaii Exchange for Local Investment and would administer the exchange. The work group considered various issues including the securities laws and regulations associated with the formation of a local investment exchange, the appropriate agency to regulate it, the appropriateness of a nonprofit corporation, the criteria for listing enterprises on the exchange, and indemnification.

The reasons for this investigation stated in the resolution were as follows:

1. The essential sustainability of economic diversification in Hawaii for continued fiscal growth and development;
2. Neither local lenders nor governmental entities are equipped to make significant investments in local enterprises;
3. Hawaii investors do engage in risk-oriented investments primarily through out-of-state entities and national or international exchanges;
4. Hawaii companies seeking capital are restricted under current securities laws to accredited investors and qualified institutional investors;
5. The requirements and costs for listing small-to-medium sized businesses on national or international exchanges are generally prohibitive;
6. Securities laws do allow for a more publicly transparent equity investment process to be conducted between private enterprise and investors located within the same state;
7. Local investment in local companies is an effective means of driving economic growth through the development of diversified industries within the State;
8. A local investment exchange is an effective and efficient method of connecting local investors with local enterprises seeking equity capital;

9. A local investment exchange provides protection for investors and listed enterprises through the enforcement of clear standards and mandatory disclosures for listed enterprises and investors;
10. A local investment exchange will generate awareness of an interest in locally based investment opportunities; and
11. Other jurisdictions which have created or are investigating the possibility of creating local investment exchanges.

B. WORK GROUP

1. **Tasks.** The function of the work group was to investigate the relevant securities laws and regulations relating to the formation of a local exchange, and to recommend to the legislature how to create the necessary regulatory framework for a local investment exchange. Included in these recommendations are for the appropriate agency to exercise regulatory authority, the appropriate staffing for the agency to exercise its regulatory authority, management of the nonprofit corporation, the criteria for listing enterprises on the exchange, indemnification of the exchange from civil and criminal liability, and policies and procedures for securities compliance. A final responsibility of the work group is to submit a report of its findings and recommendations to the Legislature no later than 20 days prior to the convening of the Regular Session of 2012.

2. **Members.** Members of the Hawaii Exchange for Local Investment (“HELI”) Work group include: Iris Ikeda Catalani, Commissioner of Financial Institutions and HELI Chairperson; Richard B. Dole, CEO of Dole Capital, LLC, HELI Vice Chair; Tung Chan, Commissioner of Business Registration Division and HELI Secretary; Dale Kobayashi of Morgan Stanley; David K. Rair, Esq., of Cades Schutte; Brian V. Kearns of HawaiiUSA Federal Credit Union; Gerald Sumida, Esq., of Carlsmith Ball; Neal Okabayashi of Hawaii Bankers Association; Mark Oyadomori of First Hawaiian Bank; and Virendra Nath of HDEP International.

3. **Meetings.** HELI met 5 times: July 28, 2011, September 9, 2011, October 12, 2011, November 21, 2011 and December 16, 2011. In addition, the HELI formed two investigative groups to investigate alternative trading platforms and the Third Frontier, a comprehensive model for coordinating business activity to achieve an orchestrated goal for investment and possible fiscal growth. The HELI was formed to more quickly investigate the two alternatives.

II. INVESTIGATIVE WORK GROUPS

A. ALTERNATIVE TRADING PLATFORMS

1. INVESTIGATION

This investigative group (“IGATP”) investigated existing alternative trading platforms (“ATPs”) regulated by the Securities and Exchange Commission (“SEC”). The IGATP members

were: Richard B. Dole, CEO of Dole Capital, LLC; David K. Rair, Esq., of Cades Schutte; Brian V. Kearns of HawaiiUSA Federal Credit Union; Mark Oyadomori of First Hawaiian Bank; and Virendra Nath of HDEP International. The IGATP found that the existing trading platforms on the U.S. Mainland were either registered as broker-dealers or were organized as branch offices of broker-dealers, utilizing registered representatives for the securities business. These ATPs are engaged in the trading of interests in entities that are not registered for public trading.

Due diligence by the ATP was conducted on every company listed on the trading platforms that was at least as rigorous as for a private offering, to determine if a company is suitable for anyone at all. Once a company is registered (listed), there are investment opportunities for both capital raises and secondary transactions among qualified buyers and sellers. Secondary transactions are conducted both on an auction and a negotiated basis. Qualified buyers and sellers are all either accredited investors or qualified institutional investors. These are the investors who are sophisticated and knowledgeable about investments and are in the position to lose their entire investment.

1. Summary of ATPs. There aren't many regional stock exchanges around today. The Miami Stock Exchange serves as a major currency trading market for the 27 Latin American and Caribbean exchanges. There are also electronic communication networks (ECNs). Prior to closing in 2001 due to a lack of trading, the Arizona Stock Exchange was an electronically enabled stock exchange for carrying out e-Trading after usual market hours. Use was restricted to large institutional users.

The NASDAQ Stock Exchange wasn't always a stock exchange. NASDAQ was a subsidiary of the NASD (now FINRA), before the NASD restructured it in 2000 by selling shares to its members. NASDAQ wasn't approved as a national securities exchange until 2007.

In addition to stock exchanges with trading activities, there are information exchanges that facilitate capital transfer. One is The California Stock Exchange. This exchange serves as a match making and listing service where buyers and sellers can meet in person and work out transactions between themselves.

There are also clearinghouses for private secondary transactions. These clearinghouses or ATPs register companies, accredited investors, and qualified institutional investors. Due diligence on any company registering on a trading platform would be at least as rigorous as for any private offering. Once a company is registered, there are investment opportunities for both capital raises and secondary transactions among qualified buyers and sellers.

2. Existing ATPs.

(a) SecondMarket. SecondMarket claims to be the largest marketplace for private company stock. SecondMarket connects buyers directly with sellers. One must qualify as an Accredited Investor or Qualified Institutional Investor, to view SecondMarket's listings. SecondMarket specializes in pre-IPO companies where significant trading. Activity could be generated. In the case of most small-to-medium sized Hawaii businesses interested in listing on the SecondMarket trading platform, a company would be required to have a minimum market

capitalization of \$100 million in order to list. SecondMarket sometimes makes size requirement exceptions for community banks.

(b) **SharesPost.** SharesPost also connects private companies with investors. SharesPost is a passive bulletin board that enables sophisticated buyers and sellers of private company securities to view existing portfolio items held by its members. As with SecondMarket, SharesPost also specializes in pre-IPO companies where significant trading activity could be generated, and will not list a company on its platform unless it has a minimum market capitalization of \$100 million.

(c) **Mission Markets.** Mission Markets has no minimum market capitalization requirement for companies, and no requirement for company audited financial statements. The average market capitalization of companies is \$2.0 million. Mission Markets charges no due diligence or registration fees. Its revenue source is trading fees in the range of 2%-to-6% per transaction, and may consider a revenue-sharing arrangement with a Hawaii broker dealer. Mission Markets is not a broker-dealer. It is an Office of Supervisory Jurisdiction (OSJ), conducting its securities and investment products through PrimeSolutions Securities, Inc., a registered broker-dealer and FINRA member. Registered representatives with Mission Markets are registered with PrimeSolutions Securities, an independent broker-dealer.

3. ATP Operations and Requirements.

(a) **Summary of How ATPs Work.** A company may offer information about its business, including information about its business model, management and prospects, and allow qualified investors to request information about the company. In the case when an investor wants to buy shares of a registered company, the investor would receive a stock purchase agreement along with a buyer's investment representation statement and indemnification agreement. Once counter-signed by the seller, the agreements are delivered to an escrow agent to open escrow. The escrow agent holds the buyer's funds until the shares are transferred.

(b) **Listing Requirements for Companies.** The requirements of a company to list on an ATP would vary depending on the types of companies an individual ATP would seek to attract, but basically the objective is to determine if the investment is suitable to anyone, based on the company, its management, and its prospects.

(c) **Qualification Requirements for Investors.** All three of the existing ATPs require investors to be either accredited investors or qualified institutional investors. Accordingly, they were not available for general retail investors.

4. ATP Alternatives for Hawaii.

(a) **HELI as ATP.** The setup and operating costs would need to be incurred by HELI, as well as securities industry compliance of personnel, and enhanced supervision by a broker-dealer.

(b) **Relationship with Existing ATP.** The set-up and operating costs of a Hawaii HELI would be avoided, but the existing ATP would have control over the registration of Hawaii companies. There is no assurance that a Hawaii company would ever be registered.

Mission Markets appears to be the only option for an existing ATP, but an endorsement by the State of a single existing ATP might be questionable.

5. Demand for ATP.

(a) **Local Company Demand.** Local company demand would need to be determined. While Hawaii investors might be interested in investing in developing enterprises in Hawaii, it would require a survey of private company indications of interest for listing on a Hawaii ATP to see if there is sufficient demand from companies to list. This could be accomplished with a public announcement, together with a posted term sheet that would detail requirements for listing. However, the HELI has not been asked to investigate the demand for an exchange or an ATP alternative.

(b) **Local Investor Demand.** Local investment demand would need to be determined, but activity would be limited to companies registered on the Exchange. An investment exchange could be an excellent opportunity for someone in the private sector, as opposed to the State, because it would offer a service that is not now provided for high net worth investors. There would be less of a demand by general retail investors, because they would not have the same benefits of tax harvesting as would high income investors with sizable taxable income.

2. CONCLUSIONS

The IGATP concluded that there is a precedent for an ATP. Among the benefits of an ATP is that qualified investors would have the opportunity to know about companies, their management, and prospects before capital is raised, and companies would have the opportunity to identify interested investors. There are no assurances that an ATP will increase liquidity, unless an active secondary market develops. There are opportunities for tax harvesting. Many of the companies listed on an ATP are unproven enterprises, and it is likely that only a few will succeed. Losses on the unsuccessful ones may be netted against gains from winners. It's difficult to realize losses unless there is a trading market.

The IGATP concluded that there were a number of unknown factors which the work group was unable and determine. Among the unknown factors are:

- Both the cost and demand for an ATP featuring Hawaii securities are undetermined;
- The willingness of a company to list on an ATP;
- The willingness of an ATP to list a company; and
- The interest investors have in trading their investments.

The IGATP found three ATPs operating on the U.S. Mainland. A Hawaii based company can list on one of these ATPs with no cost to the State. However, two of the ATPs had minimum market capitalization requirements for a company of \$100 million. The remaining one had no minimum size requirement. There is no assurance that a U.S. Mainland ATP would find it

beneficial to list a Hawaii company, because due diligence on the Hawaii company would be expensive, and there are other company listing opportunities to choose from that are operating outside of Hawaii.

A home grown ATP potentially could be formed, but its activity would need to be accomplished by using a broker-dealer¹. It may not be appropriate for the State to endorse any one broker-dealer for this purpose, because ATP employees engaged in the securities business would need to be registered representatives of that broker-dealer.

While Hawaii investors might be interested in investing in developing enterprises in Hawaii, it would likely require a survey of private company to indicate the level of interest for listing on a Hawaii ATP and to see if there is sufficient demand from companies to list. This could be accomplished with a public announcement, together with a posted term sheet that would detail and identify the requirements for listing.

The HELI has not been asked to investigate the demand for an exchange or an ATP alternative, but only to address the relevant securities laws and regulations associated with its formation, together with details as to its operation. It is the recommendation of the work group that demand needs to be first addressed before moving forward on the formation of any exchange or ATP.

An investment exchange could be an excellent opportunity for someone in the private sector, as opposed to the State, because it would offer a service that is not now provided for high net worth investors with high taxable income. High net worth investors may increase their exposure to venture capital if there was an active secondary market for these securities. The State, as a regulator, may not be the appropriate agency to determine the feasibility of an investment exchange.

B. THIRD FRONTIER

1. INVESTIGATION

At the Hawaii Stock Exchange meeting held on September 9, 2011, David Watumull of Cardax Pharmaceuticals spoke to the HELI members about exploring a larger framework for economic development in Hawaii. He recommended exploring an effort taken in Ohio that has shown much success in moving Ohio from a rustbelt economy to a technology based economy. At this meeting, it was determined that an investigative group (“IGTF”) would be formed and tasked with exploring Ohio’s model. The IGTF reviewed the Ohio model and had discussions and suggestions from Karl Fooks of the Hawaii Strategic Development Corporation.

The IGTF specifically recognized that there are several key ongoing efforts seeking to promote economic development and diversification in the State of Hawaii that involve the State and County governments as well as the private sector and the University of Hawaii. Currently the various efforts have been largely undertaken without the benefit of the long-term, integrated

¹ A person or firm that is engaged in the business of buying or selling securities on its own behalf or for others. Most broker-dealers must register with the SEC.

and comprehensive mindset embodied in the Ohio model, which the IGTP considered an effective template in this regard.

The ITGP further acknowledged that several investor forums also exist, including business competition and investor conferences sponsored by several educational and venture capital organizations in Hawaii. The IGTP believed that these are extremely valuable initiatives, and believed that a joint approach involving these organizations, especially on a State-wide basis, may help to strengthen the ability of Hawaii-grown start-up companies to find suitable investor financing.

2. CONCLUSION

After further discussion among the entire HELI, the HELI concluded that Ohio's experience offered a valuable model and that several of Ohio's initiatives should be raised in for consideration by the legislature:

- **Long-term integrated economic development program:** The State of Hawaii should consider an overall multi-prong integrated economic strategy that includes raising the level of research and development by attracting world class professors and researchers to our universities, commercial zones to support incubators, establishing a Hawaii State venture capital authority to make investments in start-ups based on merit and financial incentives for local investors and start-ups.
- **Annual Forum:** The creation of a well-capitalized live forum, i.e. an annual investor forum event, where start-up companies have the opportunity to present their ideas and companies to potential investors, participate in networking with other start-ups and investors, engage in educational programming and learn about the programs and support that Hawaii offers to start ups and investors.

III. HAWAII EXCHANGE FOR LOCAL INVESTMENT

A. BRIEF HISTORY OF HONOLULU STOCK EXCHANGE

A local stock exchange is not new to Hawaii. The Honolulu Stock Exchange was formed in 1898, a month after Annexation was approved. In those days before information could be transmitted via telegraph, trades had to be delivered by ship, which took more than a couple of weeks. A cable linking Hawaii with the US Mainland wasn't available until 1901.

Securities traded on the Honolulu Exchange included a number of sugar and other companies previously formed in the Kingdom of Hawaii, or later in the Republic of Hawaii. Among them were Amfac (formerly American Factors with its sugar subsidiaries), C. Brewer and Company, Castle & Cooke with its sugar subsidiaries, Hawaiian Commercial & Sugar Company (now a subsidiary of Alexander & Baldwin), Hawaiian Electric Company, Hawaiian Telephone Company, among others.

The Honolulu Stock Exchange wasn't limited to Hawaiian securities. Also listed were a number of Asian securities, such as Bogo-Medellin Milling Co., Hawaiian-Philippine Company, and San Carlos Milling Co.

The Honolulu Stock Exchange closed its doors in 1978, primarily because of a lack of trading activity. By the time it closed, many of the listed companies traded on the major exchanges or on NASDAQ. Amfac, C. Brewer, Castle & Cooke, Hawaiian Electric, and others traded on multiple exchanges.

There were efforts to resurrect the Honolulu Stock Exchange in the 1980s, with a goal of listing securities of international companies to trade when other exchanges were closed. This effort did not materialize.

B. LEGAL FRAMEWORK FOR HELI

The federal and Hawaii securities laws currently offer issuers of securities with a variety of options in which to offer securities to public and private investors. Both sets of laws permit issuers of securities to register securities for sale to the public and to offer unregistered securities to private investors in non-public offerings. Although the registration of securities allows issuers to sell securities directly to the public, the registration process and periodic reporting requirements necessary to maintain registration are expensive and normally out of the reach of small issuers. On the other hand, the sale of unregistered securities in private sales is less expensive since the securities are not registered and subject to periodic reporting requirements, initial and subsequent sales of unregistered securities are restricted.

1. Federal Securities Laws.

(a) **Registration Requirements.** Generally, offerings of securities must be registered with the Securities and Exchange Commission (the "SEC") unless an exemption is available and can be perfected. The primary federal statute governing the issuance and sale of securities is the Securities Act of 1933 (the "Securities Act"). Specifically, Section 5 of the Securities Act requires that every time a security is sold, the security must either be registered with the SEC or be exempt from such registration. When a security is registered for sale with the SEC, the security is commonly referred to as publicly offered security, and securities that are sold without registration under law exemption from registration are commonly referred to as a privately offered security. If a security is registered, the issuer is subject to the periodic reporting and disclosure requirements of the Securities Exchange Act of 1934 (the "Exchange Act").

(b) **Federal Exemptions from Registration.** In many cases, the costs of registration are prohibitive to small issuers and the initial costs can exceed by amount the small issuer is trying to raise. Fortunately, there are a number of exemptions from registration under the Securities Act.

(i) **Regulation A.** The SEC adopted Regulation A pursuant to Section 3(b) of the Securities Act, which grants an exemption from registration for securities offerings of \$5 million or less in any twelve-month period, including no more than \$1.5 million in resale's by parties other than the issuer. The Regulation A exemption is available to U.S. and Canadian companies that are not: (a) reporting companies under the Exchange Act; (b) investment

companies under the Investment Company Act of 1940; (c) development stage companies; and (d) issuers of fractional undivided interests in oil or gas rights. Regulation A is not available, however, to issuers deemed “unworthy” of the exemption because they have engaged in some activity indicating that potential investors need the protection of a full registration under Section 5 of the Securities Act. To perfect the exemption, the issuer must file an offering statement with the SEC. The offering statement must be “qualified” by the SEC, and the qualification process can take up to 60 days. However, an issuer can obtain indications of interest before filing the offering statement, a practice known as “testing the waters,” and can offer securities after the offering statement is filed, but cannot accept any offers for purchase until the offering statement is qualified. Once the offering statement is qualified, the issuer can sell its securities publicly, up to the Regulation A limits. Regulation A offerings are advantageous because insurers may solicit investors for indications of interest before the offering statement is filed and allows for the general solicitation of investors after the offering statement is qualified. However, the qualification is often characterized as the “mini-registration” exemption since the filing and qualification requirements can be expensive and offerings are limited to \$5 million.

(ii) Rule 147. The SEC adopted Rule 147 pursuant to Section 3(a)(11) of the Securities Act. Rule 147 is known commonly as the intra-state exception and grants an exemption from registration to issuers conducting an intra-state offering. The issuer must be organized and doing business in the state where the securities are offered and sold. General advertising and solicitations of the sale of the securities are permitted only within the state and there is no limit on the amount of securities that may be sold. Resales of the securities are permitted to residents in the state, and resale’s by holders that are not affiliated with the insurer to out-of-state residents are only permitted nine months after the initial offering. The Rule 147 exemption is destroyed at any time offers or sales are made to out-of-state residents. The in-state requirements of Rule 147 severely restrain the type of investors that issuers may sell their securities to and hamper resales of the securities. Therefore, Rule 147 can be of limited benefit to companies seeking to raise capital.

(iii) Regulation D. The SEC adopted Regulation D, pursuant to Section 3(b) of the Securities Act, which offers the best method of raising capital for many small issuers. Regulation D provides for a limited offer and sale of a company’s securities without registration under the Securities Act, and allows for three types of limited offerings. Regulation D is the most frequently used of the exemptions from registration under the Securities Act, since there are no SEC disclosure statement filing requirements and waiting periods, and because under Rule 506 of Regulation D, there is no limits on the amount of money that can be raised.

(1) Rule 504. Under Rule 504, issuers can offer up to \$1 million of securities in a twelve-month period. Rule 504 is not available to companies subject to the reporting requirements of the Exchange Act, investment companies or blank check companies. Although Rule 504 is permitted issuers to use general advertising to solicit the securities if certain state registration requirements were met in the past, Rule 504 offerings are now subject to the general advertising and solicitation prohibitions applicable to other Regulation D offerings. Under Rule 504, there is no limit on the number of investors, and there are no sophistication or experience qualifications placed on investors. In addition, issuers offering securities under Rule 504 are not obligated to provide investors with disclosure materials regarding the offering. However, issuers typically do provide disclosure materials to avoid

liability under the anti-fraud provision of the Securities Act. However, due to the \$1 million ceiling on the amount of capital that can be raised under Rule 504, issuers do not use Rule 504 as frequently as other types of Regulation D offerings.

(2) Rule 505. Under Rule 505, issuers can offer up to \$5 million of securities over a twelve-month period. Rule 505 is not available to investment companies or companies disqualified under Regulation A. Rule 505 does not permit an issuer to use general advertising to solicit securities. Rule 505 is available to an unlimited number of accredited investors and up to 35 non-accredited investors. Non-accredited investors must receive a substantive disclosure document that includes financial statements. Since the Rule 505 exemption imposes a \$5 million limit on the amount of capital that can be raised, limits the manner of offering and limits the number of non-accredited investors that may purchase securities, issuers often do not choose Rule 505 for their private offerings.

(3) Rule 506. Rule 506 contains no limit on the amount of capital that can be raised in an offering. In addition, there are no restrictions on the types of issuers that can use Rule 506. An issuer using Rule 506 cannot engage in general advertising to solicit the sale of its securities. Rule 506 is available to an unlimited number of accredited investors and up to 35 non-accredited investors. Unlike Rule 505, all non-accredited investors, either alone or with a purchaser representative, must have sufficient knowledge and experience in financial and business matters to make them capable of evaluating the merits and risks of the prospective investment. Non-accredited investors must receive a substantive disclosure document that includes financial statements. Because Rule 506 contains no limitation on the amount of funds that can be raised, it is the exemption from registration most frequently used by companies seeking to raise capital.

(iv) Section 4(5). Section 4(5) of the Securities Act, which until recently was Section 4(6) of the Securities Act, allows offerings of securities exclusively to accredited investors up to a maximum amount of \$5 million. Under Section 4(5), an issuer cannot engage in general advertising or general solicitation to market its securities. Section 4(5) is rarely relied upon by issuers because of the parallels between it and Rules 505 and 506, which contemplates the offering of securities to non-accredited investors as well.

2. Hawaii Securities Laws.

(a) Registration Requirements. Like its federal counterparts, Hawaii Revised Statutes (“HRS”) Chapter 485A generally prohibits the offer or sale of a security in Hawaii when the security is registered or is exempt from registration. The registration requirements of securities laws under Hawaii law are similar to the requirements under the Securities Act.

(b) Hawaii Exemptions from Registration. Under HRS, Chapter 485A and Hawaii Administrative Rules (“HAR”), Title 16, Chapter 39 (“HAR Title 16”), the offer or sale of securities offered or sold in compliance with Regulation D and in compliance with HAR Title 16 are exempt from registration. However, HAR Title 16 does not provide an exemption from registration for Rule 504 securities. Likewise, any person who is disqualified by the SEC from

perfecting an exemption from registration under Regulation D is also disqualified from exemption from Hawaii registration under HAR Title 16.

3. Hawaii Securities Commissioner. The Securities Division is responsible for the registration of securities and the licensing of all broker-dealers and their sales persons, investment advisers and their representatives doing business in Hawaii.

4. Need for Legislation. Broker-dealers who may currently invest in the regulatory scheme of the State and Federal laws.

C. LEGAL AND REGULATORY REQUIREMENTS FOR HELI

In order for the HELI to operate as a stock exchange, the HELI will need to address certain business entity and regulatory issues. As a business, the HELI will need to be incorporated or registered as a business entity and will need to meet certain business registration and organizational requirements. As an “exchange”, the HELI is subject to the federal and Hawaii broker-dealer requirements.

1. Business Registration and Organizational Requirements. In order to operate as an ongoing business in Hawaii, the HELI will need to be incorporated as a corporation or registered as another legal entity, such as a limited liability company.

2. SCR No. 134 SD1, suggested that the HELI would be a non-profit corporation, however, the non-profit corporation option has several limitations. The primary limitation is that a non-profit corporation cannot issue stock, and the HELI, as a non-profit, would need to rely on member dues, charitable contributions or other non-stock sources of capital to operate, such as funding from the State of Hawaii. As a business entity, the HELI will need to have a board of directors or managers that will govern the HELI. Therefore, the HELI, the incorporators or organizers of the HELI, will need to recruit a board of directors and recruit and employ a competent staff to operate the HELI and find capital for the start-up costs.

3. Broker-Dealer Requirements. If the HELI acts as a securities exchange, it will be affecting transactions in the sale and purchase of securities, and therefore, will be subject to the federal and Hawaii securities laws.

Under the Exchange Act, an “exchange” is defined as an organization, association or group of people that organize, maintain or provide a market place or facilities to bring together purchasers and sellers of securities or otherwise perform the function commonly performed by a stock exchange. Generally, the federal and Hawaii securities laws impose significant requirements on persons who operate an exchange and act as a broker or dealer in securities. Specifically, the Exchange Act provides that no person may affect transactions in or under the purchase and sale of any security unless the person is registered with the SEC as a broker or dealer. Chapter 485A, HRS and Title 16, HAR, contain similar requirements for persons acting as a broker or dealer in Hawaii. In order to register as a broker-dealer, the HELI will need to meet all of the SEC and State of Hawaii requirements for broker-dealers, including but not limited to maintaining adequate capital. In addition, employers of the HELI will generally need to be registered as brokers dealers as well.

IV. CONCLUSION

The HELI believes there are indicators that there is a need for an investment exchange. The entity would not be a State sponsored solution, as the State's securities commissioner would necessarily regulate the entity. The HELI believes more investigation regarding whether there is demand for this type of local investment and what the focus of the local investment entity would be and what type of local investments would generate the greatest equity investment for start-up companies or existing companies.

The current regulatory scheme is sufficient to allow broker-dealers to engage in Alternative Trading Platform transactions.

The long view of the HELI believes that a coordinated effort on the part of the State to determine what type of industry the state wants to focus its energy and resources on, what type of jobs would be needed and thus what type of educational opportunities would the State or private industry need to provide, how the State can market this coordinated effort to attract research and development companies and whether the state should provide tax credits or other financial incentives are questions should be answered. This coordinated approach was conducted by the Ohio Third Frontier to bring in the financial and education resources to make the coordinated effort a success.

The HELI does not suggest or recommend either of these alternatives, but to engage in further discussion should the State want to pursue either of the alternatives.