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Wisconsin Venture Center (Commerce -- Economic Development)

Base Agency

[LFB 2007-09 Budget Summary: Page 86, #3]

CURRENT LAW

The high-technology business development corporation program was created by 1999 Wisconsin Act 106. Commerce is required to organize and assist in maintaining a high-technology business development corporation as a nonstock, nonprofit corporation under Wisconsin law for the exclusive purpose of promoting and supporting the creation, development, and retention of science-based and technology-based businesses in the state.

In November, 2000, the Governor first appointed members to the Wisconsin Technology and Entrepreneur's Council which was created to promote development of science- and technology-based businesses in Wisconsin. The Council was formed as a nonprofit corporation and the Council's board of directors approved the formation of the non-profit Wisconsin Technology Council in January, 2001. Commerce awarded the Council a grant of $50,000 to fund start-up and administrative costs. The Wisconsin Technology Council is an independent, nonprofit, tax-exempt corporation which serves as the leading policy adviser and catalyst for creation, development, and retention of science- and technology-based businesses in Wisconsin.

Commerce is authorized to make grants to the high technology business development corporation following specified criteria. Annual base level funding of $250,000 GPR is provided for these grants.

GOVERNOR

Require Commerce to organize and assist in maintaining an emerging industries development corporation as a nonstock, nonprofit corporation under state law for the purpose of facilitating raising capital to promote and support emerging industries in Wisconsin. The emerging industries development corporation would be governed by a board of directors. Commerce would be provided $1.0 million GPR annually for grants to the emerging industries development corporation. The Department would be required to make a one-time grant of $700,000 in 2007-08 to the emerging industries development corporation and no matching funds would be required if the corporation used the grant for start-up capital and reasonable administrative expenses. Beginning in 2008-09, the Department would be required to make an annual grant of $500,000 to the corporation, and no matching funds would be required if the grants were used for operating expenses.

DISCUSSION POINTS

1. Under the bill, the emerging industries development corporation would be required to do all of the following:

a. Establish and implement programs to prepare entrepreneurs of emerging industries for angel and venture capital investments.

b. Strategically match entrepreneurs of emerging industries with sources of capital or management expertise or both.

c. Work with technology transfer offices of universities and colleges to facilitate a match between entrepreneurs of emerging industries and sources of capital or management expertise or both.

d. Provide research and analysis services regarding emerging industries in Wisconsin to prospective angel investors and venture capitalists.

e. Provide a venue for bringing together prospective angel investors and venture capitalists with entrepreneurs of emerging industries.

2. The corporation's board of directors would include the Secretary of Commerce or designee, and the Secretary of the Department of Financial Institutions (DFI) or designee. In addition there would be up to 12 members, one or more of whom represented each of the following categories: (a) entrepreneurs in Wisconsin; (b) high-technology businesses in Wisconsin; (c) research institutions in Wisconsin; (d) the state's venture capital industry; (e) the state's investment banking industry; (f) the state's business development community; and (g) professionals in Wisconsin who are experienced in providing services to these individuals. Initially, the Governor would appoint these board members for five-year terms. The emerging industries development corporation would be required to specify a method for replacing these appointees in its bylaws.

3. The assets transferred to, and assets and liabilities of, the emerging industries development corporation would be separate from all other assets and liabilities of the state, of all political subdivisions of the state, and of the Department. Neither the state, any political subdivision of the state, nor the Department would guarantee any obligation of, or would have any obligation to the emerging industries development corporation. Neither the state, any political subdivision of the state, nor the Department would be liable for any debt or liability of the emerging industries development corporation.

4. SB 40 would create a venture capital grant program and provide $1.0 million GPR annually for grants to the emerging industries development corporation. Commerce could make a grant to the emerging industries development corporation if all of the following applied:

a. The corporation submits an expenditure plan to the Department detailing the proposed uses of the grant proceeds and the Secretary of Commerce approved the plan.

b. The corporation enters into a written agreement with the Department that specifies the conditions for the use of the grant proceeds, including reporting and auditing requirements.

c. The corporation provides matching funds equal to 50% of the grant proceeds (or one-third of project costs, except no match would be required for operating costs of up to $500,000 annually beginning in 2008-09).

d. The corporation provides information requested by the Department about private funding the corporation has received or will receive for the purposes detailed in the expenditure plan.

e. The corporation agrees in writing to submit to the Department, within six months after spending the full amount of the grant, a report detailing how the grant proceeds were used.

The bill would specifically require Commerce to make a one-time grant of $700,000 in 2007-08 to the emerging industries development corporation, and no matching funds would be required if the corporation used the grant for start-up capital and reasonable administrative expenses. Beginning in 2008-09, the Department would be required to make an annual grant of $500,000 to the corporation, and no matching funds would be required if the grants were used for operating expenses.

5. Recent economic studies have identified certain linkages between entrepreneurship and economic growth. Entrepreneurial enterprises are viewed as significant factors for increasing, employment and productivity. Entrepreneurs are often distinguished from small business owners who organize, operate, and assume risk for a business venture. Growth rates and desired outcomes most often distinguish entrepreneurial ventures from other small businesses. Typically, entrepreneurial companies target annual growth rates of 15% to 20% in either revenues, employment, or both. Entrepreneurs also usually intend to build businesses that provide an innovative product or service.

One econometric study using a Census Bureau database (Acs, Armington, 2004) found that higher rates of entrepreneurial activity were strongly associated with faster growth of local economies. New organizations were able to take advantage of information useful to business produced through economic activity in the area (knowledge externalities). Higher levels of employment growth rates were also strongly positively associated with such entrepreneurial activities. The authors found that, for 1995-96, establishments that were less than two years old accounted for all net national job growth. However, establishments that were at least 10 years old accounted for 60% of total employment and offered jobs with good prospects for continued employment.

Another area of research views entrepreneurship as a critical spur for commercial introduction of new goods and services, and the opening of new markets to innovations. Researchers focus on the role of economic experiments in economic growth (Rosenberg, 1994). Entrepreneurs engage in activities referred to as "extreme experiments," since start-up companies are not constrained by the limits of old technologies, traditional methods of organizing production, or the need to serve established markets. Entrepreneurs can be more aggressive in pursuing radical approaches to the creation of economic value. In addition, unlike purely scientific experiments, economic experiments compete with other economic experiments. As a result, the value of start-up activity is not limited to the value created by new businesses, but also includes benefits from increased competitive pressure on established firms. Entrepreneurship also contributes to the range and diversity of economically useful knowledge. Collectively, entrepreneurs are often able to pursue a more diverse and idiosyncratic range of technical experimentation approaches to a potential technology, which increases the possibility of achieving a technological breakthrough (Fleming 2001, Fleming and Sorenson 2003). The value from new technologies relies on the ability to apply that new technology to new markets in new ways and market experimentation can significantly enhance the range of potential market applications (Shane, 2000). Entrepreneurs undertake organizational experiments to develop an organization to best take advantage of specific technical and market opportunities.

A 2007 report prepared by Global Insight for the National Venture Capital Association *(Venture Impact: The Economic Importance f Venture Capital Backed Companies to the U.S. Economy, Third Edition),* using a database of nearly 23,500 venture backed companies, found that such companies employed just over 10 million American workers in high-quality jobs and generated $2.1 trillion in revenue in 2005. The total revenue of venture capital financed companies comprised 16.6% of U. S. gross domestic product, while total employment of such firms represented 9.0% of U.S. private sector employment in 2005. Venture backed companies outperformed non-venture backed businesses in both job creation and revenue growth. Employment in venture backed companies increased 4.1% between 2003 and 2005, while national employment grew 1.3% during the same period. Similarly, venture backed company sales between 2003 and 2005, grew by more than 11.0%, compared to an overall increase in U. S. company sales of 8.5%.

6. As a new business venture progresses from the initial idea and business plan until it reaches maturity through an initial public offering (IPO), acquisition, or buyout, it also moves

through funding stages. Each of these stages involves certain potential sources of capital for the business that can differ from stage to stage. The exact number of financing stages can vary from venture to venture. Some firms will have no more than two stages of financing after the seed stage, while others might require a series of financing stages during expansion. Also, the specific number of stages described varies among financial practitioners. The typical financing stages for new business venture financing and the sources of funds at each stage include the following:

Seed/Concept. The venture is in the process of examining idea feasibility and its product or service is not fully developed. Funds are used for product and/or service development (including prototype development), patent filings, market surveys and research, incorporation, management recruitment, legal structuring for investment, and development of a business plan if product or service development is successful. Sources of capital for the venture include the entrepreneur's personal savings and earnings, credit cards, and monies from friends and relatives. New ventures might qualify for U.S. Small Business Innovation Research (SBIR) program funding. Phase I awards provide funding to support exploration of the technical merit or feasibility of an idea or technology. Phase II provides funds for research and development (R&D) and evaluation of commercialization potential. In some cases, angel investors provide seed financing.

Start-Up. Product or service development could be complete, in testing, or a pilot project. At least one principal is working full-time, market studies are complete, and a business plan is complete. The venture may be in business and generating some revenues. Key management is being assembled or is in place. Generally, this is the stage at which outside funding sources are sought. A primary source of capital at this stage would be angel investors or angel networks that provide financing from their own funds. Banks might provide financing if the entrepreneur has a solid credit history, venture-related experience, and can offer collateral, such as a house. Early stage venture capitalists may provide funding in some cases.

First-Stage. The firm has begun production or is providing a service. Management and employees are on the job, and the company is making some sales. Further funding is needed to increase productions or services, increase productivity, and build the sales organization and distribution system. Angel investors and networks continue to be a source of capital. This is also the stage where venture capital investors like to begin financing.

Second Stage. The company is producing and shipping products, or providing services to customers. A significant amount of revenues are developing, and accounts receivable and inventory are accumulating. However, the company may not yet be profitable. Second level management is being identified and hired. Financing at this stage is working capital for further expansion, and for increasing marketing, accounts receivable and inventory. Angel investors may still provide some funding. If monthly cash flow is at a break-even point, banks may provide a line of credit. Venture capital firms specializing in later stage funding provide financing.

Third Stage. At this stage the company is typically looking for a major expansion of operations. Sales are increasing and second level managers are in place. Internal funds, including

profits and lines of credit, are insufficient to support plant expansion, product improvement, marketing, and other assets and the internal capabilities necessary for stronger sales. Because of the ability to raise substantial amounts of capital, venture capital funds are a primary source of capital at this level of development. Corporate venture investments can also be a source of financing at this stage.

Bridge/Mezzanine. Mezzanine financing is typically a hybrid of debt and equity financing that is use to provide funds for expansion of an existing company. Bridge financing is interim financing used to meet short-term cash flow needs until more permanent financing (usually larger amounts) is secured. Mezzanine or bridge financing is a short term form of providing funds used to prepare a company for going public through an initial public offering (IPO), or for a leveraged buyout or acquisition. The funds are used to remove accumulated debt from the firm's balance sheet, buy out early investors and founders if necessary, and to pay other costs related to the public offering of stock, buyout, or acquisition of the company. This funding may come from a venture capital firm or bridge financing specialist, who are usually paid from the proceeds of the IPO, acquisition, or buyout.

IPO/Acquisition/Buyout. Traditionally, entrepreneurs and investors, cashed out their interests in the firm through an initial public offering of stock in the company. However, acquisitions by other firms and management buyouts of the firm are becoming more common ways of realizing the returns from investing in the company.

7. Angel investors are typically high net worth individuals and/or entrepreneurs who have "cashed-out" of a business, who have capital and business experience and are interested in investing in potentially high-growth business ventures. A common definition of an angel investor is an individual with $200,000 in income for the past two years or with a net worth of over $1.0 million. Most angel investors are experienced businesspersons or successful entrepreneurs who invest in the seed and start-up entrepreneurial ventures as a part-time avocation. Often they invest in the industry in which they gained wealth or have experience. Angel investors provide funds for proof of concept, product development, market research, business plan development, recruiting management, early stage production, and expansion. Generally, a number of individual angels will fund a round of investment in new ventures, with certain angels working with the company for several years as mentors, coaches, and directors. If the business flounders, angels may become full-time executives.

Individual angels typically invest $5,000 to $100,000 in a venture, and require a share of ownership or control. Angel investors seek to fund business ventures with the potential for rapid growth, and expect a rate of return on the investment of 30% to 40%, within three to five years. Because this type of investing is high-risk, some angels invest in eight to 10 companies at a time, allocating between 10% to 15% of their total investment funds to seed, start-up and early stage entrepreneurial ventures. Since the late 1990's, angels have been forming groups or networks to pool resources and expertise, generate deal flow, and create a formal screening process to identify promising investment opportunities. In general, before investing funds in an entrepreneurial venture, angels evaluate the quality of management, soundness of the financial structure, the uniqueness of

the product or service, the size of the product/service market and potential customer base, the level of investment by the entrepreneur, family and friends, and the venture's potential for growth.

Angel investors are not venture capitalists. Angels invest their own personal funds, invest in start-up and early stage businesses, and usually invest no more than $100,000 in a single venture. Venture capitalists may invest some money, but raise most investment funding from institutional and other sources, prefer later stage companies, and invest up to $2.0 million in a single company. Angel investors are the largest private source of capital for earl-stage entrepreneurs, and are the most likely source of seed and start-up capital, after the resources of friends, family and the entrepreneur are exhausted. According to the Angel Capital Education Foundation, approximately 90% of outside equity capital in seed and start-up companies comes from angel investors. The University of New Hampshire center for Venture Research estimates that the total amount of angel investment in the U.S. in 2006, was about $25.6 billion in approximately 51,000 firms. The Center estimated that 234,000 individuals were actively investing as angels, with an average of four to five investors providing funds to each entrepreneurial start-up. Forty-six percent of angel investments were in the seed or start-up stage, while 40% were in post seed/start-up investments The acceptance rate for deals (the percent of total deals identified for angels that resulted in investment) was 20.1%. The National Association of Seed and Venture Funds estimated that between 140 and 200 angel groups were operating in the U. S. A 2006 study of risk capital in Wisconsin (*Risk Capital in Wisconsin: A Progress Report, 2006*), estimated that angel investment activity in 2005 exceeded $50 million.

8. Venture capitalists are professional investors who specialize in funding and building young innovative enterprises with a high potential for growth. There are several types of venture capital firms, but most firms invest their capital through funds organized as limited partnerships in which the venture capital firm or fund manager serves as the general partner, and the investors in the fund serve as limited partners. Venture capital firms are also organized as closely held corporations, and limited liability companies [LLCs] or limited liability partnerships [LLPs], but a partnership is the predominant form of organization. Venture capital firms typically raise capital for their funds from institutional investors, such as public and private pension funds, insurance companies, banks, endowments, foundations, wealthy individuals, and other entities. The partnership is organized as a pooled fund, comprised of the general partner and investors (limited partners), that is capitalized by commitments of funding from the limited partners. Once the fund has reached its target size, the partnership is closed to further investment, so that the fund has a fixed capital pool from which to make its investments. Similar to a mutual fund company, a venture capital firm may have more than one fund in existence.

Each venture capital fund has its own investment strategy, generally focusing on various industry sectors, geographic locations, or stages of a company's life. Venture capital firms also vary in size, from seed specialist firms with less than $2.0 million under management to funds with over $1.0 billion with worldwide investments. According to data from Dow Jones VentureOne, the average venture capital fund size in the U. S. in 2006 was slightly over $200 million. About 16% of the venture capital funds raised in 2006 were $500 million or greater, while 34% of the funds raised were smaller than $100 million.

When a venture capital firm makes an investment in an enterprise it is an equity investment in that company. The initial investment usually is the beginning of a continuing relationship between the venture capitalist and the businesses enterprise. Funds are reserved for future rounds of financing to pay for expansion of the business enterprise, and each successive round involves equity investment in the enterprise. Venture capital investments can range from $250,000 to millions of dollars. Typically, investments exceed $1.0 million. VentureOne data indicate that, in 2006, the median amount of funding for all investment rounds was $7.0 million. Venture capitalists actively work with the company's management, and assist in building management teams, providing management and other business expertise, and linking the business with industry and financial networks. Since the stock of the business is essentially illiquid and worth little, similar to an angel investor, the venture capitalist expects to make a return on the investment when the business matures and issues an IPO or is bought or acquired. Generally, the venture capitalist plans for a return on investment of about 25% to 50% in five to seven years, because the investment is risky and funds are committed for a relatively long period. In addition, venture capital firms mitigate some of the risk by investing fund capital in a number of companies. Investments with substantial returns on investment offset those with average or no returns. Venture capital firms also co-invest with other professional funds.

9. For every 100 funding proposals submitted to a venture capital firm, usually about 10 are investigated. The remainder are rejected quickly because they do not meet established geographical, technical, or market policies of the firm, or because they are poorly prepared. After the initial screening, the venture capitalist conducts a detailed analysis on the remaining 10 proposals. The venture capital firm assesses the management team, the concept, the marketplace, the project's fit to the fund's objectives, production costs, the capital required to build a successful business, and the value-added potential for the firm. The management team of the business should have expertise in the fundamentals of the business, financial expertise, and sales ability. The product or service should be differentiated, innovative, demonstrably better than others in the marketplace, and be patentable. The expected rate of return depends upon the stage of business development, with a higher rate expected for earlier stages, and can range from 25% to 50%. The venture capitalist will also want an equity interest in the company for each round of funding. Generally, venture capital firms perform due diligence, which can include formal market studies, reference checks, consultation with third parties, such as customers, review of legal issues such as contracts and intellectual property rights.

The investment process leads venture capitalists to operate in areas where there are a substantial and continuous number of entrepreneurial ventures in which to invest. A certain level of firms requiring venture capital and that qualify for venture capital investments is necessary. Because venture capital investing often requires frequent contact with investment enterprises, the venture capitalist prefers to invest in firms located where travel is easy and quick. In order to complete a deal and support a business, an infrastructure of attorneys, consultants, accountants, and bankers is necessary. The time, and often the cost, of evaluating enterprises for investment does not vary much by the size of the investment, and in recent years, venture capitalists have made larger investments in later stage firms. This provides an opportunity for greater returns on those investments.

10. Nationally, institutional venture capital is concentrated both geographically and by stage of development. Table 1, which is based on data from the PriceWaterhouseCoopers/National Venture Capital Association, MoneyTree Report for 2006 (data from Thomson Financial) shows total U. S. venture capital investments by stage of development. In 2006, venture capitalists invested $25.5 billion in 3,416 deals. Of the total, 19.6% of the investments funded seed and early stage companies, 43.9% of the investments funded expansion stage companies, and 36.5% of the deals funded later stage companies. Of the total amount of venture investments, 65.6% funded later and expansion stage companies, 25.3% funded early stage firms and 9.1% funded seed or startup enterprises. Data from the Dow Jones VetnureOne venture capital report indicate that, in 2006, $25.75 billion was invested in 2,454 companies. (The figures differ because not all venture capitalists report deals, and the two organizations use different criteria in compiling databases.) VentureOne data show a similar distribution of investment, with around 48% of the $25.75 million in total venture capital investments, going to later stage firms. However, the number of deals were more balanced, with about 36% of the 2,454 total deals being with early stage firms and a similar percentage with later stage firms.

TABLE 1

Moneytree 2006 Venture Capital Report

Developmental Stage	Investments*	Percent of Total	Deals	Percent of Total
Expansion	$11,208	43.94%	1,283	37.56%
Later	9,313	36.51	957	28.02
Early	3,825	15.00	864	25.29
Startup/Seed	1,159	4.54	312	9.13
Total	$25,505	100.00%	3,416	100.00%

*Millions of dollars.
Source: PriceWaterhouseCoopers/National Venture Capital Asscn./Thomson Financial, MoneyTree Report, 2006

Table 2, from the MoneyTree survey, shows the total amount of venture capital investments and number of deals for the top ten states in 2006. Table 2 shows that national venture capital investing is centered on the two coasts, particularly in California and the Northeast. California accounted for 48% of total venture capital investments and over 42% of deals in 2006. Massachusetts and New York ranked in the top four states in terms of investments and deals. The top ten states had over 86% of venture capital investments and about 81% of venture capital deals. The VentureOne data for 2006 for individual states is similar with California showing 48% of total venture capital investments and 44% of the deals. Massachusetts and New York were also leading states in terms of venture capital investments and deals.

TABLE 2

State	Investments*	Percent of Total	Deals	Percent of Total
California	$12,242	48.00%	1,445	42.30%
Massachusetts	2,819	11.05	368	10.77
Texas	1,385	5.43	176	5.15
New York	1,259	4.94	190	5.56
Washington	1,012	3.97	135	3.95
Pennsylvania	778	3.05	102	2.99
New Jersey	771	3.02	84	2.46
Maryland	636	2.49	108	3.16
Colorado	622	2.44	92	2.69
North Carolina	472	1.85	65	1.90
Other	3,508	13.75	651	19.06
Total	$25,504	100.00%	3,416	100.00%

*Millions of dollars.
Source: PriceWaterhouseCoopers/National Venture Capital Asscn./Thomson Financial, MoneyTree Report, 2006

Data from VentureOne indicate that there were 12 venture capital deals in Wisconsin in 2006, with total venture capital investment of $58.47 million. MoneyTree reported total Wisconsin venture capital investments of $60.3 million. These amounts were less than 3% of total national venture capital investments for 2006. The NorthStar Economics, Inc. report on risk capital in Wisconsin found that, in 2005, $69 million in venture capital was invested in 12 deals. The NorthStar report is based on information from both the MoneyTree and VentureOne reports.

11. Conventional financial theory asserts that in perfect financial markets the return required for investment in a project by a rational investor is influenced by the return on investment and the risk of the project. Typically, the investor will allocate funds to the projects with the highest relative present value or internal rate of return based on an evaluation of each project. In a truly competitive capital market in an economic sense, investment funds would be allocated to entrepreneurial businesses through the normal functioning of the markets.

However, the market for venture capital investments is not perfect in allocating investments: (a) not all investors have the same information at the same time; (b) most investments are illiquid and cannot be sold easily at any point in time; (c) high information and transaction costs require large investments and subsequent gains, restraining the ability to diversify; and (d) venture capital investments are more risky than investments in established businesses. The majority of entrepreneurial ventures are seeking funds for activities that aren't yet proven, in markets that may not exist, with products and services that haven't been produced, with financial plans that may not be comprehensive. The transaction costs associated with finding the right deal, assessing its value, negotiating it, and ensuring that the venture matures according to plan are significant.

In many cases, venture capitalists mitigate the uncertainties of the investment process by

participating in networks that include other venture capitalists, former entrepreneurs, industry experts, financial institutions, and business executives with whom there is mutual trust. The relationships with others familiar with venture capital investing provide the venture capitalist with sources of expertise in identifying good ideas, deal making, financing, industry characteristics, management and other factors relevant to successful ventures. These type of networks are characteristic of areas, such as Los Angeles/Orange County and San Francisco Bay, where the venture capital industry is well developed.

12. The Wisconsin Venture Center (WVC) is intended to be a public and private sector partnership that would act to increase capital investments in and provide management assistance to entrepreneurial ventures in targeted industries that have been identified as integral to increasing economic growth in Wisconsin. The targeted industries include biotechnology, bioindustry and clean technology, nanotechnology, and information technology and business services. A substantial number of potential entrepreneurial ideas are generated through the research and technological advances developed by state institutions and organizations, such as the University of Wisconsin, WARF and WiSys, Marshfield Clinic, and the Medical College of Wisconsin. However, many out-of-state venture capital investment firms are not aware of entrepreneurial ventures that have resulted from this activity and that offer an investment opportunity. Conversely, some entrepreneurs have difficulty in attracting sufficient venture capital investment to expand operations for promising technologies, products or services. The national data show that less than 1% of venture capital investments are made in Wisconsin enterprises.

The WVC would provide services to both entrepreneurs and venture capitalists that would be designed to raise the level of venture capital investment, particularly by out-of-state firms, in Wisconsin entrepreneurial ventures. WVC would connect Wisconsin entrepreneurs with sources of venture capital needed to expand their business. The Council would also provide enterprises with access to management talent and with management and financial assistance that is required in order to attract venture capital investments.

WVC would be a point of contact for out-of-state investors seeking deals in Wisconsin. WVC staff would understand the venture capital firm's investment criteria and introduce them to companies that met their objectives. The Center would provide office space for out-of-state venture capital firms that were interested in investigating investment opportunities in Wisconsin. In addition, the Council would connect the out-of-state firms with in state venture capitalists, financial institutions, business service providers, and businesses to help develop an in-state venture capital network and sufficient deal flow to attract more firms to Wisconsin. WVC staff would be experienced entrepreneurs, venture capitalists, financiers, or business persons with expertise and contacts in national venture capital markets. Staff would travel to states where networks of venture capitalists were operating in order to promote Wisconsin as a place to invest, and to develop contacts in the industry.

The WVC would complement the activities of the Wisconsin Angel Network, Wisconsin Innovation Network of the Wisconsin Technology Council, and the Wisconsin Entrepreneurs Network. WVC staff would view these organizations as focusing primarily on assisting

entrepreneurs during the concept, seed, start-up and early stages of a businesses development. WVC assistance would focus on financial assistance during the business expansion and maturation stages. Moreover, WVC activities would increase the amount of capital in Wisconsin that would be available for all stages of an entrepreneurial venture's life. The Council would be organized as separate non-profit organization, with a specialized Board of Directors. It is believed that this would allow staff to focus on developing the venture capital industry in Wisconsin.

13. Annual funding of $1.0 million would be provided including $700,000 in 2007-08 to fund administrative start-up and administrative costs, with no matching funds required. A grant of $500,000 in 2008-09 would be provided for operating expenses, and again no matching funding is required. Commerce could make grants of an additional $300,000 in 2007-08, and $500,000 in 2008-09, but the WVC would have to provide matching funds. The funds would be used to pay staff salaries, overhead and administrative expenses, and marketing costs. Technical and marketing staff salaries are expected to be relative high in order to attract competent individuals who have experience and expertise in the venture capital and related industries. In one model proposed by the administration, WVC would have six to eight positions and a total annual budget of $1.6 million, of which $1.1 million would be operating expenses.

14. The proposed WVC is modeled after BioEnterprise in Cleveland, Ohio. BioEnterprise is a business formation, recruitment, and acceleration initiative designed to stimulate the growth of health care companies and commercialize bioscience technologies. Based in Cleveland, BioEnterprise is a partnership of The Cleveland Clinic, University Hospitals, Case Western Reserve University, and Summa Health System. The initiative includes the collective activities of the following partner commercialization offices: (a) the Case Office of Technology Transfer; (b) Cleveland Clinic Innovations; (c) University Hospitals Case Medical Center -- Center for Clinical Research; and (d) Summa Enterprise Group. Companies that are served include firms producing or providing emerging medical devices, biotechnology, and health services. Each year the BioEnterprise groups choose a select number of such companies on which to focus. The resources and networks of the initiative are directed to assist those companies achieve greater levels of business success.

BioEnterprise provides the following services to support the development and growth of client health care businesses:

Management Support. BioEnterprise provides health care enterprises with a wide range of executive-level management advice and support on issues of strategy and marketing positioning, product development, operations, strategic alliances, financing, and organizational development. BioEnterprise has also developed an extensive network of management and technical executives that are interested in working with start-up heath care companies.

Clinical Collaborations. The initiative has established close working relationships with many world-class clinical and research institutions in Northeast Ohio. Initiative partners (Cleveland Clinic, University Hospital Health systems, Case Western Reserve University, and Summa Health system) work closely with biotechnology, medical device, and health care service

company start-ups. BioEnterprise assists these companies in gaining access with partner institutions, and facilitating clinical validation and development collaborations for their products or services.

Investment Capital, Start-Up Funding. BioEnterprise provides support for companies seeking investment capital and other start-up funding by developing and maintaining relationships with health care venture capital firms, private equity groups, and investment banks throughout the U. S., and by working with several Ohio seed funding sources. BioEnterprise offers services that assist companies in preparing for and obtaining capital. The initiative also identifies opportunities for obtaining grants to fund product and clinical development.

Business Development. BioEnterprise helped form a network of industry contacts and experienced businesses development individuals and other entities which are linked companies to explore and enter strategic relationships. The network includes successful medical device, pharmaceutical, and health services companies, and strategic advisory firms.

Resource Network. BioEnterprise has developed a network of consultants and services that support the growth of health care companies. The network can provide technical equipment and services, research services, and incubation space (including the BioEnterprise facility). The consultants have expertise in all aspects of commercializing health care technology, encompassing basic market research, product and regulatory development, clinical support, and marketing and sales support. In addition, BioEnterprise has established a set of preferred relationships with professional service firms for business law and intellectual property, accounting and business administration, and regulatory services.

BioEnterprise also publishes resources that can assist entrepreneurs in starting and expanding bioscience businesses, such as the Entrepreneur's Guide for bioscience companies, a Bioscience Consultant's Directory listing experts in related fields, and various reports on health care venture investment and start-up activity, and health care industry information for the Cleveland region and the Midwest. The initiative also supports conferences and seminars for entrepreneurs, venture investors, and industry officials and experts.

Bioenterprise started with a $1.0 million grant from the state of Ohio for operations, and an $8.5 million grant for capital renovations of the building in which it is located. The organization has a staff of 15 full-time employees and an annual budget of $3.4 million. Bioenterprise receives an annual grant of $230,000 from the state and $1.3 million from a regional foundation. Staff is experienced in the venture capital industry and is paid relatively more than most public employees.

15. In neighboring states, the Venture Michigan Fund Invests in venture capital firms which target seed and early-stage investments. Moneys for the $95 million fund are provided by private investors who receive state single business tax credits for investing in the fund. The 21st Century Investment fund has $109 million in state funds that are invested in private equity, mezzanine and venture capital firms located in Michigan for investment in specified technologies.

Michigan provided funds for the Michigan Venture Capital Association, which advocates for the private equity/venture capital industry.

Iowa created the Entrepreneurial Ventures Assistance (EVA) program that provides financial and technical assistance to start-up and early-stage companies, and existing companies that are developing a new product or technology, Up to $250,000 can be awarded for working capital, purchasing equipment and machinery, software, or other approved expenses. Up to $25,000 can be awarded for technical assistance. Iowa has also established business accelerators in various locations. Staff include experienced professionals that assist new businesses in venture funding and business growth activities.

Illinois administers the Illinois Entrepreneurship Network that connects entrepreneurs with different service providers through various state centers. Technical, financial, and marketing assistance and training are provided through small business development centers, technology enterprise centers, procurement technical assistance centers, international trade centers, manufacturing extension centers, and small business environmental protection centers. In addition, the state recently created entrepreneurship centers, which are 13 regional offices that assist high growth potential businesses in connecting with financial and other resources, help with product development and obtaining patents, and provide customized marketing strategies.

Minnesota provides access to the BizPathways network which provides financing information to entrepreneurs and links them with resource providers. The network was developed by Minnesota Rural Partners and financed by a grant from the U. S. Department of Commerce, and offers on-line assessments, financial, marketing, and technology planning tools. Minnesota state and local governments also offer the Bioscience Zone program which provides tax state and local tax exemptions and credits, and loans, grants, and other subsidies to qualified bioscience and health science businesses, including start-up businesses, that locate and operate in a designated area.

16. The Wisconsin Technology Council was created under the provisions of 1999 Wisconsin Act 106. The Act required Commerce to organize and assist in maintaining a high-technology business development corporation as a nonstock, nonprofit corporation under Wisconsin law for the exclusive purpose of promoting and supporting the creation, development, and retention of science-based and technology-based businesses in the state. In November, 2000, the Governor first appointed members to the Wisconsin Technology and Entrepreneur's Council which was created to promote development of science- and technology-based businesses in Wisconsin. The Council was formed as a nonprofit corporation and the Council's board of directors approved the formation of the non-profit Wisconsin Technology Council in January, 2001. Commerce awarded the Council a grant of $50,000 to fund start-up and administrative costs. The Wisconsin Technology Council is an independent, nonprofit, tax-exempt corporation which serves as a leading policy adviser and catalyst for creation, development, and retention of science- and technology-based businesses in Wisconsin.

17. A board of directors consisting of the Secretary of Commerce, or a designee, the President of the University of Wisconsin System, or a designee, the director of the Wisconsin

Technical College System (WTCS) Board or a designee, the president of the Wisconsin Association of Independent Colleges and Universities or a designee, and at least eleven other members governs the high-technology development corporation. Of the eleven other members, one or more must represent the following categories: (1) entrepreneurs in the state; (2) high-technology businesses in the state; (3) the state's venture capital industry; (4) the state's investment banking industry; (5) local governments in the state; (6) the state's business development community; and (7) professionals that provide services to these categories. The board members are appointed by the Governor or legislative leadership and serve five-year terms. The high-technology business development corporation is required to specify in its bylaws the method of electing new board members and filling vacancies.

18. The Wisconsin Technology Council has three main functions:

a. Policy Guidance. The Council is the science and technology advisor to the Governor and Legislature and provides policy guidance to them and to state agencies, and other related institutions. In performing this function the Council has developed the Vision 2020 report (*Vision 2020: A Model Wisconsin Economy, 2002*), and published white papers that analyze economic development issues related to technology development.

b. Networking. The Council serves an in-state networking role through the Wisconsin Innovation Network (WIN) and other affiliates, such as the Wisconsin Biotechnology Association, Accelerate Madison, and eInnovate. Out-of-state networking is also provided through the I-Q corridor linking organizations and individuals in Wisconsin, Minnesota, and Illinois, and through national events such as the international BIO conference. WIN is the membership subsidiary for the Wisconsin Technology Council with chapters in Chippewa Valley, the Lake Superior Region-Ashland, Madison, Milwaukee, and Northeast Wisconsin. WIN is a community-based economic development organization designed to foster innovation and entrepreneurship. Local chapters offer connections with local entrepreneurs and a variety of industries and professionals in high-technology, law, banking, government, public relations, and manufacturing. WIN provides venues for entrepreneurs and technologists to attend seminars, speeches, "how-to" conferences, and to trade and compare information. Issues of regional importance that should be addressed by the Technology Council are identified by local WIN chapters.

c. Economic Development Catalyst. The Technology Council serves as an economic development catalyst through a number of programs including: (1) WIN; (2) the Wisconsin Entrepreneurs' conference, which provides assistance to entrepreneurs at all stages of business development; (3) the Wisconsin Early Stage Symposium (formerly Life Sciences and Venture Conference) for technology companies seeking capital; (4) the Governor's Business Plan Contest competition that provides business plan advice and cash and in-kind prizes; and (5) the Wisconsin Security Research Consortium comprised of public and private research organizations acting to develop expertise and link state organizations with federal homeland security projects.

The Council also operates the Wisconsin Angel Network (WAN) which was created with initial funding from Commerce, DFI, and the SBC Foundation, to build angel investor network

capacity in Wisconsin in order to increase the number and amount of early stage equity investments in Wisconsin businesses. In general, membership in WAN is limited to investment funds and angel networks. For membership purposes, an angel network is a group of accredited investors who co-invest on a fairly regular basis in early-stage deals. WAN operates the deal flow pipeline, which is an Internet site that allows angel investors to review projects submitted by entrepreneurs for investment consideration. The Network works with members to organize, publicize and secure sponsorships for educational programs designed and tailored for early-stage investors. WAN developed an angel investing guide with information about state tax credits, due diligence, valuation techniques, and deal structure. The Network includes website resource pages for investors and entrepreneurs, such as the recently developed entrepreneurial presentation template for creating an effective investor presentation. Video and computer equipment along with server space is available to WAN members at reduced rates.

19. The Wisconsin Security Research Consortium was created as a separate nonprofit entity, with a separate board of directors, in the fall of 2005 by the Technology Council and 11 public and private research partners. The Technology Council signed a memorandum of understanding to become the administrative agent for the consortium. Consortium activities include: (a) assessing the state's core competencies in technologies related to homeland security; (b) assisting companies in applying for federal grants; (c) providing a pathway to federal opportunities for professors and researchers at public and private institutions; (d) establishing a system to link businesses with UW System or private college expertise; (e) organizing a team of research, development, and technology transfer experts to identify opportunities for state entities to participate in federal programs or obtain federal funds and to notify members of the congressional delegation; and (f) where necessary, designating the independent, nonprofit WSRC to serve as a "catch-point" for federal R & D funds in classified and sensitive areas of research. The Consortium is funded by a federal grant of $493,000, that was received in 2005.

20. The high-technology business development corporation grant program was created by 1999 Act 106 to provide state funding for the entity that would be developed under the provisions of the Act. Commerce is authorized to make grants to the high-technology business development corporation if all of the following apply: (a) the corporation submits an expenditure plan to the Department detailing the proposed use of the grant proceeds and the Secretary of Commerce approves the plan; (b) the corporation enters into a written agreement with the Department that specifies the conditions for the use of grant proceeds, including reporting and auditing requirements; (c) the corporation provides matching funds equal to 50% of the grant proceeds; (d) the corporation provides Commerce with any information requested concerning private funding the corporation has received or will receive for the purposes detailed in the expenditure plan; and (e) the corporation agrees in writing to submit to the Department, within six months after spending the full amount of the grant, a report detailing how the grant proceeds were used. Annual base level funding of $250,000 is provided for grants to the high-technology business development corporation.

21. The Wisconsin Technology Council is staffed by an executive director and four other positions and is funded by annual high-technology business development corporation grants

from Commerce and by matching contributions from the private sector. In addition, the Council is awarded separate Commerce grants for specific purposes. In 2006, state funding included: (a) the $250,000 annual grant; (b) a community-based economic development program grant of $50,000 for participation in the venture capital fair; and (c) a gaming economic diversification award of $75,000 for administering the Angel Network. (State funding for the Angel Network ended on December 31, 2006.) The Council generated approximately $940,000 in private matching funding.

22. The Wisconsin Entrepreneurs' Network (WEN) was created to promote entrepreneurship and innovation in Wisconsin, and includes the University of Wisconsin System, the Wisconsin Technical College System (WTCS), the WiSys Technology Foundation, and the Agricultural Innovation Center. WEN, which began operations in June, 2005, incorporates the services and resources of: (a) the UW-Extension statewide small business outreach network, with 13 campus-based small business development centers; (b) WiSys Technology Foundation (a non-profit subsidiary of the Wisconsin Alumni Research Foundation) that protects, patents and licenses inventions created by scientists at the UW campuses, other than UW Madison; (c) the WTCS network of 16 colleges throughout the state; and (d) the Department of Agriculture, Trade and Consumer Protection (DATCP) Agriculture Innovation Center providing assistance to agriculture-related entrepreneurs. The Network offers a variety of services to entrepreneurs in all industries and at all stages of development including business planning, educational workshops, executive programs, peer learning, access to capital, technology transfer assistance, and assisting high-growth businesses to the next level.

WEN is comprised of 25 intake centers, four regional technology-transfer centers at UW-Eau Claire, UW-Milwaukee, UW-Madison, and Northeast Wisconsin Technical College (Green Bay), and 26 counselors. Counselors at the intake centers assess clients' projects for the capacity to grow and succeed. Potential high-growth client projects are referred to one of the regional centers where staff evaluate the management team, market size, competitive advantage, and other related factors. Certain clients are identified to receive highly personalized attention, including assistance in gaining access to capital and other financial resources, which continues until the new ventures are self-sufficient.

23. In May, 2006, Commerce transferred the Early Planning Grant (EPG) program for the Department's major financial assistance programs (Wisconsin Development Fund, Rural Economic Development, Minority Business Development) and the Technology Assistance Grant (TAG) program of the WDF technology commercialization grant and loan program to WEN for administration. WEN also administers the Entrepreneurial Training Grant program. Commerce contracts with WEN to provide funding for the grant programs and WEN operations. The grant programs' general provisions are: (a) urban early planning grants provide financial assistance to entrepreneurs and small businesses to fund professional services related to business start-ups or expansion; (b) entrepreneurial training grants are awarded through a program developed in conjunction with the University of Wisconsin-Extension Small Business Development Center (SBDC) designed to help entrepreneurs by providing financial assistance to cover a portion of the cost of attending SBDC's Entrepreneurial Training Program; (c) technology assistance grants to provide financial assistance to entrepreneurs and to start-up and early stage businesses to fund

research and development or professional services related to obtaining early stage funding.

24. WEN has a program coordinator, an administrator, a minority business development specialist, and four regional directors and staff. WEN administrative activities include technical assistance, application intake, producing credit reports, distributing grant funds, and conducting follow-up surveys and reporting. Staff uses the WEN Tracker data processing system. Commerce has contracted with WEN to provide funding from 2005 through 2008 for operation expenses and grants to entrepreneurs. WEN will receive a total of $3.2 million in Wisconsin Development Fund (WDF) and Rural Economic Development Program (RED) grants, and a $3.0 million CDBG economic development grant. A total of $1.2 million of WDF and RED grants are allocated for entrepreneurial training, early planning, and technical assistance grants to entrepreneurs. Commerce has access to the WEN Tracker data processing system, and receives periodic reports on grant activities. A Commerce underwriter also attends WEN weekly review meetings.

25. The technology commercialization grant and loan program was created by 2003 Wisconsin Act 255 to provide financial assistance to entrepreneurs at various stages of business growth. This program, which is administered by Commerce, was incorporated into the WDF in 2005 Wisconsin Act 25. To be eligible for grant programs applicants include: (1) a small business, or an individual entrepreneur who intends to form a small business; or (2) an individual who is starting or developing a business which has significant growth potential, as evidenced by the potential to attract and receive early stage financing from third parties, but who needs assistance with a specific facet of starting or developing the business. Funding is distributed through the following programs: (a) technology assistance grants to provide financial assistance to entrepreneurs and to start-up and early stage businesses to fund research and development or professional services related to obtaining early stage funding; (b) matching grants (administered by WEN) and loans provide funding to individuals, entrepreneurs, and small businesses for professional services related to developing or the accelerated commercialization of a technologically innovative product, process, or service; (c) bridge grants and loans provide financial assistance to individuals, entrepreneurs and small businesses experiencing financial hardship to cover expenses between early-stage and later-stage financing; and (d) venture capital grants and loans provide financial assistance to individuals, entrepreneurs, and small businesses for early stage financing. About $3.0 million was awarded through these programs in 2005-06.

26. Act 255 also created the early stage business investment program that included the angel investment tax credit and The angel investment tax credit provides a credit for an angel investment in a qualified new business venture, while the early stage seed tax credit provides a credit for an investment by a fund manager in a qualified new business venture (certified business). In order to qualify for tax credits, an investment must be made in a "qualified new business venture" (certified business). A "qualified new business venture" is an early stage business conducting precommercialization activity related to proprietary technology and that is certified by Commerce.

Angel Investment Tax Credit. The angel investment tax credit is equal to 12.5% of the claimant's bonafide angel investment made directly in a qualified new business venture in a tax year. The 12.5% tax credit can be claimed for two years, beginning with the tax year as certified

by Commerce. The maximum aggregate amount of angel investment tax credits that may be claimed for a tax year is $3.0 million. The maximum total amount of tax credits that can be claimed for all tax years is $30 million. The total amount of angel investment tax credits allocated was $3.0 for tax year 2005, and $2.4 million for tax year 2006.

Early Stage Seed Investment Tax Credit. The early stage seed investment tax credit is equal to 25% of the claimant's investment paid in the tax year to a fund manager that the fund manager invests in a business certified by Commerce (qualified new business venture). The maximum aggregate amount of early stage seed investment tax credits that can be claimed for a tax year is $3.5 million. There are $3.4 million in credits remaining to be allocated for tax year 2005, and $2.1 remaining for tax year 2006.

27. The State of Wisconsin Investment Board (SWIB) has targeted venture capital investment opportunities since 2000 through the Wisconsin Private Equity Program. Between 2000 and 2005, SWIB has made commitments to allocate a total of $185 million to six venture capital firms operating in Wisconsin. These venture capital firms have interests covering a range of technologies, including biomedical, life science, business services, enterprise software and applied technology (wireless devices, fuel cells). The type of investments include providing seed money to new companies to investing additional funds for expansion and growth. SWIB investment commitments are allocated to the funds over five to six years after the fund has been established. Research and investment decisions are the responsibility of the managing partners of the respective funds. Each of the funds invests in a diverse portfolio of companies that fall within the company's investment strategy. Typically returns are not generated for at least five years. SWIB committed $45 million to two funds in 2000, $30 million to one fund in 2003, $60.0 million to one fund in 2004, and $50 million to two funds in 2005. The two most recent commitments are to firms with prior SWIB private equity commitments. The investment strategy for those funds is focused on seed and early stage financing for investment opportunities produced through Wisconsin universities and medical research facilities. As of December 31, 2006, $72 million had been allocated to the venture capital funds.

28. The Wisconsin Technology Council, Wisconsin Entrepreneurs' Network, technology commercialization grant and loan programs, angel investor and seed fund investment tax credits, and SWIB Private Equity Program are all initiatives that receive state funding and are designed to generate capital and/or provide financial and technical assistance for entrepreneurial ventures. Most of these initiatives were started within the last five years, and have had a significant number of clients. In April, 2007, WAN had 25 members representing 250 individual investors, and listed 125 deal summaries. WEN has provided technical assistance to entrepreneurs and awarded $350,000 in grants in fiscal year 2005-06. In the same fiscal year, a total of $2.9 million in technology commercialization grants and loans was awarded to 24 companies. Finally, SWIB has provided $72 million in funds for venture capital investments, another $115 million is committed for future investments. Marketing of these programs raises awareness of investment opportunities and intellectual capital available in Wisconsin. This could be viewed as creating the underpinnings of a capital investment network and a market for future venture capital investments that would attract out-of-state capital.

29. If the Committee wishes to establish a venture center, one alternative would be to establish it as a separate nonprofit entity with the Technology Council as administrative agent. This would be similar to the organization of the Wisconsin Security Research Consortium.

ALTERNATIVES TO BASE

1. Adopt the Governor's recommendation to require Commerce to organize and assist in maintaining an emerging industries development corporation as a nonstock, nonprofit corporation under state law for the purpose of facilitating raising capital to promote and support emerging industries in Wisconsin. Require that the emerging industries development corporation would be governed by a board of directors and provide Commerce $1.0 million GPR annually for grants to the emerging industries development corporation.

ALT 1	Change to Bill Funding	Change to Base Funding
GPR	$0	$2,000,000

2. Adopt the Governor's recommendation, but require that the Wisconsin Technology Council be administrative agent for the Venture Center.

ALT 2	Change to Bill Funding	Change to Base Funding
GPR	$0	$2,000,000

3. Maintain current law.

ALT 3	Change to Bill Funding	Change to Base Funding
GPR	- $2,000,000	$0

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