

New Tax Incentives for Investments in High Growth Early Stage Businesses in Wisconsin

With the enactment of 2003 Wisconsin Act 255 (the "Act") on April 15, 2004, the State of Wisconsin was aiming to boost economic activity within the State through tax incentives that would attract capital and promote investment in certain qualified high growth early stage technology companies. The Act created two new tax credits effective commencing in tax year 2005: an Early Stage Seed Investment Credit and an Angel Investment Credit.¹

While the new law provides generous tax credits of up to 25% of the investor's cash investment, the total available tax credits under the Early Stage Seed Investment Credit program and the Angel Investment Credit program are only \$3.5 million and \$3.0 million per year, respectively. Therefore, businesses hoping to take advantage of the opportunity for investment through the new tax credit programs, as well as investors seeking credits, will need to act quickly to get a portion of the annual allocation of credits from the Wisconsin Department of Commerce.

Below is a summary of the nature of the businesses eligible under the new tax credit programs as well as some of the key differences between the Early Stage Seed Investment Credit and an Angel Investment Credit.

What types of companies may be eligible for investment?

Only "Qualified New Business Ventures" are eligible under the tax credit program. To become certified by the Department of Commerce as a "Qualified New Business Venture" the company must meet certain objective and subjective criteria. The objective criteria that the business must meet include:

- ❖ Headquarters in the State of Wisconsin;²
- ❖ At least 51% of its employees in the State;
- ❖ Engage in (or commit to engage in) developing a new product or process;
- ❖ Engage in manufacturing, agriculture, or processing or assembling products and conducting research and development;
- ❖ Not be engaged in certain service industries such as real estate development, insurance, banking, among others;
- ❖ Conduct activity relative to the development of proprietary technology;
- ❖ Not received more than \$1 million in aggregate investments that have qualified for credits under the Angel Investment Credit; and
- ❖ At the time of certification, have less than 100 full time employees, be in operation for 7 consecutive years or less, and not have received private equity cash investments of over \$5 million.

In addition to the objective criteria set forth above, the Department of Commerce will consider additional subjective criteria in making the determination whether or not to certify the company as a Qualified New Business Venture. Those subjective criteria or qualifications include:

¹ In addition to the two new tax credits, the Act also created a Technology Commercialization Grant and Loan Program that will provide loans and grants primarily to assist companies in obtaining professional services (such as costs associated with feasibility studies, business plans, market research and patent protection) to assist the company seeking financing or capital in the marketplace.

² To meet this criterion, the company has to either have its principal central administration office in the State or pay at least 80% of payroll to employees in the State.

- Whether the business is one of Wisconsin's targeted industries determined by the Department of Commerce (biotechnology, health technology, information technology or nanotechnology);
- Whether the company has high-growth potential, long-term sustainability and sufficient barriers to entry;
- The experience level of the management team;
- The financial need of the business;
- The percentage of funds being sought for investment that will be spent in the state; and
- Whether the company has an innovative or novel product or process.

As of March 25, 2005, twenty-one businesses had been certified by the Department of Commerce as Qualified New Business Ventures.

The business activities of those companies certified to date include technology or the development of products for or relating to or used in:

- Proprietary test kits and reagents for drug discovery labs;
- Instrumentation and consumables for life sciences research and pharmaceutical development;
- Antioxidant oils and botanic materials for use in cancer therapeutics and nutritional products;
- Imaging and treating cancer tumors in humans;
- Technologies for the prevention and treatment of pathogenic bacterial infections;
- Developing biochip products for life science, pharmaceutical and diagnostic researchers;
- Proteins for control of foodborne pathogens and alternatives to veterinary antibiotics, particularly those used in foodstuffs;
- Gene cloning, genomics and enzyme discovery; medical devices, including magnetic resonance (MR) imaging-guided interventional systems;
- Monoclonal antibodies for research, diagnostic and therapeutic applications;
- Devices and services to support MRI-based diagnostic evaluations;
- A natural antibody product to improve food efficiency and enhance growth of feed animals;
- Nanotechnology-based products for the life sciences;
- A multiplexer device to transfer physiological data from the home to the electronic records of health care providers;
- Novel protein-based cancer therapies; treatments for neurodegenerative diseases such as Alzheimer's and Parkinson's diseases;
- Software products to help consumers manage and maintain personal health records;
- Directional sound reproduction and amplification systems;
- Hydrogen and hydrocarbon fuel gas from oxygenated compounds; and
- A proprietary electrotactile human-machine interface platform.

Eighteen of the twenty-one companies certified to date are located in the Madison area; one is located in Milwaukee; one is located in Spooner and one is located in Neenah, Wisconsin.

Differences between the Early Stage Seed Investment Credit and the Angel Investment Credit.

While both tax credit incentives relate to investments in Qualified New Business Ventures, there are differences in the two programs. Some of the key differences in the tax credit programs are set forth below:



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	<i>Early Stage Seed Investment Credit</i>	<i>Angel Investment Credit</i>
<i>Investor invests capital in:</i>	Venture capital fund that invests in Qualified New Business Venture	Qualified New Business Venture directly
<i>Total Credits Available under Program</i>	\$3,500,000/year (\$35,000,000 over ten year life of program)	\$3,000,000/year (\$30,000,000 over ten year life of program)
<i>Credit as Percentage of Investment</i>	Up to 25% credit may be taken in year 1.	Up to 12.5% credit in each of the first two years
<i>Investor Suitability</i>	Suitability is for investment in the venture fund itself; most likely only accredited investors under state and federal securities laws.	Each Angel Investor (or member of an Angel Investor network) must be an accredited investor. Accredited Investor for purposes of the Angel Investment Credit includes: <ul style="list-style-type: none"> • Investor with Net Worth (with or without spouse) over \$1 million; • Income over \$200,000 in last 2 years (\$300,000 with spouse) and same expectation for current year; • A director, officer or general partner of issuer (or relative of any of the foregoing) provided no more than 20% interest in the company; or • An individual with knowledge and experience in financial and business matters capable of evaluating the risks of the investment.
<i>Fund Manager</i>	Must be Certified by the Department of Commerce. Criteria include: manager's experience, past performance, expected level of investment in Qualified New Business Ventures, targeted industries, and commitment to Wisconsin.	N/A
<i>Maximum Aggregate Investment in New Business Venture that may qualify for credits</i>	Up to \$2 million in aggregate investment by a certified fund manager in a qualified new business venture over the life of that business.	Up to \$500,000 in aggregate investment by an angel investor or member of an angel network in a qualified new business venture.

The new tax incentives are a good step toward attracting new capital investment in emerging companies within the State. However, since the amount of credits available is relatively small, investors and companies hoping to qualify for investment will need to take prompt action.

The Business Practice Group of Whyte Hirschboeck Dudek S.C. has significant experience in representing angel investors and investor networks in making private equity investments as well as representing emerging companies in seeking and obtaining capital. **For more information, please contact Don Rintelman at (414) 978-5506 or Lisa Lange at (608) 258-7129.**