MIKE KUGLITSCH

STATE REPRESENTATIVE • 84TH ASSEMBLY DISTRICT

DATE: October 18, 2017
RE: **Testimony on 2017 Assembly Bill 489**

TO: The Assembly Committee on Jobs and the Economy
FROM: Representative Mike Kuglitsch

Thank you, Mr. Chairman and Committee Members for holding a public hearing on Assembly Bill 489. The biggest hurdle many emerging companies face is lack of capital and this legislation builds upon the success of an already successful program.

Currently in Wisconsin, investors of Qualified New Business Ventures (QNBV) can receive a nonrefundable tax credit of 25% of their total investment into any certified QNBV. To achieve QNBV certification from the Wisconsin Economic Development Corporation, companies must meet the following measures:

- Headquartered in Wisconsin
- At least 51 percent of employees based in the state
- Have fewer than 100 employees
- In operation for 10 consecutive years or less
- Offer significant potential or increasing jobs or increasing capital investment in Wisconsin
- Have not received aggregate private equity investment in cash of more than $10 million

Under current law, the maximum amount of investment dollars that qualify for angel and early stage seed credits is $8 million. This legislation raises the cap from $8 Million to $12 million. This change will entice investors across the state to continue to invest in Wisconsin's growing businesses. According to the Wisconsin Economic Development Corporation, there are currently 194 certified businesses within the state. Roughly 30 of these certified companies are approaching or have reached the current maximum threshold. Many of these companies have expressed interest in continued participation of the program if the cap was raised from $8 to $12 million and they have also indicated their need for additional capital moving forward.

These businesses have already been vetted and have been receiving investment capital from angel and venture investors across the state. In terms of the capital continuum, many of these businesses that have met the cap, are in what many call the valley of death. It is at this point where capital becomes harder to obtain. This tool will continue to incentivize money flowing to already successful businesses and move Wisconsin's private sector forward in terms of job and company creation.

As legislators and members of the Committee on Jobs and the Economy, I believe it is imperative to deploy as many tools as possible to connect capital with emerging industries. Without capital, these small businesses can get lost and die on the vine. Thank you for allowing me to testify and I ask that you support AB 489.

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TOM TIFFANY

STATE SENATOR • 12TH SENATE DISTRICT

Testimony on Assembly Bill 489

Assembly Committee on Jobs and the Economy

October 18, 2017

Thank you Chairman Neylon and members of the Assembly Committee on Jobs and the Economy for holding a public hearing on Assembly Bill 489 which seeks to raise the investment ceiling of $8 million on credit-eligible companies for the purposes of being certified as a QNBV to $12 million.

Act 255 sets an investment ceiling of $8 million on credit-eligible companies. After nearly 12 years, inflation alone indicates that the ceiling placed in 2005 is far too low. Additionally, there are more capital-intensive operations that simply require more capital investment to fuel their growth.

There is no one-size-fits-all solution to growing young companies. According to the Department of Revenue, there are 211 certified qualified new business ventures (QNBV). Last year six QNBVs received the maximum allowable eligible investments bringing the total to reach the threshold to eleven. Of those certified QNBVs, 22 have received more than $4 million of investments and could reach the threshold within the current biennium. There are also several QNBVs who previously reached the statutory limit and who may want to recertify as a QNBV. In total, WEDC believes this bill could reach about 35 different companies.

Startup companies help grow our communities by hiring within the community, often utilizing resources (people, investment, real estate) in the community as well. I believe we in the legislature need to ensure that we create solutions that work across industries rather than hamstring particular ones simply because they are more capital-intensive. AB 489 will ensure we continue to grow Wisconsin's home-spun startups and continue to push investment in small businesses across the state. We would appreciate your support for AB 489.

Tom Tiffany
Wisconsin State Senate
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WISCONSIN TECHNOLOGY COUNCIL

October 18, 2017

TO: Members of the Assembly Committee on Jobs and the Economy
FROM: Tom Still, president of the Wisconsin Technology Council
RE: Assembly Bill 489

Dear Chairman Neylon and members of the committee:

One of Wisconsin's most successful strategies for spurring the growth of young companies for the past decade or so has been its Qualified New Business Venture law, known as the "Act 255" investor tax credits law because of how the law was titled when it passed.

The program provides tax credits to qualified Wisconsin investors who put money into young companies with some sort of technology base, even if the company is aligned with a more traditional sector such as manufacturing or agriculture.

Since it took effect in 2005, the Act 255 program has prompted at least $466 million in private investments in emerging companies that have earned QNBV status through the Wisconsin Economic Development Corp. (previously, the Wisconsin Department of Commerce) based on standards set by a law that has changed only incrementally over time.

It's a rigorous vetting process that, once completed, earns the angel and venture capital equivalent of a "Good Housekeeping Seal of Approval" for young companies. Potential investors in Wisconsin often won't consider companies that are not QNBV-certified because they trust in the process enough to know it's worth taking a closer look.

They also like the tax credits, which are worth $1 in state relief for every $4 invested. There are scores of examples of investors who took a chance on a young company knowing the credits would help mitigate the risk or allow them to invest more than they had planned.

About $116.5 million in credits have been granted over time, all retroactive to the actual investment, and nearly 1,200 new jobs have been created in the past six years alone. The law has been a model for investment tax credit laws in other states add a major reason why Wisconsin's early stage investment community has grown from a handful of venture and angel funds or networks in the early 2000s to about 40 such groups today.

In 2016, for example, about $276 million in angel or venture capital was invested in 136 Wisconsin companies – 84 of which were QNBV-certified.

As time passed, however, some parts of the law aged. One update, as embodied in AB 489 and its Senate companion, is lifting the lifetime cap on credit-eligible investments in any single company from $8 million to $12 million.

The $8 million cap has been in place almost since the dawn of the law, and inflation alone suggests it should be raised. The biggest problem is that many tech-based companies, especially those in health care or manufacturing, are so capital-intensive that it takes more money to fuel their growth. The typical venture capital investment of 2005 is not the norm in 2017.

So far, 14 emerging companies in Wisconsin have been "capped out," meaning those companies hit the $8 million investment ceiling that yielded $2 million in credits for their investors. Another 20 are poised to bump against the ceiling soon, based on an analysis by the Legislative Fiscal Bureau.

While there are other improvements that could be made in the Act 255 law over time, this change is most timely because most of the companies at or near the $8 million ceiling are poised for rapid growth – if they can land more investment dollars. Those companies are statistically likely to produce large numbers of good-paying jobs, as well.

Sometimes overlooked is how much those emerging companies buy in supplies, goods and services from other companies across Wisconsin. That supply-chain effect means a company based in Madison, Milwaukee or Menomonie may be buying equipment or other services from firms in Rhinelander, Green Bay or Wausau. In that sense, the entire state has a stake in the success of young, tech-based companies.

Some have criticized Wisconsin policymakers for doing too much for big companies. Passage of SB 398 and AB 489 would help companies on the other end of the spectrum.

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Oct. 18, 2017

TO: Members of the Assembly Committee on Jobs and the Economy
FROM: Jason Graham, Associate Director, Golden Angels Investors, LLC
RE: Assembly Bill 489

Dear Chairman Neylon and members of the committee:

Thank you, Chairman Neylon and members of the committee for the opportunity to testify. I am here today representing the interests of Golden Angels Investors, LLC, one of the state's largest and most active angel investing networks. We have more than 160 members and are on pace to invest in excess of $6 million in early stage ventures this year, the majority in Wisconsin-based companies.

Golden Angels strongly supports increasing the tax credits available under Act 255 from the first $8 million invested to the first $12 million invested. As a CPA and former Chief Financial Officer, I understand that investors are tax sensitive. An underpinning of modern finance theory is that the value of an investment is equal to the present value of future after-tax cash flows.

Golden Angels invests at the earliest stages in a company's life cycle – both pre-revenue and early-revenue. While our investment diligence process is lengthy, comprehensive and informed by the deep subject matter expertise of our network members, the risk profile of the companies in which we invest remains extremely high. Our experience bears that out: from 2002 through October 2017, we exited 14 companies in which we had made previous investments. Four returned more than our invested capital, five returned less and five were complete losses.

When we invest, we always seek to be more than merely a source of capital to the entrepreneur. Our members provide our investee companies with coaching and mentoring, customer introductions, and often serve as Board Directors. Stylistically, we aim to be full life-cycle investors – investing from the earliest stages through commercialization, growth and eventual exit.

The companies in which we've invested are solving urgent problems in medicine, technology and other fields and creating jobs and economic development. Due to our lifecycle investing approach, two of our portfolio companies based in Wisconsin have run into the $8 million cap imposed by Act 255 – Promentis and Perblue Entertainment. A third, Emopti, is near the cap.

Given the aforementioned high degree of investment risk coupled with investors' tax sensitivity; I am concerned that the current $8 million cap is not sufficient to incentivize the appropriate capitalization of these early stage ventures. Achievement of satisfactory investment returns at the earliest and most risky stage of a company's life cycle hinges in part on the receipt of tax credits. I fear that a failure to raise the cap will lead to investors seeking later-stage and therefore, less risky investment opportunities and reduce investment capital available to companies in the earliest stages of innovation and disruption.

Wisconsin has taken bold action with Foxconn to fundamentally transform the technology and manufacturing ecosystem in the State. Smaller enabling efforts such as increasing the limit of the Act 255 credits may not generate the same type of splashy headlines but are no less important to creating an environment of innovation, capital formation, job creation and economic development.

Thank you, Chairman Neylon and members for permitting me this opportunity to speak.

Oct. 18, 2017

TO: Members of the Assembly Committee on Jobs and the Economy
FROM: Todd Sobotka, Managing Director and Portfolio Manager, Brightstar Wisconsin Foundation
RE: Assembly Bill 489

Dear Chairman Neylon and members of the committee:

I am asking for your strong consideration and support of Assembly Bill 489. Over most of the past decade, I have been actively involved with the early stage sector throughout the state. The advances that have been made over the past 10-15 years are remarkable, and the QNBV tax credit was and is a key reason for it. I can state without hesitation that these credits have pulled a substantial amount of new capital into the early stage space and made some deals happen that perhaps otherwise would have struggled to receive funding. Additionally, early stage investors tend to re-invest available capital into other deals, thus expanding the overall pie and providing a multiplier effect. The credits have been incredibly positive, but when exhausted, so many companies get stuck close to the finish line.

So many of the dozens and dozens of QNBV certified companies are stil making progress (which means the creation of value, wealth, and jobs here in our state), but have hit the capital wall—the Wisconsin Wall (also known as the Valley of Death). It is when a company enters a stage of its business when its capital needs can no longer fully be satisfied by angel investors, the need is not big enough yet for normal VC's to step in, and the company is far too early for traditional bank lending. This wall is thicker in Wisconsin because of the lack of venture capital funds and angel capital can only go so far. Yet, we need these individual angels and start-up funds to stretch just a little farther to bridge the company to the stage where more substantial money/venture capital is willing to step in. In some unique cases, this stretching of capital could also lead to an exit even prior to a major venture capital round—which also has an amplifying effect on the Wisconsin early stage space.

Incentives need to be given for already exhausted angels to invest further or to attract and entice new investors to break through the wall and assure the capital necessary for the early stage company to bring in venture capital or a potential aquirer.

The expansion of tax credits from a maximum of $8MM in investments to $12MM helps fill this gap as it mitigates the continued risk of current investors and allows new investors to partake in this risk mitigation which otherwise would not have been available to them—which then would probably keep their essential capital on the sidelines instead of deployed for the good of the state. This expansion makes a difference, and would make an immediate impact in capital raises that are ongoing with my current portfolio entrepreneurs.

So many Wisconsin companies are doing what they need to do, and it was the Qualified New Business Venture Tax credit that helped get them there. The QNBV program has performed the way it was supposed to by advancing the Wisconsin early stage space, drawing in more capital, and catalyzing more deals to get done. Through the expansion of this program, let's please give these entrepreneurs the last step of tax credit support they need to bridge the valley or climb the wall.

Respectfully,

Todd E. Sobotka
Managing Director and Portfolio Manager
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Oct. 18, 2017

TO: Members of the Assembly Committee on Jobs and the Economy
FROM: Justin Beck, CEO, PerBlue Entertainment Inc.

RE: Assembly Bill 489

Dear Chairman Neylon and members of the committee:

I grew up in Middleton, WI and graduated from the University of Wisconsin-Madison with a double major in Computer Engineering and Computer Science. While in school, I interned at Google in San Francisco in 2007 and Microsoft in Seattle in 2008. In 2008 we started PerBlue with some classmates from UW. PerBlue makes mobile games and is based in Madison with a team of 40 people. Our games have been played by millions of people around the world.

We raised over $11M for PerBlue in equity and debt financing between 2008-2016. Our financing came from funds in Denver, Chicago (Lightbank), Milwaukee (Golden Angels), and other angels from around the region. We almost moved PerBlue to California multiple times over the years chasing talent, capital, and acquirers. But we decided to keep PerBlue here in Madison and are proud of it. We sold our biggest product (DragonSoul) to a public Japanese technology company in a transaction in late 2016 for a reported value of over $35M. We continue to operate PerBlue independently making new games, and are continuing to grow our team in Madison.

There are 3 main reasons why increasing the Act 255 company cap is important to companies like PerBlue, and a valuable use of state funds:

1. First, we have to look at the success of the original Act 255. It has provided strong capital incentive to direct capital into WI emerging companies.
    a. Act 255 unlocks capital. It gets more angel investors off the bench, and encourages those already investing to look for more deals.
    b. Angel investors make up a large volume of WI deal volume. When angel investors are choosing how to allocate their personal investments, whether in a follow-on angel investment or to put it in the public markets, Act 255 helps swing decision.
    c. Act 255 helps attract out of state VCs to invest in WI companies. Our Chicago based VC has now invested in 3 WI companies, and having access to the Act 255 credits affects the investment volume they are willing to do in a deal and enables them to justify larger investments.
    d. Investors naturally want bigger stakes in companies, but it comes down to capital return. The secondary market sale of tax credits has made VCs willing to take bigger stakes in WI companies which gives WI companies access to more capital. It has also made more VCs interested in stepping up to "lead" deals.

RE: Assembly Bill 489, Continued:

2. Second is about growth of emerging companies and scaling employment.
    a. Companies that are past Series A into Series B and C stage are scaling up quickly. They employ more people and hire many more people than a Seed Stage company. They are hiring from the local job market, but also pull experienced employees from around the country into the WI job market.
    b. Companies require a lot more cash to compete in the market place now than they 5 years ago. Average Series A is well north of $6M now.
    c. Retaining companies in WI post-Series A stage is arguably an even more important thing for our state's long term economic health. Once a company has established their full operating team at that scale it makes relocating nearly impossible. Instead of external VC's encouraging a company to relocate out of WI you will now have VC's encouraging them to stay. The optics of that make WI seem relevant nationwide in the growth company market.
3. Third is about compounding returns.
    a. If VCs can make favorable investments in WI, they will look harder and do more deals in the state.
    b. Better funded companies staying in WI will create compounding returns. Those companies will retain and attract talented employees to the state. Those employees have spouses that are also employed in the state, kids in schools, and are spending in local communities.
    c. Angel investors have more capital to work with, more dollars invested, and more seeded companies. This creates more shots on goal for the state of WI to build the next batch of high growth companies and big employers.

Sincerely,

Justin Beck

Co-founder and CEO
PerBlue Entertainment, Inc

Email: justin@perblue.com
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316 W. Washington, Suite 900
Madison, WI 53703
Oct. 18, 2017

TO: Members of the Assembly Committee on Jobs and the Economy
FROM: Brian Lindstrom, COO, Datica Health, Inc.
RE: Assembly Bill 489

Dear Chairman Neylon and members of the committee:

Thank you for your time today and for the opportunity to let me speak to you regarding a topic I am passionate about: that is planting and growing companies in Wisconsin. I want to share with you my personal experience and observations and how they shaped my view that investing in entrepreneurship is a wise and necessary action to take in Wisconsin.

By way of introduction, I am currently the Chief Operating Officer at Datica, a HIPAA compliant cloud hosting company started in Milwaukee, but subsequently moved to Madison. We enable healthcare entities to exchange messages with healthcare IT vendors, payers/insurers, and pharma in a safe and secure manner along storing information, when necessary, in the cloud. We were founded four years ago, are a certified QNBV company, and have borrowed $500k from WEDC. We have 40 total employees, about 3/4 of whom are in Wisconsin. The average wages and benefits per employee across the company is approximately $125,000.

I am proud to be a "native" of Wisconsin having been born and raised in the Menomonee Falls/Mequon area. After college in Illinois, I returned to Milwaukee to work for Arthur Andersen. I have been fortunate to have worked in "startups" in various locations throughout the state including Kimberly-Clark in Neenah, Schneider Trucking in Green Bay, and Epic in Madison. My whole career has been in the accounting and finance arena providing analysis, reporting, and guidance to company leadership on how to best manage scarce financial resources.

Over the last several years, I have worked with in smaller companies backed by both private equity and venture capital investors, all in healthcare technology, a rapidly expanding area in which Wisconsin has a competitive advantage. I personally enjoy working with these smaller companies due to their mission, their passion, and their energy. I would like to share with you my experience working in these environments and why I do believe raising the current cap on Act 255 investments from $8M to $12M is a wise and appropriate investment to perform in the state. To be competitive on a national scale, I do support the increase in the cap.

I want you to know I am an "operator," not an entrepreneur. I don't come up with those creative, breakthrough ideas that enable hospitals to store patient records like an Epic or more efficiently deliver food to consumers and businesses like the most valuable startup in the state, EatStreet. Rather, I have often been responsible to find funding, be it debt for a new building campus or be it equity for working capital needs to keep day to day operations going. I have been with companies (two within the last year) which were hours away from not making payroll. In an internet connected world, if we failed to make payroll, it would have been across the web nearly instantly where both customers and employees would lose faith in the company as a going concern. Those near-death experiences, for better or for worse, are a common occurrence on a regular basis to fledgling new businesses due to a variety of factors, including access and availability of capital.

Most of my experience relates to 'scaling' businesses. In other words, after the company has established product/market fit and needs access to capital to grow and expand, I work to find access to that capital. In my current role at Datica, I can share a bit regarding the company's experience in raising funds which is pretty typical of growth businesses. After graduating from the Gener8tor incubator in Milwaukee, the company has raised several rounds of funding, nearly all of which came from out of state venture capital firms including Baird Ventures and Chicago Ventures from Illinois, Lewis and Clark Ventures from Missouri, and Arthur Ventures from North Dakota. Debt financing is even more difficult to find in Wisconsin. There are no venture banks based in the state, and banking regulations have made it difficult for traditional lenders to enter the space. We raised $3M last summer with the only banks participating in the bidding process were Comerica from Texas, Square 1 from North Carolina, Silicon Valley Bank from California, and Wintrust from Illinois. Note all of these aforementioned entities are out of state as most of their investors. Raising capital from such a syndicated group is difficult due to the multiple constituencies to manage. In addition, the ease of raising capital is inversely proportional to the distance traveled. In other words, when a VC is not in relative close proximity to the target company, the network effects do not happen. VCs don't hear, what is interesting, what is novel, what is breakthrough in Madison or Milwaukee let alone Wausau, Green Bay, Eau Claire, or Superior. In fact, a significant proportion of VCs in the San Francisco Bay area will not even talk to companies that are in 'flyover' country. Be it distance, or simply arrogance, the financing opportunities are difficult to find for these scaling businesses.

I do think there are 'green shoots' at the micro company level as there are a growing number of seed/angel level organizations in the state, perhaps 40-50 in total. That said, my observation is there is a significant funding gap for entities in the state that can cut larger checks (for example, $1M+). If you were to review the "Wisconsin Portfolio" publication written by the Wisconsin Technology Council (full disclosure, of which I am a board member) for the last several years in which closed deals are listed, very few seven figure deals were done by VCs in the state. Several organizations can such as 4490 Ventures, Venture Investors, WARF, and SWIB can cut those checks, but the overall number is very low.

When you are an exec or founder in a startup, they say 50% of your day is selling, 50% of your day is running the business, and 50% of your day is raising money. Personally, I want to grow the business at the fastest rate I can. If 50% of my time is spent in talking to investors and banks, that distracts me from other key activities; this includes determining strategy, hiring talent, nurturing sales leads, etc. Having more investors in the state with capital in hand could be a game changer.

VC investing is incredibly risky, which makes it difficult for the prospective portfolio company to raise money. Of course, there are stories out there regarding the Unicorns, or startups with an estimated enterprise value of $1B or more, such as Uber, Lyft, AirBnb, etc. In a recent story in Pitchbook, an organization that tracks venture and private equity investment, only .14% of venture investments make it to $1B. A vast majority fail. In fact, in venture funds with "professional" investors, most of their portfolio companies fail. The VCs are hoping that one or perhaps two portfolio companies return 10x to help offset the losses so the fund can return 2-3x over 10 years. This investment class is so risky that I do believe providing some incentive to investors will permit some breakthrough, incredible companies, the opportunity to receive an investment and thrive.

In conclusion, I am passionate about small businesses in this state. I do pro-bono work for several startups in Madison and I also volunteer to help get Starting Block off the ground. I admire people who get a SBA loan, pledge all the personal assets they own as collateral, don't take a salary, and try to do something they believe in their heart of hearts can make a difference. Yes, some do it to get rich so it is not completely altruistic, but most don't (perhaps I am too close to the healthcare IT startups as I do see many of those entrepreneurs in it to change the way healthcare is delivered vs. simply for the economic payday). Raising the cap from $8M to $12M will give some of these companies a chance to succeed. If the State of Wisconsin can sponsor the venture based growth in the state, I believe the ROI will be positive.

Thank you for your time and consideration.

Regards,

Brian Lindstrom

Brian Lindstrom
Chief Operating Officer
Datica Health, Inc.

TO: Members of the Assembly Committee on Jobs and the Economy
FROM: Todd Asmuth, SHINE Medical
RE: Assembly Bill 489

Thank you for inviting me to speak here today. My name is Todd Asmuth. I am here as the President of SHINE Medical Technologies, but also as a member of the new product and new company community. I am working in my 6th startup and have been a board member and investor in over 30 other companies. I grew up in Milwaukee, lived outside of the state for 14 years and have lived in Madison for the last 14 years.

SHINE Medical is building a plant in Janesville, WI to make medical isotopes. This is a key medical industry raw material that is used in 20M US medical procedures annually for the detection of heart disease and cancer. If you think of a heart stress test, the treadmill test, where they inject a radioactive tracer into the body, so the camera can see bloodflow through the heart, then you understand what we are making.

Nobody makes this product in the US today, in fact nobody makes this product in North America today, Canada just shutdown their 60 year old research nuclear reactor that used to make these isotopes. SHINE is 7 years in to a 10-year project to replace that capacity but with a better method. Simply put, SHINE is going to Make American Isotopes Again.

Our research came out of the UW where our founder Greg Piefer invented a way to manufacture the same isotopes we use today, but in an more efficient, safer and greener way. His invention replaces the use of a nuclear research reactor with a nuclear accelerator. SHINE has 57 employees based in Janesville, WI and we are ramping up to 150 over the next two years. Currently we have 13 open positions for which we are recruiting. We have our federal regulatory permit to build the plant, over $120M in orders from GE Healthcare and other companies, and have broken ground on a prototype plant in Janesville.

We have been helped by UW, WARF, WEDC, the City of Janesville, the Federal Department of Energy and the local private investment community. The Act 255 program has been key to us getting started, and we still are raising funds to deliver our prototype facility and prove that it works.

We are a manufacturing company with a medical market, but there is a really clear public benefit as we come to market. You start with the 150 jobs which are a primarily a mix of engineering and operations jobs. We have a program with Blackhawk Technical College in Janesville to train the operators we will need to run the plant. Then you look at the construction project workforce of 300-400 people for 2 years. In addition, we have along list of local vendors for concrete, steel rebar, tanks, vessels, pipes, asphalt and engineering and construction services.

From there, you look at the medical benefit of having access to these isotopes for patients in Wisconsin, the US and the world. On a pro-rata basis, we estimate 300-350K patients in Wisconsin use these isotopes each year. We project that we will have over $100M in profits by 2025 and there will be a large investor return, much of which will be reinvested, and a significant tax base – payroll taxes, real estate taxes , dividend and capital gain taxes. That said we have needed the support of these Wisconsin institutions to get to where we are today. Our foreign competitors were 100% government funded. For SHINE, government funds have helped us achieve key milestones that de-risk the technology and the regulatory hurdles so that the private market can fund the growth capital

We have larger plans past the medical isotope industry in Janesville for the next stage of the technology.

Committee members, thank you for listening today. I would be happy to answer any questions.