

## COMMENT

### WISCONSIN'S QUALIFIED NEW BUSINESS VENTURE PROGRAM: BUILDING ON THE FOUNDATION TO MAXIMIZE ENTREPRENEURIAL GROWTH

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Start-ups are the future of American business and are essential to the nation's transition from a manufacturing to a knowledge economy. A decade ago, the Wisconsin Legislature recognized the importance of start-ups and enacted the Qualified New Business Venture Program ("QNBV program" or "the program"). The QNBV program incentivizes early-stage investments in high-tech businesses through nonrefundable tax credits. While the program has seen some early success, Wisconsin's economy has struggled and job growth has been limited.

This Comment analyzes the QNBV program and concludes that the Wisconsin Legislature must update the program to better compete for investment capital and to maximize Wisconsin's entrepreneurial growth potential. This Comment argues that the legislature should update the program by (1) making the tax credits refundable to attract out-of-state investors, (2) providing additional tax credits for investments in accelerators nurturing certified businesses, (3) allowing early-stage businesses in restricted industries to rebut the presumption of disqualification from the QNBV program, and (4) providing additional tax credits for investments in specific industries. While these updates to the program will allow Wisconsin to remain competitive for early-stage investments, this Comment concludes that Wisconsin must undergo a more significant legal and cultural undertaking to create a community that mentors and invests in entrepreneurs.

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#### INTRODUCTION

“[S]tartups aren’t everything when it comes to job growth. They’re the only thing.”<sup>1</sup> Entrepreneurs and innovation are the future of American business,<sup>2</sup> yet government officials and scholars debate the extent to which government policy should seed entrepreneurial activity.<sup>3</sup>

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1. TIM KANE, EWING MARION KAUFFMAN FOUND., THE IMPORTANCE OF STARTUPS IN JOB CREATION AND JOB DESTRUCTION 2 (2010), *available at* [http://www.kauffman.org/~media/kauffman\\_org/research%20reports%20and%20covers/2010/07/firm\\_formation\\_importance\\_of\\_startups.pdf](http://www.kauffman.org/~media/kauffman_org/research%20reports%20and%20covers/2010/07/firm_formation_importance_of_startups.pdf) (analyzing the U.S. government report called Business Dynamics Statistics and concluding that, without startups, the U.S. economy would have no net job growth). “States and cities with job creation policies aimed at luring larger, older employers can’t help but fail, not just because they are zero-sum, but because they are not based in realistic models of employment growth.” *Id.* at 6.

2. *See, e.g.*, ROBERT D. ATKINSON & LUKE A STEWART, INFO. TECH. & INNOVATION FOUND., THE 2012 STATE NEW ECONOMY INDEX: BENCHMARKING ECONOMIC TRANSFORMATION IN THE STATES 3 (2012), *available at* <http://www2.itif.org/2012-state-new-economy-index.pdf>. (“For the United States to be competitive, one key will be to compete more on the basis of innovation and entrepreneurship, and less on cost. With a globalized economy enabling easy access to low cost production systems in nations like Mexico and China, U.S. competitive advantage will continue to be found in making things and providing traded services that other nations are unable to make or provide as easily or as efficiently.”); DARIAN M. IBRAHIM, *Financing the Next Silicon Valley*, 87 WASH. U. L. REV. 717, 723 (2010) (stating that non-tech regions in the United States are attempting to spur entrepreneurial growth as the country transitions from a manufacturing economy to a knowledge economy).

3. *See, e.g.*, Mike Ivey, *Sinking with Old Economy: Wisconsin Lags in Developing 21st-Century Companies*, CAPITAL TIMES, Dec. 19, 2012, [http://host.madison.com/news/local/writers/mike\\_ivey/sinking-with-old-economy-wisconsin-lags-in-developing-st-century/article\\_9c07de84-494e-11e2-af46-001a4bcf887a.html](http://host.madison.com/news/local/writers/mike_ivey/sinking-with-old-economy-wisconsin-lags-in-developing-st-century/article_9c07de84-494e-11e2-af46-001a4bcf887a.html). Some leaders believe that government incentives tend to impact a state’s economic growth negatively and reward specific businesses that have political clout. *Id.* Others believe that

A decade ago, Wisconsin state legislators considered this significant policy decision.<sup>4</sup> With the goal of facilitating economic and job growth,<sup>5</sup> the state legislature enacted the Qualified New Business Venture Program (“QNBV program” or “the program”) to incentivize early-stage investments in high-tech businesses through nonrefundable tax credits.<sup>6</sup> The program’s certified businesses have realized over \$1 billion in total funding<sup>7</sup> and produced new jobs in the state.<sup>8</sup> Nevertheless, Wisconsin’s economy continues to sputter<sup>9</sup> and struggles to adapt to the “new

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Wisconsin has to make a meaningful commitment to state-sponsored incentives to remain competitive. *Id.* However, both of these opinions may have merit depending on the specific circumstances of a state. Ibrahim, *supra* note 2, at 723. For example, “Silicon Valley and Boston’s Route 128 sprang up organically.” *Id.* North Carolina’s Research Triangle Park was entirely planned by state and local government. *Id.* Austin, Texas, used a hybrid of these two models. *Id.*

4. 2003 Wisconsin Act 255, 2003 Wis. Sess. Laws 878 (2004) (implementing a government-sponsored tax credit program to incentivize investment in early-stage businesses).

5. CHRIS SCHIFFNER, WIS. ECON. DEV. CORP., ACT 255: EARLY STAGE BUSINESS INVESTMENT PROGRAM 2012 ANNUAL REPORT 3, 7 (2012), available at <http://inwisconsin.com/content/uploads/2013/02/2012-act-255-early-stage-annual-Report.pdf>.

6. *Id.*; WIS. ECON. DEV. CORP., INVESTING IN NEXT GENERATION OPPORTUNITIES IN WISCONSIN 1 (2013), available at [http://inwisconsin.com/wp-content/uploads/2013/07/WEDC\\_2013-QNBV-Report.pdf](http://inwisconsin.com/wp-content/uploads/2013/07/WEDC_2013-QNBV-Report.pdf). Neighboring states have replicated the QNBV program. SCHIFFNER, *supra* note 5, at 3 (stating that the QNBV program served as a model for Minnesota and Illinois); WIS. TECH. COUNCIL, THE FUTURE IS NOW: FOUR STRATEGIES FOR WISCONSIN’S HIGH-GROWTH ECONOMY 20–21 (2012), available at [http://www.wisconsintechcouncil.com/uploads/PDFs/2012\\_whitepaper.pdf](http://www.wisconsintechcouncil.com/uploads/PDFs/2012_whitepaper.pdf) (stating that numerous states have replicated the QNBV program, including Minnesota, Illinois, and Nebraska). The QNBV program is also referred to as either (1) the Act 255 investor tax credits or (2) Accelerate Wisconsin. SCHIFFNER, *supra* note 5, at 3. See *infra* note 45 and accompanying text for a discussion on the difference between refundable and nonrefundable tax credits.

7. WIS. ECON. DEV. CORP., *supra* note 6, at 1.

8. *Id.* at 5, 11 (stating that certified businesses under the QNBV program accounted for 1,102 full-time positions in 2012 with an average salary of \$76,581).

9. In March 2014, Wisconsin ranked 35th in private-sector job creation according to the U.S. Bureau of Labor Statistics. See, e.g., Mary Spicuzza, *On Politics: Wisconsin Ranks 35th in Job Creation, Federal Numbers Show*, WIS. ST. J., Mar. 20, 2014, at A3, available at [http://host.madison.com/wsj/news/local/govt-and-politics/on-politics/on-politics-wisconsin-ranks-th-in-job-creation-federal-numbers/article\\_7ee6bc89-39d0-5e8a-9fb8-b2749676227f.html](http://host.madison.com/wsj/news/local/govt-and-politics/on-politics/on-politics-wisconsin-ranks-th-in-job-creation-federal-numbers/article_7ee6bc89-39d0-5e8a-9fb8-b2749676227f.html) (stating that “Wisconsin continues to lag behind most Midwestern states, including Michigan, Minnesota, Ohio and Iowa”). In June 2013, Wisconsin ranked 37th in the nation in job creation over the previous 12 months. John Schmid & Kevin Crowe, *Quarterly Data Rank Wisconsin 37th in Private-Sector Job Growth*, MILWAUKEE J. SENTINEL, Dec. 18, 2013, <http://www.jsonline.com/business/quarterly-jobs-data-for-wisconsin-nation-set-to-be-released-b99165965z1-236368171.html> (calling Wisconsin a “chronic laggard” with respect to job growth). In 2013, Forbes named Wisconsin one of the worst states for business in its “The Best States for Business” ranking based on business costs, labor supply, regulatory environment, economic climate, growth prospects, and quality of life. *The Best States for Business and*

economy.”<sup>10</sup> While the QNBV program has helped capitalize many early-stage companies,<sup>11</sup> the state legislature should revisit the program and make substantive changes to better compete for investment capital and maximize Wisconsin’s entrepreneurial growth potential.<sup>12</sup>

The QNBV program, administered by the Wisconsin Economic Development Corporation (WEDC), has played a major role in changing the perception of Wisconsin in the capital world.<sup>13</sup> Prior to the program’s existence, investment capital for early-stage businesses was scarce.<sup>14</sup> The legislature passed the QNBV program to provide tax credits to investors who invest capital in Wisconsin’s early-stage businesses.<sup>15</sup> A decade

*Careers*, FORBES, <http://www.forbes.com/best-states-for-business> (last visited Oct. 11, 2014) (ranking Wisconsin 41st in the nation).

10. The “new economy” is defined as an emerging “global economy that is ever more dependent on knowledge and innovation for growth.” ATKINSON & STEWART, *supra* note 2, at 3. Wisconsin has struggled to adapt to the economy. *Id.* at 10–11 (ranking Wisconsin 31st in the nation in its “2012 State New Economy Index” that focuses on “to what degree . . . the structure of state economies match the ideal structure of the New Economy”); *see also* Ivey, *supra* note 3 (analyzing Wisconsin’s struggle with adapting to a changing global economy). One commentator believes the motto should be, “Start-ups, not bailouts: nurture the next Google, don’t nurse the old G.M.’s.” Thomas L. Friedman, *Start Up the Risk-Takers*, N.Y. TIMES, Feb. 21, 2009, [http://www.nytimes.com/2009/02/22/opinion/22friedman.html?\\_r=2&](http://www.nytimes.com/2009/02/22/opinion/22friedman.html?_r=2&).

11. WIS. ECON. DEV. CORP., *supra* note 6, at 2 (stating that 63 certified businesses received funding under the QNBV program in 2012).

12. *See infra* Part II for a discussion of the recommended substantive changes to the QNBV program.

13. “In the capital world, Wisconsin is a fly-over state . . . . A large part of that is perception. Act 255 is a major change from that perception.” Marv Balousek, *Banker: Encourage Investing in New Companies Expert Says at Capitol Hearing that Changes in State Law Are Needed*, WIS. ST. J. (Aug. 24, 2005, 12:00 AM), [http://host.madison.com/business/banker-encourage-investing-in-new-companies-expert-says-at-capitol/article\\_d2c58a4b-7265-5f74-9669-d768a5fd5bb4.html](http://host.madison.com/business/banker-encourage-investing-in-new-companies-expert-says-at-capitol/article_d2c58a4b-7265-5f74-9669-d768a5fd5bb4.html) (quoting Attorney Joe Hildebrandt from Foley & Lardner LLP); *see also* Steve Faulkner, *Wisconsin: Land of Beer, Cheese, and...Startups*, TECHCRUNCH (July 24, 2010), <http://techcrunch.com/2010/07/24/wisconsin-land-of-beer-cheese-and-startups/> (stating that “[m]ost people associate Wisconsin with cheese and beer, but you should think about adding startups to that list”); Jonathan Shieber, *For Tech Investors, The Midwest Is Flyover Country No More*, TECHCRUNCH (Mar. 17, 2014), <http://techcrunch.com/2014/03/17/for-tech-investors-the-midwest-is-flyover-country-no-more/> (stating that “[t]hese days, Midwestern entrepreneurs and investors are seeding more than just fields”); Tom Still, *Wisconsin and Midwest Slowly Finding Way on to Investors’ Radar Screens*, WIS. ST. J. (Mar. 22, 2014, 7:00 PM), [http://host.madison.com/business/tom-still-wisconsin-and-midwest-slowly-finding-way-on-to/article\\_4a740d43-d32a-5004-86cf-7718f0a89beb.html#ixzz2x87GhSjG](http://host.madison.com/business/tom-still-wisconsin-and-midwest-slowly-finding-way-on-to/article_4a740d43-d32a-5004-86cf-7718f0a89beb.html#ixzz2x87GhSjG) (stating that “[i]nvestors from Illinois, Minnesota and New York are increasingly showing up in deals in Wisconsin, especially around software companies and a variety of digital products.”).

14. *See infra* note 17 and accompanying text.

15. 2003 Wisconsin Act 255, 2003 Wis. Sess. Laws 878 (2004).

removed from the program's birth,<sup>16</sup> early-stage investments in Wisconsin businesses have substantially increased.<sup>17</sup>

Despite these early victories, Wisconsin has struggled to improve its business climate.<sup>18</sup> Historically, Wisconsin relied on the industrial sector to create jobs,<sup>19</sup> but these traditional industries have been disappearing from the state.<sup>20</sup> Wisconsin is equipped with the resources necessary to compete in new economy sectors,<sup>21</sup> but the state must make a "meaningful commitment to be competitive."<sup>22</sup> Recent legislation suggests that Wisconsin is beginning to make this "meaningful

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16. *Id.* The QNBV program was enacted in 2004 and took effect in 2005. *Id.* at 878, 883–84.

17. WIS. TECH. COUNCIL, WISCONSIN INVESTMENTS ON THE RISE: PUTTING RISK CAPITAL TO WORK 3 (2013), available at [http://www.wisconsinangelnetwork.com/uploads/WIportfolio\\_2013.pdf](http://www.wisconsinangelnetwork.com/uploads/WIportfolio_2013.pdf). In 2004, early-stage investments in Wisconsin totaled \$3.7 million from angel investors and \$55.4 million from venture capital. *Id.* In 2012, early-stage investments in Wisconsin totaled \$67.1 million from angel investors and \$95.2 million from venture capital. *Id.* In 2000, Wisconsin had two angel investment groups. Judy Newman, *Small Businesses Get Angelic Help Angel Investments on the Rise in Wisconsin*, WIS. ST. J. (Feb. 2, 2006, 12:00 AM), [http://host.madison.com/business/small-businesses-get-angelic-help-angel-investments-on-the-rise/article\\_1bf18bfa-d40e-5d36-8aa1-297af8679802.html](http://host.madison.com/business/small-businesses-get-angelic-help-angel-investments-on-the-rise/article_1bf18bfa-d40e-5d36-8aa1-297af8679802.html). In 2013, the Wisconsin Angel Network listed 32 angel groups on its website. WIS. ANGEL NETWORK, [http://wisconsinangelnetwork.com/WAN\\_Map/](http://wisconsinangelnetwork.com/WAN_Map/) (last visited Oct. 11, 2014). An "angel" is typically a wealthy investor who is an "accredited investor" under securities laws and invests personal funds in early-stage businesses. See Jill E. Fisch, *Can Internet Offerings Bridge the Small Business Capital Barrier?*, 2 J. SMALL & EMERGING BUS. L. 57, 73–74 (1998).

18. See *supra* note 9 and accompanying text.

19. See, e.g., Ivey, *supra* note 3 (stating that, for more than a century, Wisconsin relied on its industrial sector, including paper-making and production-line jobs).

20. For example, product-line jobs have moved abroad or to low-wage southern states, and the paper industry has declined due to a decreased demand for printing in a digital age. *Id.*

21. "Wisconsin has long possessed the basic ingredients to compete in the innovation economy, with the most glaring exception being sufficient venture capital to help its best start-up companies prosper and grow close to home." WIS. GROWTH CAPITAL COAL., BUILDING COMPANIES & JOBS: THE CASE FOR A VENTURE CAPITAL PROGRAM IN WISCONSIN 3 (2011), available at [http://www.wisconsintechcouncil.com/uploads/WGCC\\_BuildingCompanies\\_final.pdf](http://www.wisconsintechcouncil.com/uploads/WGCC_BuildingCompanies_final.pdf). For example, "[t]he Wisconsin Alumni Research Foundation ranked fourth for university biotechnology patents issued in the U.S. and Europe from 2008 to 2012." Jennifer Sereno, *WARF Biotech Patent Ranking Highlights UW-Madison Research Productivity*, U. WIS.-MADISON NEWS (July 10, 2013), <http://www.news.wisc.edu/21944>.

22. Ivey, *supra* note 3. "The new economy sectors are where there is the greatest opportunity for growth of high-paying jobs . . . . If we want to be a player, we need to make a meaningful commitment to be competitive." *Id.* (quoting John Neis, managing director of Venture Investors of Wisconsin).

commitment” and is amenable to making changes to the QNBV program.<sup>23</sup>

This Comment argues that the Wisconsin Legislature should update the QNBV program to attract investors that provide capital and resources to Wisconsin’s early-stage businesses.<sup>24</sup> Part I of this Comment generally discusses early-stage tax credit programs and specifically describes the background, provisions, and recent results of the QNBV program. Part II analyzes the substantive changes necessary for the QNBV program to maximize entrepreneurial growth in the state. These changes include (1) making the tax credits refundable to attract out-of-state investors, (2) providing additional tax credits for investments in accelerators nurturing certified businesses, (3) allowing early-stage businesses in restricted industries to rebut the presumption of disqualification from the QNBV program, and (4) providing additional tax credits for investments in specific industries. Finally, this Comment concludes that while an updated QNBV program will allow Wisconsin to remain competitive for early-stage investments, the program is only a portion of a more significant legal and cultural undertaking to create a community that mentors and invests in entrepreneurs.

#### I. EARLY-STAGE INVESTMENT PROGRAMS: WISCONSIN AND BEYOND

Many states view early-stage investment tax credits as a “win-win-win” because “[n]ew businesses get an infusion of capital, investors receive a tax credit, and the states see increased employment and innovation that enhance the local economy.”<sup>25</sup> Early-stage tax credits generally encourage investment in new business ventures with innovative

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23. See discussion *infra* pp. 1050–52.

24. This Comment does not assess the merits of tax credits for innovative investments. Wisconsin’s early-stage tax credit program will likely continue, and this Comment seeks to optimize its success.

25. David A. Hughes, *Angel Investment Tax Credits: A Win-Win-Win for Taxpayers, New Ventures, and the States*, J. MULTISTATE TAX’N & INCENTIVES, Nov.–Dec. 2010, at 10 (providing a survey of angel investment tax credit programs and describing variations among 23 states with a program). The Wisconsin Legislative Fiscal Bureau recently assessed early-stage investment credits in 22 total states. WIS. LEGISLATIVE FISCAL BUREAU, ANGEL INVESTMENT TAX CREDIT -- ELIMINATE MAXIMUM CREDIT LIMIT 15–23 (2013), available at <http://legis.wisconsin.gov/lfb/publications/budget/2013-15%20budget/documents/budget%20papers/281.pdf>. Studies indicate that business tax credits foster their targeted activities, but other studies reveal that at least some of those activities would have occurred in the absence of the credits. JENNIFER WEINER, NEW ENG. PUB. POLICY CTR., STATE BUSINESS TAX INCENTIVES: EXAMINING EVIDENCE OF THEIR EFFECTIVENESS 3 (2009), available at <http://www.bostonfed.org/economic/neppc/dp/2009/neppcdp0903.pdf>. Some studies state that tax credits simply shift money between states instead of raising the nationwide level of spending. *Id.*

technologies.<sup>26</sup> Under such a program, an investor can claim a state income tax credit equal to a percentage of the investment in a qualified early-stage business.<sup>27</sup>

Increasingly, states utilize early-stage tax credits to encourage economic development and job growth.<sup>28</sup> However, each state's program varies by what investments qualify for tax credits and how an investor is compensated.<sup>29</sup> In Wisconsin, an investment in a qualifying business qualifies for a 25 percent nonrefundable tax credit.<sup>30</sup> Part I will discuss state early-stage tax credit programs generally and then will offer details about Wisconsin's QNBV program.

#### *A. The General Framework for State-Sponsored Early-Stage Investment Programs*

Many states utilize early-stage tax credits to encourage economic development and job growth.<sup>31</sup> However, each state's specific approach is unique.<sup>32</sup> Although most terms vary from state to state, early-stage investment programs commonly differ in important aspects, including the types of businesses that qualify under the programs, the amount of tax credits given to investors, and whether out-of-state investors can benefit from the incentive.<sup>33</sup>

First, each state's early-stage tax credit program varies based on the types of businesses that qualify under the program.<sup>34</sup> States generally require the same qualifications to ensure that businesses are truly early-stage businesses and are located within the state.<sup>35</sup> However, each state varies based on the principal industry of the business allowed under

26. See Hughes, *supra* note 25, at 12.

27. *Id.* See, for example, *infra* notes 40–44 and accompanying text for examples of state statutes that authorize different amounts of tax credits as a percentage of the investment in a qualified early-stage business.

28. Hughes, *supra* note 25, at 12–13.

29. *Id.* at 17, 47.

30. WIS. STAT. § 71.07(5b)(b), (5d)(b) (2011–12).

31. Hughes, *supra* note 25, at 12–13.

32. *Id.* at 17, 47.

33. *Id.*

34. *Id.*

35. Early-stage tax credit programs typically require that a business has fewer than 25 to 100 employees, is predominantly located in the state giving the tax credits, has been operated for under 6 to 10 consecutive years, received under a certain threshold of prior equity capital investment, and received under a certain threshold of investments qualifying for tax credits. See, e.g., WIS. STAT. § 238.15(1) (2011–12); MINN. STAT. ANN. § 116J.8737(2)(c) (West 2014); 35 ILL. COMP. STAT. ANN. § 5/220(e) (West 2012 & Supp. 2014).

the program.<sup>36</sup> Some states create a narrowly defined focus of acceptable industries.<sup>37</sup> Other states allow businesses from a broader range of industries.<sup>38</sup> Most states define industries that automatically do not qualify for tax credits, including real estate, professional services, and banking.<sup>39</sup>

Second, states vary by the percentage of the investment that will qualify for tax credits.<sup>40</sup> The percentage of the investment qualifying for tax credits has ranged from 4%<sup>41</sup> to 100%.<sup>42</sup> Many states provide 25 %.<sup>43</sup>

36. Compare CONN. GEN. STAT. ANN. § 12-704d(a)(3) (West Supp. 2014) (stating that a business under the program must be “engaged in bioscience, advanced materials, photonics, information technology, clean technology or any other emerging technology as determined by the Commissioner of Economic and Community Development”), and KY. REV. ANN. § 154.20-254(17) (LexisNexis 2009) (stating that a business under the program must be engaged in “any industrial, manufacturing, mining, mining reclamation for economic development, commercial, health care, agricultural enterprise, or agribusiness activity”), with COLO. REV. STAT. ANN. § 24-48.5-112(g)(IV) (West Supp. 2013) (stating that a business under this 2010 pilot program must be engaged “primarily in research and development or manufacturing of new technologies, products, or processes”), and IND. CODE ANN. § 6-3.1-24-7(a)(2) (LexisNexis 2007 & Supp. 2014) (stating that a business under the program qualifies if it is “primarily focused on . . . the application of new technology” or the Indiana economic development corporation determines that the business has significant potential to bring substantial capital to the state, create jobs, diversify the business base in the state, or promote the purposes of the program in any other way). However, almost every program contains limiting language that disqualifies a business engaged in such activities as real estate, banking, insurance, and professional services. See, e.g., IND. CODE ANN. § 6-3.1-24-7(a)(5).

37. See, e.g., N.M. STAT. ANN. § 7-2-18.17K.(6)(b) (LexisNexis 2008 & Supp. 2013) (stating that a qualified business must engage “in high-technology research or manufacturing activities in New Mexico”).

38. See, e.g., IND. CODE ANN. § 6-3.1-24-7(a)(2) (allowing a business to qualify under the program if it promotes the purposes of the program in any way).

39. See, e.g., MINN. STAT. ANN. § 116J.8737(2)(c)(4) (stating that a business cannot qualify for the tax credit program if it is “engaged in real estate development, insurance, banking, lending, lobbying, political consulting, information technology consulting, wholesale or retail trade, leisure, hospitality, transportation, construction, ethanol production from corn, or professional services provided by attorneys, accountants, business consultants, physicians, or health care consultants”).

40. See, e.g., 35 ILL. COMP. STAT. ANN. § 5/220(b) (providing a 25% tax credit); MINN. STAT. ANN. § 116J.8737(5)(a)(1) (providing a 25% credit); R.I. GEN. LAWS § 44-63-2(a) (2013) (providing a 50% tax credit); VT. STAT. ANN. tit. 32, § 5830b(a) (2013) (providing a tax credit of the “lesser of four percent of the taxpayer's contribution or 50 percent of the taxpayer's tax liability”).

41. VT. STAT. ANN. tit. 32, § 5830b(a) (providing a tax credit of the “lesser of 4% of the taxpayer's contribution or 50 percent of the taxpayer's tax liability”).

42. HAW. REV. STAT. ANN. § 235-110.9(a), (k) (LexisNexis 2014) (providing a tax credit through 2010 that accumulated to 100% over five years).

43. See, e.g., MINN. STAT. ANN. § 116J.8737(5)(a)(1); WIS. STAT. § 71.07(5b)(b), (5d)(b) (2011–12).



Some states provide a higher credit for investments in specific industries under a tiered structure.<sup>44</sup>

Third, states vary by the compensation given to out-of-state investors by offering refundable and nonrefundable tax credits.<sup>45</sup> Most states offer nonrefundable credits for qualifying investments.<sup>46</sup> Out-of-state investors generally cannot use nonrefundable tax credits because the investor does not have tax liability within that state.<sup>47</sup> However, a few states, including Minnesota, offer refundable tax credits.<sup>48</sup> Because an out-of-state investor can claim the tax credits regardless of state tax liability, refundable tax credit programs attract a significant amount of out-of-state investments.<sup>49</sup>

### *B. Wisconsin's Early-Stage Investment Program*

In Wisconsin, the legislature enacted the QNBV program to drive equity investment in early-stage and high-tech businesses with the potential to significantly impact Wisconsin's economy.<sup>50</sup> Specifically, the program encourages investments in emerging companies that develop

44. See, e.g., ARIZ. REV. STAT. ANN. § 41-1518(E) (2011 & Supp. 2013) (providing a 30% tax credit with an additional 5% over three years if the business is located in a rural county or is a bioscience enterprise).

45. Compare MD. CODE ANN., TAX-GEN. § 10-725(d)(3) (LexisNexis 2013) (refundable tax credit), and MINN. STAT. ANN. § 116J.8737(5) (refundable tax credit), with 35 ILL. COMP. STAT. ANN. § 5/220(b) (West 2012 & Supp. 2014) (nonrefundable), and WIS. STAT. § 71.07(5b)(b), (5d)(b) (nonrefundable). Both refundable and nonrefundable tax credits reduce tax liability. I.R.S. Publ'n 17, 245 (2012), available at <http://www.irs.gov/pub/irs-pdf/p17.pdf>. If nonrefundable credits are more than the tax, the excess is not refunded to the taxpayer. *Id.* If refundable credits are more than the tax, the excess is refunded to the taxpayer. *Id.* Therefore, out-of-state investors generally do not benefit from nonrefundable tax credits because they do not have Wisconsin state income tax liability. *Id.*

46. See, e.g., 35 ILL. COMP. STAT. ANN. § 5/220(b); WIS. STAT. § 71.07(5b)(b), (5d)(b).

47. Nonrefundable credits can reduce tax, but if the total credits are more than the tax, the excess is not refundable to the taxpayer. I.R.S. Publ'n 17, 244 (describing nonrefundable tax credits under federal income tax).

48. See, e.g., MD. CODE ANN., TAX-GEN. § 10-725(d)(3); MINN. STAT. ANN. § 116J.8737(5). But see *infra* note 148 and accompanying text for a discussion on arguments against a refundable tax credit program.

49. MINN. STAT. ANN. § 116J.8737(5); see MINN. DEP'T OF EMP'T & ECON. DEV., MINNESOTA ANGEL TAX CREDIT PROGRAM 2012 ANNUAL REPORT 8 (2012), available at [http://mn.gov/deed/images/Angel\\_Tax\\_Credit\\_Program\\_Annual\\_Report\\_to\\_the\\_Legislature\\_2012.pdf](http://mn.gov/deed/images/Angel_Tax_Credit_Program_Annual_Report_to_the_Legislature_2012.pdf) (stating that 28% of the \$48 million qualifying for tax credits came from out-of-state investors).

50. SCHIFFNER, *supra* note 5, at 3. Lisa Johnson, Vice President of Entrepreneurship and Innovation at the WEDC, stated that the QNBV program "directs equity investments to a critical sector of Wisconsin's economy, one that will play a large role in creating future jobs: high growth seed and early-stage companies." *Id.* at 8.

new technologies, bring products to market, and provide high-quality jobs in Wisconsin.<sup>51</sup> Through statutory provisions<sup>52</sup> and administrative regulations,<sup>53</sup> the program effectuates these goals by specifying the types of investments that qualify for tax credits<sup>54</sup> and by requiring a state agency, the WEDC, to certify businesses receiving investments.<sup>55</sup> The annual reports by the WEDC indicate that the QNBV program has positively impacted Wisconsin's economy over the past decade.<sup>56</sup>

#### 1. LIMITS ON INVESTMENTS THAT QUALIFY FOR TAX CREDITS

The QNBV program authorizes two different types of tax credits.<sup>57</sup> First, the “angel investment credits” provide tax credits to eligible investors<sup>58</sup> making cash equity investments in certified businesses.<sup>59</sup> If an investor makes a “bona fide angel investment” in a certified business,<sup>60</sup> the investor will receive a nonrefundable state income tax credit equal to

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51. *Id.* at 7.

52. WIS. STAT. §§ 71.07(5b), (5d), 238.15(2) (2011–12).

53. The Wisconsin code authorizes the WEDC to implement the QNBV program. § 238.15. Currently, the WEDC's regulations for the QNBV program are not part of the Wisconsin Administrative Code and are only available on the WEDC website. *See* WIS. ECON. DEV. CORP., ENTREPRENEURSHIP & INNOVATION: EARLY STAGE BUSINESS INVESTMENT PROGRAM, <http://inwisconsin.com/content/uploads/2013/04/QNBV-policy-SB-3-27-2013.pdf> (last visited Oct. 12, 2014).

54. *See infra* Part I.B.1 for a discussion of the investments that qualify under the QNBV program.

55. *See infra* Part I.B.2 for a discussion of the businesses that qualify under the QNBV program.

56. *See infra* Part I.B.3 for a discussion of the reported results in the QNBV annual reports. Through the end of 2012, certified businesses in the QNBV program have attracted over \$916 million in capital. WIS. ECON. DEV. CORP., *supra* note 6, at 1, 3. In 2012, businesses currently in the QNBV program accounted for 1,102 full-time and 220 part-time jobs. *Id.* at 5. However, some have concerns over the accuracy of this data. *See infra* note 97.

57. § 71.07(5b) (authorizing the “early stage seed investment credit”); *id.* § 71.07(5d) (authorizing the “angel investment credit”).

58. WIS. ECON. DEV. CORP., *supra* note 53, at 1 (requiring that individual angel investors and investors in angel investment networks satisfy the U.S. Securities and Exchange Commission Accredited Investor definition at the time of the investment).

59. § 71.07(5d); *see also* SCHIFFNER, *supra* note 5 (summarizing the current QNBV program and presenting its impact on the state).

60. § 71.07(5d)(a) (defining a “bona fide angel investment” as “a purchase of an equity interest . . . made by . . . [a] person [or network of persons] who reviews new businesses or proposed new businesses for potential investment of the person's money”). The regulations define an “investment” as “the investment of cash in a qualified new business venture that is used for legitimate business purposes in exchange for . . . common stock, partnership or membership interest, preferred stock, or an equivalent ownership interest.” WIS. ECON. DEV. CORP., *supra* note 53, at 1.

25 percent of the investment.<sup>61</sup> An investor's basis for this credit is capped at \$2 million for each investment.<sup>62</sup> The aggregate amount of tax credits that may be issued for the angel investment tax credit program in a given calendar year is \$20 million.<sup>63</sup>

Second, the "early stage seed investment credits" provide the same tax benefits to certified venture funds<sup>64</sup> investing in certified businesses.<sup>65</sup> An investor in the fund will receive a tax credit equal to 25 percent of the investment in the fund,<sup>66</sup> unless the fund manager allocates the credits differently.<sup>67</sup> An investor can transfer credits to another person only under the early-stage seed investment program.<sup>68</sup> The

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61. § 71.07(5d)(b). A partnership or limited liability company making an investment may not claim the credit and must compute the proportionate tax credit for each of its partners or members. *Id.* § 71.07(5d)(c)3m. Originally, the tax credit was spread equally over a two-year period. *See* WIS. LEGISLATIVE COUNCIL, ACT MEMO: 2003 WISCONSIN ACT 255, at 2 (2004).

62. § 71.07(5d)(c)2. Initially, an investor's basis for this credit is capped at \$500,000 for each investment. *See* WIS. LEGISLATIVE COUNCIL, *supra* note 61, at 2.

63. WIS. STAT. § 238.15(3)(d) (2011–12). Initially, the aggregate amount of tax credits that could be issued in a given calendar year was \$3 million for the angel investment tax credit program. *See* WIS. LEGISLATIVE COUNCIL, *supra* note 61, at 2–3. Recently, the angel investment tax credit program was set to expire due to a \$47.5 million lifetime cap. WIS. LEGISLATIVE COUNCIL, ACT MEMO: 2011 WISCONSIN ACT 213, at 1 (2012); Wis. Angel Network, *Angel Tax Credit Cap Lifted as Part of Wis. Budget*, 30 FORWARD (July 1, 2013), <http://blog.wisconsinangelnetwork.com/2013/angel-tax-credit-cap-lifted-as-part-of-wis-budget/> (stating that \$36 million of the lifetime cap had been used through 2012). However, the lifetime cap was lifted after the 2013–2015 fiscal biennium budget was passed. A.B. 40, 2013–14 Leg. (Wis. 2013). The program only retains the annual limit. § 238.15(3)(d).

64. § 238.15(2). When certifying fund managers, the WEDC is required to consider the fund manager's experience in managing venture capital funds, the past performance of any funds managed by the fund manager, the size of the fund, and any other relevant factors. *Id.* Additionally, the WEDC must only certify fund managers that commit to investing in certified businesses. *Id.* The WEDC added evaluation criteria, including the fund manager's experience in investing in high growth and early-stage businesses, past performance of businesses assisted by the fund manager, geographic distribution of funds, industry focus, ability to access follow-on funding, services provided, commitment to Wisconsin, and administrative and management fees. WIS. ECON. DEV. CORP., *supra* note 53, at 3–4 (providing the QNBV program regulations). If a certified fund manager has principal offices outside of Wisconsin, the WEDC can require side-by-side investment with equity investors based in Wisconsin. *Id.* at 4.

65. § 71.07(5b); *see also* SCHIFFNER, *supra* note 5, at 7.

66. § 71.07(5b)(b)1.

67. *Id.* § 71.07(5b)(c). The tax credits are calculated at the fund manager level. *Id.* § 71.07(5b)(b)2. However, the fund manager's organizational documents can allocate tax credits contrary to the investor's proportionate ownership of the fund. *Id.* § 71.07(5b)(c).

68. § 238.15(3)(e). To transfer the credit, an investor has to notify the WEDC, provide documentation to the WEDC, and pay one percent of the total tax credits transferred. *Id.*; WIS. ECON. DEV. CORP., *supra* note 53, at 5. A credit cannot be transferred more than once in a 12-month period. § 238.15(3)(e).

aggregate amount of tax credits that may be issued for the early-stage seed investment tax credit program in a given calendar year is \$20.5 million.<sup>69</sup>

Both types of tax credits restrict the character of the investment.<sup>70</sup> An investor must invest cash in exchange for common stock, preferred stock, partnership or membership interest, or an equivalent.<sup>71</sup> However, the investment does not include cash exchanged for debt, unless it is later converted into one of the permitted ownership interests.<sup>72</sup> An investor cannot control more than 20 percent of the ownership interest in the business at the time of the investment.<sup>73</sup> After an investor receives tax credits, the WEDC may revoke the credits if the investment is not held for at least three years.<sup>74</sup> An investor does not have to repay the tax credits if an investment becomes worthless<sup>75</sup> or a bona fide liquidity event occurs during the three-year period.<sup>76</sup>

## 2. CERTIFICATION REQUIREMENTS FOR EARLY-STAGE BUSINESSES

To receive state income tax credit, an investor can only invest in qualified early-stage businesses.<sup>77</sup> The WEDC certifies businesses based on several requirements that serve the program's goal of driving equity investment in businesses with a potential to significantly impact

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69. § 238.15(3)(d). Initially, the aggregate amount of tax credits that could be issued in a given calendar year was \$3.5 million for the “early stage seed investment credits.” See WIS. LEGISLATIVE COUNCIL, *supra* note 61, at 2–3.

70. WIS. ECON. DEV. CORP., *supra* note 53, at 4.

71. *Id.*

72. *Id.*

73. *Id.* This requirement also applies if the investor is closely related to someone who controls more than 20 percent of the ownership interest in the business at the time of the investment. *Id.*

74. WIS. STAT. § 71.07(5b)(d)3. (2011–12) (stating that the minimum holding period for the “early stage seed investment credit” is three years); *id.* § 71.07(5d)(d)1. (stating that the minimum holding period for the “angel investment credit” is three years); WIS. ECON. DEV. CORP., *supra* note 53, at 5.

75. WIS. ECON. DEV. CORP., *supra* note 53, at 5. “Worthless” means that the company is deemed insolvent and has evidence of a “cessation of business or a sale of substantially all of the company’s assets to repay outstanding debts, bankruptcy or receivership filings.” *Id.* at 2.

76. WIS. STAT. § 238.15(3)(d) (2011–12); WIS. ECON. DEV. CORP., *supra* note 53, at 1, 5 (defining a “bona fide liquidity event” as either a “sale of a certified company or the majority of its assets which results in a payout to shareholders” or “the company’s shares begin trading on a public exchange”).

77. § 238.15(1) (requiring the WEDC to certify or recertify businesses if the business meets certain criteria). Initially, the statute required the Wisconsin Department of Commerce to certify businesses. See WIS. STAT. § 560.205 (2003–04) (initially codified under chapter 560); WIS. LEGISLATIVE COUNCIL, *supra* note 61, at 2.

Wisconsin's economy.<sup>78</sup> The WEDC can only certify a business if all of the following criteria are met: (1) the business is headquartered in Wisconsin,<sup>79</sup> (2) 51 percent of its employees are located in Wisconsin,<sup>80</sup> (3) it has under 100 employees at the time of certification,<sup>81</sup> (4) it has been in operation for not more than 10 consecutive years at the time of the initial certification,<sup>82</sup> (5) it has not received more than \$10 million in cash in aggregate private equity investment at the time of the initial certification,<sup>83</sup> and (6) it has not received more than \$8 million in investments that qualified for tax credits under the QNBV program for taxable years beginning after December 31, 2010.<sup>84</sup>

Further, the WEDC can only certify businesses with a potential for increasing jobs in Wisconsin, increasing capital investment in Wisconsin, or both.<sup>85</sup> To meet this requirement, a business must be engaged in innovation in specific high-tech industries<sup>86</sup> or be applying proprietary technology.<sup>87</sup> The WEDC cannot certify businesses primarily engaged in specific industries, including real estate development, banking, and professional services.<sup>88</sup>

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78. See *supra* note 50 and accompanying text.

79. § 238.15(1)(a).

80. *Id.* § 238.15(1)(b).

81. *Id.* § 238.15(1)(h).

82. *Id.* § 238.15(1)(j).

83. *Id.* § 238.15(1)(km).

84. *Id.* § 238.15(1)(L). In addition, the business cannot have received more than \$4 million in investments that qualified for tax credits under the QNBV program for taxable years beginning after December 31, 2007, and before January 1, 2011. *Id.* § 238.15(1)(kn). For taxable years prior to January 1, 2008, the business cannot have received more than \$1 million in investments that qualified for tax credits under the QNBV program. *Id.* § 238.15(1)(k).

85. *Id.* § 238.15(1)(f).

86. *Id.* § 238.15(1)(f)1.a.–b. A business is considered to be “engaging in innovation” if its primary activity is “manufacturing, biotechnology, nanotechnology, communications, agriculture, or clean energy creation or storage technology.” *Id.* § 238.15(1)(f)1.a. “Innovation” also includes “processing or assembling products, including medical devices, pharmaceuticals, computer software, computer hardware, semiconductors, any other innovative technology products, or other products that are produced using manufacturing methods that are enabled by applying proprietary technology.” *Id.* § 238.15(1)(f)1.b.

87. *Id.* § 238.15(1)(f)1.c. The WEDC’s QNBV policy defines “proprietary technology” as “a product or process that is marketed under exclusive legal right of the inventor or maker or is protected by secrecy, patent, trademark or copyright against free competition.” WIS. ECON. DEV. CORP., *supra* note 53, at 2. The definition also includes pre-commercialization activity related to proprietary technology. § 238.15(1)(f)2. Pre-commercialization activity includes “conducting research, developing a new product or business process, or developing a service that is principally reliant on applying proprietary technology.” *Id.*

88. *Id.* § 238.15(1)(g). Specifically, a business cannot be certified if it is primarily engaged in “real estate development, insurance, banking, lending, lobbying,

Beyond this objective review, the WEDC subjectively evaluates applications<sup>89</sup> to protect the program's goal of driving equity investment in businesses with a potential to significantly impact Wisconsin's economy.<sup>90</sup> The WEDC evaluates a business's targeted industry, growth potential, management team experience, financial need, barriers to entry, percentage of funds to be spent in Wisconsin, and innovative or novel ideas.<sup>91</sup> The WEDC does not publish information about application denials, so the extent of this evaluation is not entirely clear.<sup>92</sup>

Once approved by the WEDC, a business must agree not to relocate outside the state within three years of receiving an investment for which an investor may claim a tax credit.<sup>93</sup> A relocating business must repay all of the tax credits,<sup>94</sup> but this penalty is reduced if the business remains in state at least 12 months.<sup>95</sup> The legislature added this provision recently after several QNBV-certified businesses relocated out of state.<sup>96</sup>

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political consulting, professional services provided by attorneys, accountants, business consultants, physicians, or health care consultants, wholesale or retail trade, leisure, hospitality, transportation, or construction, except construction of power production plants that derive energy from a renewable resource." *Id.*

89. WIS. ECON. DEV. CORP., *supra* note 53, at 2–3.

90. *See supra* note 50 and accompanying text.

91. WIS. ECON. DEV. CORP., *supra* note 53, at 2–3.

92. *See infra* note 180 and accompanying text for a discussion about some of the ambiguities with the current QNBV certification process.

93. § 238.15(1)(m)1. A business “relocate[s] outside of this state” when 51% of the business’s employees, payroll, or activities of the headquarters, as determined by the WEDC, are located outside of Wisconsin. *Id.* “Headquarters” means the commercial business location where the business’s staff is physically employed and where the business’s “financial, personal, legal, planning, or other headquarters functions are handled.” WIS. ECON. DEV. CORP., *supra* note 53, at 1.

94. § 238.15(1)(m)2.

95. *Id.* § 238.15(1)(m)2.a.–c. A business relocating outside of Wisconsin must repay 100% of the tax credit if “relocation occurs less than 12 months after the investment,” 80% of the tax credit if relocation occurs 12 months or more but less than 24 months after the investment, and 60% of the tax credit if “relocation occurs . . . 24 months or more after the investment but less than 36 months after the investment.” *Id.*

96. *See* WIS. LEGISLATIVE COUNCIL, *supra* note 63, at 1. For example, the legislature wanted to stop promising Wisconsin early-stage businesses, like Brazen Careerist, Inc., from relocating out of state. *See, e.g.,* Penelope Trunk, *Brazen Careerist Opens an Office in DC*, PENELOPE TRUNK (Oct. 6, 2010), <http://blog.penelopetrunk.com/2010/10/06/brazen-careerist-opens-an-office-in-dc/> (describing the move of key personnel from Madison, Wisconsin, to a new office in Washington, D.C.). However, the WEDC does not publish information about the frequency of relocation for QNBV businesses.

## 3. IMPACT ON WISCONSIN'S ECONOMY

The WEDC asserts that the QNBV program has positively impacted Wisconsin's economy.<sup>97</sup> Through the end of 2013, certified businesses in the program have attracted over \$1 billion in total capital with \$269.1 million qualifying for tax credits.<sup>98</sup> Based on these investments, the program has distributed \$67.3 million in credits.<sup>99</sup>

Additionally, 180 businesses currently in the program had a total of 1,053 full-time and 245 part-time jobs in 2013.<sup>100</sup> Overall job creation is higher than this because the companies that are no longer in the QNBV program do not have an obligation to report to the WEDC.<sup>101</sup> The impact

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97. WIS. ECON. DEV. CORP., *supra* note 6, at 6 (stating that “few . . . states have achieved Wisconsin’s level of success of providing value to companies as well as taxpayers”). Some people question the neutrality of a report from a state agency or pseudo-state agency, which has an incentive to bolster the numbers. *See, e.g.*, GREG LEROY ET AL., GOOD JOBS FIRST, CREATING SCANDALS INSTEAD OF JOBS: THE FAILURES OF PRIVATIZED STATE ECONOMIC DEVELOPMENT AGENCIES, 11, 18–19 (2013), *available at* <http://www.goodjobsfirst.org/sites/default/files/docs/pdf/scandalsnotjobs.pdf>. Further, some question the WEDC’s integrity based on recent turmoil surrounding the agency. *Id.* at 11 (accusing the WEDC of mismanaging public money, making questionable subsidy awards, lacking adequate transparency, resisting accountability, ignoring conflicts of interest in awarding subsidies, giving WED executives lavish pay, and making questionable claims about job creation). The Wisconsin Legislature addressed the reporting controversies with the WEDC in 2013. *See* S.B. 205, 2013–14 Leg. (Wis. 2013); A.B. 228, 2013–14 Leg. (Wis. 2013) (making various changes to the WEDC and reporting requirements for economic development programs). However, other reports indicate that Wisconsin effectively monitors its business tax incentive programs. THE PEW CTR. OF THE STATES, EVIDENCE COUNTS: EVALUATING STATE TAX INCENTIVES FOR JOBS AND GROWTH 2 (2012), *available at* [http://www.pewtrusts.org/~media/legacy/uploadedfiles/wwwpewtrustsorg/reports/economic\\_mobility/PewEvaluatingStateTaxIncentivesReportpdf.pdf](http://www.pewtrusts.org/~media/legacy/uploadedfiles/wwwpewtrustsorg/reports/economic_mobility/PewEvaluatingStateTaxIncentivesReportpdf.pdf) (ranking Wisconsin as one of the top 13 “leading” states for the scope and quality of evaluation for its state tax incentive programs). While this Comment recommends specific substantive changes to the program, the Wisconsin Legislature must ensure that neutral and accurate data is collected to effectively evaluate if the program or these changes are working. *Id.* at 1 (stating that states with tax incentive programs must “produce and connect policy makers with good evidence of whether these tools deliver a strong return on taxpayer dollars”).

98. WIS. ECON. DEV. CORP., *supra* note 6, at 5.

99. *Id.*

100. *Id.* at 15.

101. WIS. ECON. DEV. CORP., DRIVING INVESTMENT TO HIGH-GROWTH BUSINESSES IN WISCONSIN 5 (2012), *available at* <http://inwisconsin.com/wp-content/uploads/2013/06/2012-QNBV-Report.pdf>. To effectively evaluate the QNBV program and these potential changes, quality data needs to go into all reporting. Thus, the WEDC and legislature should also consider adjustments to the reporting requirements for current and former businesses certified under the program. *See supra* note 97.

of the reported job creation is significant considering that the average QNBV business employs nine positions and expects to grow.<sup>102</sup>

However, the QNBV program has never used all of the credits authorized by the legislature.<sup>103</sup> Any remaining balance of available credits in a given year rolls over into the next year's available credit limit.<sup>104</sup> For example, over \$78 million in aggregate unallocated tax credits were rolled over and applied to the 2014 credit allocation.<sup>105</sup>

Since its enactment a decade ago, the QNBV program has helped to change the nation's perception of Wisconsin as a fly-over state when it comes to investable early-stage businesses.<sup>106</sup> However, even more can be done to improve entrepreneurial growth in the state.<sup>107</sup> With an economy struggling to rebound from economic recession<sup>108</sup> and a legislature willing to explore entrepreneurial programs in the state,<sup>109</sup> the timing is right to explore changes to the QNBV program.

## II. THE NEW QNBV PROGRAM: CHANGES TO IMPROVE WISCONSIN'S ENTREPRENEURIAL COMMUNITY

The Wisconsin Legislature should update the QNBV program to maximize entrepreneurial growth in the state, so as to realize economic and job growth. First, the tax credits under the QNBV program should be refundable for the state to benefit from out-of-state investors.<sup>110</sup> Second, the QNBV program should provide additional tax credits for investments in early-stage accelerators supporting qualifying businesses, because accelerators nurture early-stage businesses and contribute to their success.<sup>111</sup> Third, the QNBV program should create a rebuttable presumption of disqualification for an early-stage business in a restricted industry, allowing certification if the business meets the goals of the program.<sup>112</sup> Lastly, qualifying investments in specific industries should

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102. WIS. ECON. DEV. CORP., *supra* note 6, at 15 (stating that the employment figures have increased from six positions in 2007 to nine positions in 2013 on average).

103. *Id.* at 18.

104. *Id.* From 2009 to 2012, the WEDC transferred some of the unallocated balance in the QNBV program to the Jobs Tax Credit Program. *Id.*

105. *Id.* (stating that the "angel tax credit" had over \$42.3 million in rollover and the "early-stage seed credit" had over \$35.8 million in rollover applied to the 2014 credit allocation).

106. *See supra* note 13 and accompanying text.

107. *See infra* Part II.

108. *See supra* note 9 and accompanying text.

109. *See discussion infra* pp. 1050–52.

110. *See infra* Part II.A.

111. *See infra* Part II.B.

112. *See infra* Part II.C.



receive an additional tax credit because some industries are a core competency of the state, demonstrate a financial need, and have the potential for a significant payoff.<sup>113</sup>

#### *A. Refundable Tax Credits to Attract Out-of-State Investments*

First, the QNBV program should create a refundable tax credit structure<sup>114</sup> to provide incentives for out-of-state investors to invest in Wisconsin's early-stage businesses.<sup>115</sup> The current QNBV program offers nonrefundable tax credits that investors can use to reduce their Wisconsin tax liabilities.<sup>116</sup> However, most out-of-state investors, including large venture capital firms, do not have a Wisconsin tax liability and, thus, cannot take advantage of the QNBV program.<sup>117</sup> By providing refundable tax credits, the QNBV program would give businesses more financial resources and broader investor experiences not otherwise available in the state.<sup>118</sup>

Currently, the QNBV program limits early-stage investment opportunities for out-of-state investors<sup>119</sup> by ineffectively mimicking a refundable tax credit framework.<sup>120</sup> Under the early-stage seed investment portion of the QNBV program, an out-of-state investment fund can receive tax credits after investing "side by side with equity investors" located in Wisconsin.<sup>121</sup> The out-of-state fund can transfer or

113. See *infra* Part II.D.

114. See *supra* note 45 for a general discussion regarding refundable and nonrefundable tax credits. Alternatively, a system identical in substance could be implemented outside of the tax system. See, e.g., RICHARD SCHMALBECK & LAWRENCE ZELENAK, *FEDERAL INCOME TAXATION* 792 (3d ed. 2011).

115. See WIS. TECH. COUNCIL, *supra* note 6, at 22 (advocating that the Wisconsin Legislature change the QNBV program to provide refundable tax credits).

116. WIS. STAT. § 71.07(5b)(b)1. (2011–12) (stating that investors under the Early Stage Seed Investment Credit "may claim as a credit [equal to 25 percent of a bona fide angel investment] against the tax imposed under ss. 71.02 and 71.08, up to the amount of those taxes"); *id.* § 71.07(5d)(b) (stating that investors under the Angel Investment Credit "may claim as a credit [equal to 25 percent of a bona fide angel investment] against the tax imposed under s. 71.02 or 71.08, up to the amount of those taxes").

117. *Id.* § 71.07(5b)(b), (5d)(b) (providing a nonrefundable credit); see WIS. TECH. COUNCIL, *supra* note 6, at 22 ("Half of all investment is made by entities such as corporations or pension funds, not by individuals. The vast majority of investors in venture capital do not have a State of Wisconsin tax liability.").

118. See WIS. TECH. COUNCIL, *supra* note 6, at 22. But see *infra* note 148 for a discussion on arguments against a refundable tax credit program.

119. Compare MINN. STAT. ANN. § 116J.8737(5) (West 2014) (refundable tax credit), with WIS. STAT. § 71.07(5b)(b), (5d)(b) (nonrefundable).

120. WIS. STAT. § 238.15(3)(e); WIS. ECON. DEV. CORP., *supra* note 53, at 5.

121. See WIS. ECON. DEV. CORP., *supra* note 53, at 4.

sell credits to another individual.<sup>122</sup> To transfer the credit, the fund has to notify the WEDC, provide documentation to the WEDC, and pay one percent of the total tax credits transferred.<sup>123</sup> A credit cannot be transferred more than once in a 12-month period.<sup>124</sup>

While the QNBV program gives an option for out-of-state investors to receive a “tax credit,” this option is financially and administratively unworkable. First, the QNBV program does not extend this option to out-of-state angel investors, only to investment funds.<sup>125</sup> Angel investors are important because they provide a significant amount of capital to early-stage businesses.<sup>126</sup> Second, the fund must locate a willing buyer with Wisconsin tax liability.<sup>127</sup> If the fund locates a willing buyer, the fund will likely discount the tax credit sale compared to the full value realized by the Wisconsin taxpayer.<sup>128</sup> Third, if the fund is able to secure a buyer, it must abide by the reporting requirements and pay an administrative fee.<sup>129</sup> While reporting requirements can prevent unscrupulous behavior, a refundable tax credit would eliminate additional barriers, allow out-of-state investors to receive a tax credit directly from the state and, thus, increase the potential for investment in Wisconsin businesses.<sup>130</sup>

When seeking early-stage investments, Wisconsin start-ups directly compete with start-ups from neighboring states and, thus, compete with

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122. § 238.15(3)(e); WIS. ECON. DEV. CORP., *supra* note 53, at 5.

123. § 238.15(3)(e); WIS. ECON. DEV. CORP., *supra* note 53, at 5.

124. § 238.15(3)(e).

125. *See id.*; WIS. ECON. DEV. CORP., *supra* note 53, at 5.

126. JEFFREY SOHL, CTR. FOR VENTURE RESEARCH, THE ANGEL INVESTOR MARKET IN Q1Q2 2013: A SUSTAINABLE GROWTH CONTINUES 1 (2013), *available at* <http://paulcollege.unh.edu/sites/paulcollege.unh.edu/files/Q1Q2%202013%20Analysis%20Report.pdf> (stating that angel investments in the United States totaled \$9.7 billion for the first half of 2013 with 38 percent of this in seed and start-up stage businesses).

127. *See* WIS. TECH. COUNCIL, *supra* note 6, at 22 (“The 2009 program enhancements allow investment credits received by venture capital funds to be transferable to a Wisconsin taxpaying party.”).

128. *Id.*

129. § 238.15(3)(e); WIS. ECON. DEV. CORP., *supra* note 53, at 5. Refundable credits would eliminate these additional reporting requirements because the out-of-state investor could follow the same process as currently followed by in-state investors. *See, e.g.*, WIS. ECON. DEV. CORP., PROCESS FOR REQUESTING INVESTMENT TAX CREDITS, *available at* <http://inwisconsin.com/entrepreneurs-and-innovators/programs/qualified-new-business-venture/> (select “How to request investment tax credits” under “Resources and Forms for Investors and Certified Companies”) (providing the documentation needed for an investor to receive tax credits under the QNBV program).

130. *See, e.g.*, MINN. STAT. ANN. § 116J.8737(5)(a) (West 2014) (refundable tax credit). An investor might fund an early-stage business with significant growth potential regardless of refundable credits or administrative burdens. However, the state of Wisconsin’s economy implies that barriers to growth should be eliminated. *See supra* note 9 and accompanying text.

neighboring states' tax credit programs.<sup>131</sup> For example, the Minnesota Angel Tax Credit Program offers more favorable terms to out-of-state investors than the QNBV program.<sup>132</sup> An out-of-state investor would recognize a 25% discount for an investment in a Minnesota start-up<sup>133</sup> compared to no direct discount for an investment in a Wisconsin start-up.<sup>134</sup> By making the QNBV program's tax credits refundable, Wisconsin start-ups would at least be on an equal playing field with similarly situated Minnesota start-ups.<sup>135</sup>

Additionally, a more competitive QNBV program would attract financial and non-financial resources for Wisconsin start-ups that would not otherwise be available in the state.<sup>136</sup> Under the Minnesota Angel Tax Credit Program, Minnesota start-ups have realized substantial investments from out-of-state investors.<sup>137</sup> In 2012, 28% of the \$48 million qualifying for the Minnesota Angel Tax Credit Program were from out-of-state investors.<sup>138</sup> If Wisconsin could obtain similar

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131. See WIS. TECH. COUNCIL, *supra* note 6, at 22.

132. MINN. STAT. ANN. § 116J.8737(5); see WIS. TECH. COUNCIL, *supra* note 6, at 22 (discussing the advantages of the Minnesota Angel Tax Credit Program for out-of-state investors). After copying Wisconsin's QNBV program almost verbatim, Minnesota sweetened the pot for investors by adding refundable credits. *Id.*

133. MINN. STAT. ANN. § 116J.8737(5). "If the amount of the credit under this section for any taxable year exceeds the claimant's liability for tax under this chapter, the commissioner shall refund the excess to the claimant." MINN. STAT. ANN. § 290.0692(4) (West 2014).

134. WIS. STAT. § 71.07(5b)(b), (5d)(b) (2011–12). As discussed, the out-of-state investor can sell the Wisconsin tax credits. WIS. STAT. § 238.15(3)(e). However, this option is administratively and financially unworkable. See WIS. TECH. COUNCIL, *supra* note 6, at 22.

135. Compare MINN. STAT. ANN. § 116J.8737(5) (refundable tax credit), with WIS. STAT. § 71.07(5b)(b), (5d)(b) (nonrefundable). Unlike the other recommendations in this Comment, refundable tax credits are a "keeping up with the Joneses" approach when compared to Minnesota. While Wisconsin should avoid a bidding war for investor capital, nothing indicates that the "war" has reached this point. Whether or not these changes are ever made, the state must evaluate quality data about the program to ensure the state is realizing a positive return on its investment. See *supra* note 97 and accompanying text.

136. "The vast majority of investors in venture capital do not have a State of Wisconsin tax liability. Providing an incentive for these investors brings fresh capital into Wisconsin that would not otherwise find its way into the state." WIS. TECH. COUNCIL, *supra* note 6, at 22. The Wisconsin Technology Council focuses on increasing capital for Wisconsin start-ups but does not address the intangibles that come with this capital.

137. See MINN. DEP'T OF EMP'T AND ECON. DEV., *supra* note 49, at 8.

138. *Id.* Nationally, angel investors tend to invest in their home states. See SILICON VALLEY BANK, ANGEL RES. INST., HALO REPORT: ANGEL GROUP UPDATE 11 (2013), available at [http://www.svb.com/uploadedFiles/Content/Blogs/Halo\\_Report/halo-report-q2-2013.pdf](http://www.svb.com/uploadedFiles/Content/Blogs/Halo_Report/halo-report-q2-2013.pdf) (stating that 72% of angel investments in Q2 2013 were made by an angel residing in the same state as the business). While angel investors tend to invest

results,<sup>139</sup> Wisconsin start-ups would benefit from a larger pool of investors who would bring additional capital, better financing terms, more options to select the best strategic investor, and a bigger network of resources for entrepreneurs.<sup>140</sup>

However, not all of Wisconsin's neighbors offer refundable tax credits.<sup>141</sup> For example, Illinois offers investors a 25% nonrefundable tax credit with provisions nearly identical to the QNBV program.<sup>142</sup> While the QNBV program is competitive with the Illinois program on paper,<sup>143</sup> the Chicago start-up environment organically attracts investors and does not require as much government subsidy to spur early-stage growth.<sup>144</sup> For example, 76% of venture capital investment in Illinois businesses

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in their home state, over 25% of angel investments are out-of-state, giving Wisconsin an opportunity to capture this capital. *See id.*

139. As in Minnesota, a higher percentage of out-of-state angel investors may contribute to increased venture capital financing for more mature start-ups. Both the Wisconsin and Minnesota early-stage programs each attracted just under \$50 million in angel investments made in businesses qualifying for tax credits in 2012. *See* MINN. DEP'T OF EMP'T AND ECON. DEV., *supra* note 49, at 4 (attracting \$46.2 million in investments made in businesses qualifying for tax credits in 2012); WIS. ECON. DEV. CORP., *supra* note 101, at 10 (attracting \$48.4 million in investments made in businesses qualifying for tax credits in 2012). Additionally, Wisconsin and Minnesota have nearly identical workforce sizes with 2.36 and 2.41 million, respectively. *Legislative Success*, WIS. GROWTH CAPITAL COAL., <http://wisconsininvests.com/legislation/> (last visited Oct. 12, 2014). However, Minnesota businesses have attracted \$327 million in venture capital investments over the past five years compared to \$72 million for Wisconsin businesses. *Id.* (stating that 19% of Minnesota's work force is attributed to venture capital compared to 3% in Wisconsin). With a similar workforce size, Wisconsin has to do something to close this significant gap.

140. *See generally* PAUL A. GOMPERS & JOSH LERNER, *THE MONEY OF INVENTION* 41–59 (2001) (summarizing the benefits of venture capital investors). “In today's entrepreneurial environment, finding the right financier is a key element of building a sustainable enterprise.” *Id.* at 41.

141. *See* 35 ILL. COMP. STAT. ANN. § 5/220(b) (West 2012 & Supp. 2014) (providing a 25% nonrefundable tax credit); IOWA CODE § 15E.43(2) (West 2011 & Supp. 2014) (providing a 20% nonrefundable tax credit).

142. 35 ILL. COMP. STAT. ANN. § 5/220(b).

143. *See, e.g.*, SCHIFFNER, *supra* note 5, at 3 (stating that Illinois' early-stage tax credit program was modeled after Wisconsin's QNBV program).

144. In 2012, Chicago ranked as the ninth largest metro area in the United States receiving venture capital investment. Richard Florida, *America's Leading Metros for Venture Capital*, ATLANTIC CITY LAB (June 17, 2013), <http://www.theatlanticcities.com/jobs-and-economy/2013/06/americas-top-metros-venture-capital/3284/> (summarizing data from the National Venture Capital Association). Chicago accounted for 2% of the nation's venture capital investment dollars or \$546 million. *Id.*

came from out-of-state investors in 2010,<sup>145</sup> indicating that a refundable tax credit program is not needed.<sup>146</sup>

In 2011, the Wisconsin Legislature attempted to update the QNBV program to include refundable credits and failed,<sup>147</sup> but the current legislature is in a position to revisit the issue. While the reasons for the initial failure are not well documented, one can speculate that the legislature was concerned with the budget crisis, wanted to retain incentives only for Wisconsin residents, or believed the transferability of credits under the current QNBV program was sufficient.<sup>148</sup> However, several changes since 2011 indicate that the legislature may be willing to revisit this issue.

First, the legislature's concerns with the budget were well placed,<sup>149</sup> but a refundable tax credit does not increase the program's cost because

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145. Nat'l Venture Capital Ass'n, *Venture Capital and Entrepreneurship in Illinois* (2011), [http://www.nvca.org/index.php?option=com\\_docman&task=doc\\_download&gid=740&Itemid=93](http://www.nvca.org/index.php?option=com_docman&task=doc_download&gid=740&Itemid=93) (see slide six of the PowerPoint presentation).

146. While larger markets may have a natural advantage over the Wisconsin market, business tax incentives can help to even the playing field. *See supra* note 25 and accompanying text. Thus, the legislature must make a meaningful commitment to change, especially when Illinois has a bigger market in Chicago and the same early-stage program as Wisconsin. *See supra* note 22 and accompanying text.

147. A.B. 20, 100th Leg., 1st Sess. (Wis. 2011); *see* BACK TO WORK WISCONSIN SPECIAL SESSION 1 (Sept. 2011), *available at* <http://www.wisbusiness.com/1008/large/110928specialsession.pdf> (stating that a "refundable [credit] will make investing in [businesses certified under the QNBV program] even more attractive, particularly to out-of-state investors, increasing overall investment in early stage businesses").

148. Refundable tax credits are used throughout the federal and state tax systems. *See, e.g.*, 26 U.S.C. § 32 (2012) (authorizing the Earned Income Tax Credit, which is refundable); WIS. STAT. § 238.16 (2011–12) (authorizing the Jobs Tax Credit, which is refundable). While many view refundable tax credits as "an essential element of any tax system that attempts to promote socially valued activities," some people generally oppose refundable tax credits. *See* Lily L. Batchelder, Fred T. Goldberg, Jr. & Peter R. Orszag, *Efficiency and Tax Incentives: The Case for Refundable Tax Credits*, 59 STAN. L. REV. 23, 65–72 (2006) (detailing potential objections to refundable tax credits generally). First, opponents to refundable tax credits argue for a pure tax system. *Id.* at 65–66. Specifically, they believe that the government should not redistribute wealth between income groups and that the tax system should only be used to raise revenues. *Id.* Second, opponents argue that refundable tax credits increase administration costs and could be susceptible to fraud or abuse. *Id.* However, these arguments are objections to tax incentives generally. *Id.* at 66. Further, the administrative costs and fraud concerns are unpersuasive because these risks exist throughout the tax system and are a small price to pay for an efficient mechanism to drive socially valued activities. *Id.* at 67–72.

149. In 2011, Wisconsin struggled to correct a budget shortfall through a controversial bill that gutted collective bargaining rights for most public employees. Martin H. Malin, *Life After Act 10?: Is There A Future for Collective Representation of Wisconsin Public Employees?*, 96 MARQ. L. REV. 623, 631, 633–34 (2012). In light of this legislation, the proposed amendments to the QNBV program may have been a victim of priority compared to the Act 10 controversy.

the program has a yearly cap<sup>150</sup> and rolls over a significant amount of unused credits every year.<sup>151</sup> Unlike in 2011, the state now realizes a budget surplus<sup>152</sup> and, thus, may be more receptive to programs that appear to spend more money. Second, the legislature recently passed a \$25 million state-sponsored investment fund for later stage start-ups, indicating an interest in entrepreneurialism and a strong possibility of reviving the refundable tax credit issue.<sup>153</sup> Third, the legislature recently eliminated the lifetime cap on the QNBV program, indicating a willingness to make adjustments to the program.<sup>154</sup>

Wisconsin benefits from out-of-state capital by growing businesses<sup>155</sup> and creating jobs in the state.<sup>156</sup> The QNBV program helps to ensure that these businesses and jobs stay in Wisconsin by requiring that qualifying businesses be headquartered in the state.<sup>157</sup> While out-of-state investors have a limited option to transfer tax credits,<sup>158</sup> refundable tax credits are a better option to attract out-of-state investments and maximize early-stage growth in Wisconsin.<sup>159</sup>

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150. WIS. STAT. § 238.15(3)(d) (stating that the aggregate amount of tax credits that may be issued for the “angel investment credit” and the “early stage seed investment credit” programs in a given calendar year is \$20 million and \$20.5 million, respectively); see WIS. TECH. COUNCIL, *supra* note 6, at 22.

151. See discussion *supra* pp. 1045–46.

152. Matthew DeFour, *State Revenues Projected to be More than \$900 Million Better than Expected*, WIS. ST. J. (Jan. 17, 2014, 9:00 AM), [http://host.madison.com/wsj/news/local/govt-and-politics/state-revenues-projected-to-be-more-than-million-better-than/article\\_55e9ff04-529d-5e9e-9e83-0e146c8e9047.html](http://host.madison.com/wsj/news/local/govt-and-politics/state-revenues-projected-to-be-more-than-million-better-than/article_55e9ff04-529d-5e9e-9e83-0e146c8e9047.html) (reporting that, if Wisconsin does not change anything, the state would have a \$1 billion surplus by 2017).

153. WIS. LEGISLATIVE COUNCIL, ACT MEMO: 2011 WISCONSIN ACT 41, at 1 (2013).

154. See *supra* note 63 and accompanying text.

155. WIS. ECON. DEV. CORP., *supra* note 6, at 1, 4, 15.

156. In 2013, 180 businesses currently in the program had a total of 1,053 full-time and 245 part time jobs. *Id.* at 15. Actual job creation is higher than this because the companies that are no longer in the QNBV program do not have an obligation to report to the WEDC. WIS. ECON. DEV. CORP., *supra* note 101, at 5. The impact of the reported job creation is significant considering that the average QNBV business employs nine positions and expects to grow. WIS. ECON. DEV. CORP., *supra* note 6, at 15.

157. WIS. STAT. § 238.15(1)(m)1. (2011–12). A business seeking certification under the QNBV program must agree not to relocate outside the state within three years of receiving an investment for which an investor may claim a tax credit. *Id.* A business “relocates out of this state” when 51 percent of the business’s employees, payroll, or activities of the headquarters, as determined by the WEDC, are located outside of Wisconsin. *Id.* A relocating business must repay all or a portion of the tax credits. *Id.* § 238.15(1)(m)2. Additionally, businesses incur additional costs from moving an established business, including the cost of physically moving the business and business interruption. Mark Henricks, *How to Relocate Your Business*, ENTREPRENEUR, <http://www.entrepreneur.com/article/81406> (last visited Oct. 12, 2014).

158. § 238.15(3)(e); WIS. ECON. DEV. CORP., *supra* note 53, at 5.

159. See WIS. TECH. COUNCIL, *supra* note 6, at 22.

*B. Additional Tax Credits for Investments in Accelerators  
That Nurture Early-Stage Businesses*

Second, the QNBV program should provide additional tax credits for investments in accelerators that nurture qualified early-stage businesses.<sup>160</sup> An accelerator holds a business's hand through the start-up phase by providing early-stage investment, mentoring services, and support services to help launch businesses.<sup>161</sup> Similarly, an incubator provides support services to younger businesses, but an accelerator differs because it also provides investment and generally focuses solely on very early-stage businesses.<sup>162</sup> Many view an accelerator as a critical partner in the success of an early-stage business because some entrepreneurs lack the business skills to get an idea to market.<sup>163</sup> Accelerators provide early-stage businesses with necessary resources and, thus, produce quality early-stage investments.<sup>164</sup> Currently,

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160. Currently, investments in accelerators only qualify for a 25 percent tax credit to the extent the investment is in qualifying businesses. WIS. STAT. § 71.07(5d) (2011–12) (authorizing tax credits for “a partnership or limited liability company that is a nonoperating entity”).

161. See David Mielach, *Business Incubators and Accelerators: Here's the Big Difference*, BUSINESSNEWS DAILY (Jun. 19, 2013, 11:22 AM), <http://www.businessnewsdaily.com/4658-business-incubator-accelerator-difference.html>.

162. An incubator is a business support service that provides entrepreneurs with resources, including “management guidance, technical assistance and consulting tailored to young growing companies.” *What Is Business Incubation?*, NAT'L BUS. INCUBATION ASS'N, [http://www.nbia.org/resource\\_library/what\\_is/index.php](http://www.nbia.org/resource_library/what_is/index.php) (last visited Oct. 12, 2014). Incubators generally charge a monthly fee for the service. Mielach, *supra* note 161. An accelerator is similar to an incubator, but it provides early-stage investment and support services to help “birth” the company. *Id.* Accelerator participants usually graduate from a three- or four-month program, and incubator participants stay for a longer period of time. *Id.* Both incubators and accelerators aim to improve the overall success of an early-stage business. *Id.* For the purposes of this Comment, an “accelerator” is a company that also provides capital investment in early-stage businesses and defined support services beyond office space and general services.

163. See generally Dani Fankhauser, *The Pros and Cons of Startup Accelerators*, MASHABLE.COM (June 11, 2013), <http://mashable.com/2013/06/11/startup-accelerator-growth/> (discussing the advantages and disadvantages of accelerators).

164. TechStars, one of the leading accelerators, states that over 89 percent of the 266 businesses that completed its program are still active or have been acquired. *Stats: Techstars Delivers the Best Results*, TECHSTARS, <http://www.techstars.com/companies/stats/> (last visited Oct. 12, 2014). The Techstar-graduating businesses have created 3,422 jobs and received an average of \$1.8 million in funding per business. TECHSTARS, <http://www.techstars.com> (last visited Oct. 12, 2014); see also Peter Relan, *90% of Incubators and Accelerators Will Fail And That's Just Fine for America and the World*, TECHCRUNCH (Oct. 14, 2012), <http://techcrunch.com/2012/10/14/90-of-incubators-and-accelerators-will-fail-and-why-thats-just-fine-for-america-and-the-world/> (stating that accelerators are good for the United States, even though 90 percent of accelerators will fail). But see Jared Konczal, *Evaluating the Effects of Accelerators? Not So Fast*, FORBES (Aug. 8, 2012, 5:39 PM), <http://www.forbes.com/sites/kauffman/2012/08/08/evaluating->

accelerator activity in Wisconsin is relatively low, and an increased tax incentive would attract more accelerator activity in the state<sup>165</sup> without increasing the cost of the QNBV program.<sup>166</sup>

Other states acknowledge the value of offering support services to young companies through incentives related to incubators.<sup>167</sup> For example, Missouri offers a 50 percent tax credit for contributions to approved incubators.<sup>168</sup> The purpose of the program is “[t]o generate private funds to be used to establish a ‘protective business environment’ (incubator) in which a number of small businesses can collectively operate, fostering growth and development during a business’ start-up period.”<sup>169</sup> To qualify for early-stage tax credits in Arkansas, a business

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the-effects-of-accelerators-not-so-fast/ (stating that a handful of successful accelerators skew the statistics regarding the success of accelerator programs).

165. Gener8tor, the only significant accelerator in the state, has graduated 26 early-stage companies and currently provides participating businesses \$70,000 and “12-weeks of mentorship-driven programming.” See GENER8TOR, <http://www.gener8tor.com> (last visited Oct. 12, 2014). Gener8tor is trying to attract venture capital that is traditionally tied to the east and west coasts. See Dan Reich, *Innovation and Investment Dollars Turn to a New Region: The Midwest*, FORBES, (June 4, 2013, 9:53 AM), <http://www.forbes.com/sites/danreich/2013/06/04/innovation-and-investment-dollars-turn-to-a-new-region-the-midwest/>. Gener8tor also attracts early-stage businesses from across the United States and internationally. See, e.g., DRIBLET, <http://driblet.co>, (last visited Oct. 12, 2014) (relocating from Mexico to participate in the Gener8tor program). The Wisconsin Economic Development Corporation oversees a Seed Accelerator program, which “provides grants to eligible communities and other organizations to support a pre-seed business model program that incorporates training, mentoring and financial assistance to entrepreneurs in their area.” See *Seed Accelerator*, WISCONSIN ECON. DEV. CORP., <http://inwisconsin.com/entrepreneurs-and-innovators/programs/seed-accelerator/> (last visited Oct. 12, 2014). While this program identifies that accelerators increase the potential for entrepreneurial success, the state can breed more growth by focusing capital on accelerators.

166. This added tax credit does not increase the program’s cost because the program has a yearly cap. WIS. STAT. § 238.15(3)(d) (2011–12) (stating that the aggregate amount of tax credits that may be issued for the “angel investment credit” and the “early stage seed investment credit” programs in a given calendar year is \$20 million and \$20.5 million, respectively); see WIS. TECH. COUNCIL, *supra* note 6, at 22. Also, the QNBV program never used all of the credits authorized by the legislature. See discussion *supra* pp. 1045–46.

167. See, e.g., ARK. CODE ANN. § 15-4-3303(a)(2)(B)(iv) (LexisNexis 1987 & Supp. 2013); MO. ANN. STAT. § 620.495 (West 2014).

168. MO. ANN. STAT. § 620.495.2(2) (defining an incubator as “a program in which small units of space may be leased by a tenant and in which management maintains or provides access to business development services for use by tenants or a program without infrastructure in which participants avail themselves of business development services to assist in the growth of their start-up small businesses”).

169. *Small Business Incubator Tax Credit*, MISSOURI DEPARTMENT ECON. DEV., <http://www.ded.mo.gov/BCS%20Programs/BCSProgramDetails.aspx?BCSProgramID=79> (last visited Oct. 12, 2014).



must satisfy any two requirements from a list of six.<sup>170</sup> One of these requirements states that “[t]he business is supported by [a] business incubator[.]”<sup>171</sup> While these examples are for incubators, the accelerators offer cash investments with similar or better support and mentoring services.<sup>172</sup>

Under this proposed addition, the QNBV program would grant additional tax credits to accelerators and not incubators because of the investment component of the support. The current QNBV program is structured around equity investments, providing tax credits to qualifying angel investors and investment funds.<sup>173</sup> Tax credits associated with an accelerator are arguably a better investment for Wisconsin because the accelerator is holding the start-up’s hand through the process.<sup>174</sup> Many angel investors do not provide such a service.<sup>175</sup> Thus, the QNBV program should further incentivize accelerators, who provide these intangible services, to help grow early-stage businesses in Wisconsin. By increasing accelerator mentorship, the QNBV program will positively impact Wisconsin’s economy by better positioning the state’s early-stage businesses for success.

### *C. Rebuttable Presumption of Disqualification for Early-Stage Businesses in Restricted Industries*

Third, the QNBV program should allow an early-stage business in a restricted industry to rebut the presumption of disqualification to ensure that all innovative early-stage businesses receive tax credit support. To receive tax credits, the current QNBV program requires an early-stage business to have “the potential for increasing jobs in this state, increasing

170. ARK. CODE ANN. § 15-4-3303(a)(2)(B).

171. *Id.* § 15-4-3303(a)(2)(B)(iv); ARK. CODE ANN. § 26-51-815(d)(2)(D) (LexisNexis 1987 & Supp. 2013) (defining an incubator as “a business incubator certified by the Board of Directors of the Arkansas Science and Technology Authority as being a facility operated in cooperation with an Arkansas college or university to foster the growth of technology-based enterprises”).

172. *See supra* note 162 and accompanying text.

173. WIS. STAT. § 71.07(5b)(b), (5d)(b) (2011–12).

174. *See* Fankhauser, *supra* note 163 (stating that accelerators can be helpful to entrepreneurs because the partners running the programs “have seen the 10,000 horrible things that can happen to startups”) (quoting Garry Tan from Y Combinator).

175. GOMPERS & LERNER, *supra* note 140, at 10 (noting that “[m]any angel investors may be nothing more than wealthy local doctors, dentists, or businesspeople who have a strong desire to ‘make a fortune.’ Many are also naïve about the potential conflicts that can arise and are potentially easy prey for unscrupulous entrepreneurs. On the other hand, some angel investors can provide value to the firm and are critical to its success because of their previous experience building and managing entrepreneurial firms.”).

capital investment in this state, or both.”<sup>176</sup> Even if a business satisfies this goal, the QNBV program disqualifies a business if it is in one of the restricted industries.<sup>177</sup> However, the QNBV program should not disqualify an early-stage business based on a broad categorical exclusion and should give it an opportunity to rebut the disqualification so as to prove that it meets the goals of the program.<sup>178</sup>

The QNBV program should certify early-stage business in the excluded industries if the business significantly promotes the goals of the program to increase jobs in the state, increase capital investment in the state, or both.<sup>179</sup> This change still raises a suspicion for qualifying a traditional financial advisory firm, for example, because the firm may be included under banking, lending, or accounting. However, the change avoids any ambiguities by allowing the firm to rebut a presumption of disqualification and prove that it promotes the purposes of the QNBV program.<sup>180</sup> The exclusion was likely implemented because the excluded

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176. WIS. STAT. § 238.15(1)(f).

177. *Id.* § 238.15(1)(g) (stating that the industries not qualifying for tax credits under the QNBV program include “real estate development, insurance, banking, lending, lobbying, political consulting, professional services provided by attorneys, accountants, business consultants, physicians, or health care consultants, wholesale or retail trade, leisure, hospitality, transportation, or construction, except construction of power production plants that derive energy from a renewable resource”).

178. *Id.* § 238.15(1)(f) (“It has the potential for increasing jobs in this state, increasing capital investment in this state, or both . . .”).

179. *Id.* Most states retain similar industry restrictions to Wisconsin’s QNBV program. *See, e.g.*, 35 ILL. COMP. STAT. ANN. § 5/220(e)(4) (West 2012 & Supp. 2014); MINN. STAT. ANN. § 116J.8737(2)(c)(4) (West 2014). Indiana contemplates taking an approach similar to the proposed changes to the QNBV program. IND. CODE ANN. § 6-3.1-24-7(a)(2) (LexisNexis 2007 & Supp. 2014). The Indiana program states that a qualifying business must be “primarily focused on professional motor vehicle racing, commercialization of research and development, technology transfers, or the application of new technology.” *Id.* However, the Indiana program also states that a business qualifies if the Indiana economic development corporation determines that the business has a significant potential to bring capital to the state, create jobs, diversify the business base in the state, or promote the purpose of the program. *Id.* Despite this encouraging sign, the Indiana statute later excludes the standard industries, such as real estate, insurance, and retail sales. *Id.* § 6-3.1-24-7(a)(5). Nevertheless, Indiana still certifies some industries outside the scope of the program if the program’s goals are met. *Id.* § 6-3.1-24-7(a)(2).

180. The ambiguities in the current QNBV program are illustrated by Alice.com, Inc., a defunct start-up company based in Middleton, Wisconsin that created an online marketplace to sell consumer packaged goods online. *Alice.com*, CRUNCHBASE, [www.crunchbase.com/organization/alice-com](http://www.crunchbase.com/organization/alice-com) (last visited Oct. 12, 2014) (“Alice.com will be an open, online retail platform for consumer packaged goods, focused primarily on linking manufacturers of essential household stuff like tooth brushes, toilet paper, trash bags etc. to end consumers directly.”). The WEDC qualified Alice.com for the QNBV program. SCHIFFNER, *supra* note 5, at 12 (listing Alice.com as a qualified business under the QNBV program). Alice.com raised over \$18 million in early-stage funding and employed approximately 30 employees. Judy Newman, *Middleton-Based Alice.com Is*

industries generally do not produce innovative, high-growth start-ups.<sup>181</sup> However, exceptions exist that justify any increased burden to administering a rebuttable presumption.

A hypothetical using a past Internet darling may help illustrate the case for a rebuttable presumption. Mint.com in its infancy probably would not have qualified under the current QNBV program, despite its innovative product offering. Mint.com allows users to track bank, credit card, investment, and loan transactions through a single interface and create household budgets and goals based on this aggregated data.<sup>182</sup> Mint.com generates revenue through lead generation in which the website recommends personalized financial products to its users.<sup>183</sup> Mint.com raised \$32 million in early-stage capital before selling to Intuit for \$170 million.<sup>184</sup>

The current QNBV program appears to exclude Mint.com under banking, lending, or accounting services.<sup>185</sup> However, Mint.com also

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*Closed — at Least for Now — and Under Receivership*, WIS. ST. J. (Sept. 4, 2013, 10:45 AM), [http://host.madison.com/wsj/business/middleton-based-alice-com-is-closed-at-least-for-now/article\\_67b7e06b-129d-5022-ab94-673e28d0c31d.html](http://host.madison.com/wsj/business/middleton-based-alice-com-is-closed-at-least-for-now/article_67b7e06b-129d-5022-ab94-673e28d0c31d.html) (reporting that Alice.com had 30 employees in 2011 before filing for receivership in 2013); Judy Newman, *Alice.com Gets Another Financial Boost*, WIS. ST. J. (Jan. 31, 2012, 6:00 AM), [http://host.madison.com/wsj/business/alice-com-gets-another-financial-boost/article\\_d7490c04-4b91-11e1-b02e-001871e3ce6c.html](http://host.madison.com/wsj/business/alice-com-gets-another-financial-boost/article_d7490c04-4b91-11e1-b02e-001871e3ce6c.html) (reporting that Alice.com raised \$18.2 million in total financing by early 2012). While Alice.com satisfied the purpose of the QNBV program by attracting capital investment and creating jobs, the current statutory language should exclude qualification of a business selling toilet paper and toothpaste online. WIS. STAT. § 238.15(1)(g) (restricting qualification for businesses in the “retail trade”). The proposed change to the QNBV program clarifies the program’s qualification procedures and ensures that similarly situated companies to Alice.com are also qualified under the program.

181. See, e.g., WIS. ECON. DEV. CORP., *supra* note 53, at 2 (stating the goal of the QNBV program).

182. *Your Financial Life, All in One Place*, MINT.COM, <https://www.mint.com/what-is-mint/> (last visited Oct. 12, 2014) (“Mint pulls all your financial accounts into one place. Set a budget, track your goals and do more with your money, for free!”).

183. *Mint.com*, CRUNCHBASE, <http://www.crunchbase.com/organization/mint> (last visited Oct. 12, 2014) (“Mint.com also tries to save users money by suggesting ways to save that are personalized and objective. The company claims that users are presented with an average of \$1,000 in savings opportunities in their first session.”).

184. See Michael Arrington, *Intuit to Acquire (Former TechCrunch50 Winner) Mint for \$170 Million*, TECHCRUNCH (Sept. 13, 2009), <http://techcrunch.com/2009/09/13/intuit-to-acquire-former-techcrunch50-winner-mint-for-170-million/>.

185. See WIS. STAT. § 238.15(1)(g). Under the current QNBV program, other Internet darlings like PayPal may not qualify under the QNBV program because they are primarily engaged in banking or investing. See PAYPAL, <https://www.paypal.com> (last visited Oct. 12, 2014). Priceline.com may not qualify because it is primarily engaged in leisure and hospitality. See PRICELINE.COM, <https://www.priceline.com> (last visited Oct. 12, 2014). Legal Zoom may not qualify because it provides self-help services traditionally performed by a law firm. See LEGALZOOM, <https://www.legalzoom.com> (last visited Oct. 12, 2014).

appears to satisfy the purpose of the QNBV program because of its innovative offering and potential to increase capital investment and jobs in the state.<sup>186</sup> By creating a rebuttable presumption for excluded industries, the QNBV program would unambiguously give Mint.com an opportunity to qualify even if the business is categorized under banking, lending, or accounting services, and Wisconsin would minimize the risk of leaving a good investment on the sideline without increasing the cost of the QNBV program.<sup>187</sup>

*D. General Tax Credit with Added Incentives for  
Investments in Specific Industries*

Lastly, the QNBV program should provide additional state income tax credits to qualifying investments in specific industries. The current QNBV program offers a blanket 25% tax credit for qualifying investments.<sup>188</sup> Other states have developed tiered systems to promote general early-stage innovation and target strategic core-competencies of the state.<sup>189</sup> The QNBV program should adopt this tiered structure (1) to provide all qualifying investments with a 25% tax credit and (2) to provide qualifying investments in specific industries with an additional tax credit, so as to encourage investment in those industries specifically.

By providing a higher tier tax credit for investments in specific industries, the QNBV program can be more attractive to investors in these industries without costing the state more money. The proposal has the potential to catch Midwest investors' attention because Illinois, Minnesota, and Iowa all offer a blanket tax credit of 25% or less.<sup>190</sup> This added tax credit does not increase the program's cost because the

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186. See § 238.15(1)(f).

187. This added tax credit does not increase the program's cost because the program has a yearly cap. *Id.* § 238.15(3)(d) (stating that the aggregate amount of tax credits that may be issued for the "angel investment credit" and the "early stage seed investment credit" programs in a given calendar year is \$20 million and \$20.5 million, respectively); see WIS. TECH. COUNCIL, *supra* note 6, at 22. Also, the QNBV program never used all of the credits authorized by the legislature. See discussion *supra* pp. 1045–46.

188. WIS. STAT. § 71.07(5b)(b), (5d)(b) (2011–12).

189. See, e.g., ARIZ. REV. STAT. ANN. § 41-1518(E) (2011 & Supp. 2013) (providing a 30% tax credit with an additional 5% if the business is located in a rural county or is a bioscience enterprise); ARIZ. COMMERCE AUTH., "ANGEL INVESTMENT" SMALL BUSINESS CAPITAL INVESTMENT INCENTIVE, <http://www.azcommerce.com/assets/AngelInvestment1.pdf> (stating that the purpose of the higher tier is to "expand early stage investments in targeted Arizona small businesses").

190. 35 ILL. COMP. STAT. ANN. § 5/220(b) (West 2012 & Supp. 2014) (providing a 25% tax credit); IOWA CODE § 15E.43(2) (West 2011 & Supp. 2014) (providing a 20% tax credit); MINN. STAT. ANN. § 116J.8737(5) (West 2014) (providing a 25% tax credit).

program has a yearly cap.<sup>191</sup> Also, the QNBV program never used all of the credits authorized by the legislature.<sup>192</sup>

For example, Wisconsin's biotechnology sector possesses the characteristics worthy of a higher tier tax credit.<sup>193</sup> First, the University of Wisconsin-Madison has helped to establish biotech as a core competency of the state through a high production of patents.<sup>194</sup> Second, early-stage biotech firms have a unique financial need because of the time and cost to take a discovery to market.<sup>195</sup> Lastly, biotech firms have the potential to create a significant number of high-paying jobs.<sup>196</sup> While biotech is an ideal candidate for the higher tier tax credits, the legislature should assess other industries based on core competency, need, and return on investment to identify other candidates for this treatment.<sup>197</sup>

#### CONCLUSION:

#### BY UPDATING THE QNBV PROGRAM, WISCONSIN CAN ENCOURAGE ENTREPRENEURIAL GROWTH AND IMPROVE A STRUGGLING ECONOMY

While the QNBV program has changed the perception of Wisconsin in the capital world<sup>198</sup> and has positively impacted the state,<sup>199</sup> the

191. WIS. STAT. § 238.15(3)(d) (stating that the aggregate amount of tax credits that may be issued for the “angel investment credit” and the “early stage seed investment credit” programs in a given calendar year is \$20 million and \$20.5 million, respectively); *See* WIS. TECH. COUNCIL, *supra* note 6, at 22.

192. *See* discussion *supra* pp. 1045–46.

193. *See, e.g.*, WIS. GROWTH CAPITAL COAL., *supra* note 21, at 15–16 (advocating for state-sponsored investment in biotechnology); Sergei Kouzmine, *Why VCs Should Stop Investing in 'Internet' Startups and Start Investing in 'Tech'*, VENTUREBEAT (Dec. 17, 2013), <http://venturebeat.com/2013/12/17/vc-risk-technology/> (stating that early-stage investors should focus on “academics, scientists, and research centers — the places where the real, down-and-dirty innovation is happening”).

194. The Wisconsin Alumni Research Foundation, or WARF, ranked fourth for university biotech patents issued in the United States and Europe from 2008 to 2012. *See* Sereno, *supra* note 21.

195. *See, e.g.*, WIS. GROWTH CAPITAL COAL., *supra* note 21, at 16 (stating that federal patent backlogs and FDA regulations are part of the reason biotech firms need early-stage investments). While some programs exist to help meet the financial need, more can be done. *See, e.g.*, *Discovery to Product*, UNIV. OF WIS.-MADISON, <http://d2p.wisc.edu/about/faq/> (last visited Oct. 12, 2014) (creating a \$1.6 million fund to help University of Wisconsin-Madison faculty and students transform “ideas and discovery into companies and products to bolster Wisconsin's economy”).

196. *See, e.g.*, WIS. GROWTH CAPITAL COAL., *supra* note 21, at 16 (stating that the average Wisconsin tech job pays nearly twice the statewide per capita average).

197. The current statute identifies some industries, including “manufacturing, biotechnology, nanotechnology, communications, agriculture, or clean energy creation or storage technology,” that could serve as a starting point to determine if any other industries deserve the higher tier tax credit. WIS. STAT. § 238.15(1)(f)1.a. (2011–12).

198. *See supra* note 13 and accompanying text.

legislature should substantively change the QNBV program to maximize entrepreneurial growth in the state. The proposed changes include: (1) making the tax credits refundable,<sup>200</sup> (2) providing additional tax credits for investments in accelerators nurturing certified businesses,<sup>201</sup> (3) allowing early-stage businesses in restricted industries to rebut the presumption of disqualification from the program,<sup>202</sup> and (4) supplementing the general tax credit for investments in specific industries.<sup>203</sup> If the legislature maintains the status quo, Wisconsin will struggle to improve a poor economy<sup>204</sup> and adapt to the “new economy.”<sup>205</sup>

However, these proposed changes to the QNBV program are only a small portion of a comprehensive plan to build Wisconsin’s entrepreneurial community, grow jobs, and improve the state’s economy.<sup>206</sup> First, Wisconsin must fully address the financial needs of businesses beyond the initial rounds of financing.<sup>207</sup> While the legislature has recently addressed this issue by passing a \$25 million fund, more work is needed.<sup>208</sup> Second, Wisconsin must embrace favorable statutory,

199. Through the end of 2013, certified businesses in the QNBV program have attracted over \$1 billion in capital. WIS. ECON. DEV. CORP., *supra* note 6, at 5. In 2013, businesses currently in the QNBV program accounted for 1,053 full-time and 245 part-time jobs. *Id.* at 15.

200. *See supra* Part II.A.

201. *See supra* Part II.B.

202. *See supra* Part II.C.

203. *See supra* Part II.D.

204. *See supra* note 9 and accompanying text.

205. *See supra* note 10 and accompanying text.

206. *See generally* *Legislative Priorities*, WIS. GROWTH CAPITAL COAL., <http://wisconsinvests.com/legislative-priorities/> (last visited Oct. 12, 2014) (recommending changes to Wisconsin law to promote entrepreneurialism in the state); WIS. TECH. COUNCIL, *supra* note 6, at 22.

207.

States with low rates of company formation and low levels of venture capital investment tend to lag their peers in job creation. This is the case in the State of Wisconsin, which is in the bottom five states in new company formation and the bottom third in venture capital investment on a per capita basis.

KEGONSA CAPITAL PARTNERS, FUND OF FUNDS: A MONEY FOR MINNOWS STRATEGY TO INCREASE JOB CREATION IN WISCONSIN, <http://kegonsapartners.com/money-for-minnows-fund-of-funds.html> (last visited Oct. 12, 2014). Wisconsin has 1.84% of the nation’s population and 2.11% of the nation’s patent filings, but its companies only have 0.55% of the nation’s venture capital investment. WIS. GROWTH CAPITAL COAL., *supra* note 21, at 9. Venture capital is essential to grow a business beyond its early stage. GOMPERS & LERNER, *supra* note 140, at 21 (stating that “[90%] of new entrepreneurial businesses that don’t attract venture capital fail within three years”).

208. *See supra* note 153 and accompanying text.

tax, and securities laws to create a nurturing environment for early-stage businesses and investors.<sup>209</sup>

Lastly, Wisconsin must build an entrepreneurial culture—a significant but achievable undertaking.<sup>210</sup> While arguably risk averse,<sup>211</sup> Wisconsin has the resources to build successful businesses.<sup>212</sup> To capitalize on these resources, the state must create more programs that help bring products to market<sup>213</sup> and truly embrace entrepreneurialism.<sup>214</sup> With every meaningful change to the QNBV program and beyond, Wisconsin moves forward, reflecting the state's continuous drive to be a national leader.<sup>215</sup>

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209. For example, Wisconsin could consider changing its pro-employer non-compete agreement laws to encourage the free flow of ideas and promote innovation. *See, e.g.*, Norman D. Bishara, *Covenants Not to Compete in a Knowledge Economy: Balancing Innovation from Employee Mobility Against Legal Protection for Human Capital Investment*, 27 BERKELEY J. EMP. & LAB. L. 287, 297–99 (2006) (discussing generally the effects of government policy on human capital and trade secrets in the context of non-compete contract clauses); Jeremy Hitchcock, *Competing Against Non-Competes*, INC.COM (Dec. 19, 2013), <http://www.inc.com/jeremy-hitchcock/competing-against-non-competes.html> (discussing the importance of eliminating non-compete agreements to promote the free flow of ideas).

210. Some people claim that Midwesterners are risk averse and not entrepreneurial. Frank E. Samuel, Jr., *A Venture Capital Strategy for the Great Lakes*, CHICAGO COUNCIL GLOBAL AFF. (Mar. 2010), [http://www.thechicagocouncil.org/UserFiles/File/PolicyBrief\\_VentureCapitalFS.pdf](http://www.thechicagocouncil.org/UserFiles/File/PolicyBrief_VentureCapitalFS.pdf). However, entrepreneurs and ideas exist in the region. *Id.* “What’s lacking is an environment that makes the most of their daring ideas.” *Id.*

211. *Id.*

212. *See supra* note 21 and accompanying text.

213. *See, e.g.*, WIS. GROWTH CAPITAL COAL., *supra* note 206 (advocating for an “entrepreneur-in-residence” program to help turn ideas into marketable products). The state and University of Wisconsin–Madison have created some programs, but more work is needed. *See, e.g.*, *Discovery to Product*, *supra* note 195 and accompanying text.

214. “It’s about having a pool of entrepreneurs, getting them together and creating a climate where good ideas can take off.” Ivey, *supra* note 3 (quoting Rob Atkinson, president of the Information Technology and Innovation Foundation). Building an entrepreneurial community extends to everyone in the community. *Id.* For example, Kentucky established a program to get high school students excited about entrepreneurialism. *Id.*

215. STATE OF WIS., WISCONSIN BLUE BOOK 2013–14, at 950 (2013) (stating that “Forward” became Wisconsin’s official state motto in 1851).