

Angel Investing Activity in Wisconsin in 2005

Prepared by

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Executive Summary:

This report examines angel investing activity in Wisconsin in 2005. Using data from the Wisconsin Department of Commerce and a survey by NorthStar Economics Inc., the report examines reported angel investing by individual angels and by organized angel groups.

Overall reported angel investing in Wisconsin in 2005 was over \$19 million. Of this amount, approximately \$14 million of angel investments came from individual angel investors and over \$5 million came from organized angel groups.

For the first time, thanks to data related to Act 255, we are able to get a partial picture of individual angel investing in Wisconsin. According to data reported under Act 255, individual angels invested nearly \$14 million in angel deals in 2005.

The number of group angel investing deals and dollars invested increased substantially in 2005 when compared to 2004. The dollars amount of group investing increased 65% to \$5,587,496 while the number of deals more than doubled from 9 in 2004 to 20 in 2005.

Angel investors took full advantage of available angel tax credits in 2005. Individual angels and angel groups were allocated \$3,000,000 in angel tax credits in 2005. That was the maximum amount available for angel investments in calendar year 2005.

Act 255 has helped to create a positive climate for angel investing in Wisconsin. Though it is difficult to isolate the effect of Act 255, feedback from angel investors indicates that the availability of angel tax credits and certified new business ventures has helped to increase the number of angel deals and the focus on angel investing in Wisconsin.

Acknowledgments:

We would like to acknowledge the cooperation and support of individuals and organizations that made this report possible.

Data from this report came from several sources. The Wisconsin Department of Commerce supplied data with respect to Act 255 investments. Data on angel group investments came from contact persons in the active angel groups based in Wisconsin.

Financial support for this project was provided by the Wisconsin Department of Financial Institutions.

We also wish to acknowledge the help of the Wisconsin Angel Network and the Wisconsin Technology Council in scoping out this report.

We wish to thank all of these parties for their help and support.

Report Terms and Conditions:

This report was prepared based upon data from reports to the Wisconsin Department of Commerce and survey responses to NorthStar Economics. NorthStar has relied on these data sources and takes full responsibility for the editorial content and data calculations contained in the report.

This report is based upon Wisconsin Department of Commerce data related to Act 255 and a survey by NorthStar Economics, Inc. of active angel groups in Wisconsin. We believe that this data captures the vast majority of angel group investments and a significant portion of individual angel investments. While we do not anticipate many changes in the data, it is possible that additional information from 2005 angel deals may yet be recorded in early 2006. If that is the case, we think that any additional data reported is likely to increase the reported investment amounts and the number of deals.

Introduction:

The purpose of this report is to gather and analyze data related to angel investing in Wisconsin in 2005. More specifically, the report will deal with the following:

- An estimate of the overall level of angel investing activity in Wisconsin in the calendar year 2005.
- Analysis of that data to estimate the angel activity that resulted from the investments of individual angel investors and the angel activity that resulted from organized groups of angel investors.
- Analysis of the year over year trend in group angel activity by Wisconsin-based angel groups.
- Analysis of the impact of Wisconsin Act 255 on angel investing activity in 2005.

Angel investing is generally associated with start-up and very new companies who are at the seed or early stage. Generally, angel investors fill the gap between the seed stage and early stage investing of founders, family and friends and the later stage investing of venture capitalists.

In recent years, angel investing has rivaled total venture capital investing in the United States. The Center for Venture Research at the University of New Hampshire estimates that angel investing in 2004 was greater than venture capital investing in the same period. Table 1 summarizes the data reported by the Center for Venture Research.

Table 1 Estimates of Total Venture Capital and Angel Investing in the U.S. in the Period 2002-2004

Year	Venture Capital Investing	Business Angel Investing
2002	\$21.2 Billion	\$15.7 Billion
2003	\$18.2 Billion	\$18.1 Billion
2004	\$20.9 Billion	\$22.5 Billion

Source: The Center for Venture Research

Limitations on the Analysis of Angel Investing Activity:

There is no central data collection point for angel investments in Wisconsin or in the United States. The best existing source of U.S. data is the Center for Venture Research at the University of New Hampshire. The Center tracks angel investing by organized angel groups through a system of periodic contacts with angel groups.

For this study, we have attempted to gather data for Wisconsin group angel investments and for individual angel investments. As we explain in the methodology, angel

investments are private financial deals and are not reported in any systematic manner. We believe that we have gathered a very large percentage of the angel activity in Wisconsin but undoubtedly there is some angel activity, especially related to individual angel investments, that does not get reported. Thus the data reported here likely understates actual angel investing in Wisconsin. Put another way, the data reported here is a conservative estimate of total angel investing in Wisconsin.

Methodology:

Data for this project was gathered from several sources. Data related to angel investing in projects that qualified for the Wisconsin Angel Tax Credit (as authorized in Wisconsin Act 255) was obtained from the Wisconsin Department of Commerce. Data related to organized group angel investing was obtained through phone interviews with representatives of the active angel groups located in Wisconsin. NorthStar Economics, Inc. of Madison Wisconsin compiled historical data on angel investing in the period 2000-2004 through phone interviews and available angel investment documentation for that period. Finally, information on a handful of angel deals was available from articles in the press and on the Wisconsin Technology Network.

Data from the NorthStar survey and data from the Wisconsin Department of Commerce data were matched to sort out any duplication in reporting. This was done for both the number of deals and the angel investment amount. In both cases, there were duplications between the NorthStar survey and the Department of Commerce data related to Act 255.

The information from press articles was also matched against both data sources and in each case the deal reported in the press was matched to either the Commerce Department or NorthStar survey data.

Angel Investing in Wisconsin in 2005

Based upon the data sources shown above, it appears that total angel investing in 2005 in Wisconsin businesses exceeded \$19 million dollars.

Table 2 Total Reported Angel Investing and Angel Deals in Wisconsin in 2005

	Commerce Department Data	NorthStar Survey Data	Totals net of Duplicate Reports
Investment Amount	\$15,550,042	\$5,360,000	\$19,569,883
Number of Deals	29	18	40

Sources: Wisconsin Department of Commerce and NorthStar Economics, Inc.

The figures in Table 2 show the reported angel deals and dollars invested in Wisconsin in 2005. The numbers are derived by matching the Commerce data against the NorthStar survey data to get the net number of deals and the amount of angel investments. Based upon this methodology, the total reported angel investing in Wisconsin companies in 2005 was \$19,569,883. The total numbers of reported deals (defined as separate financing events) was 40.

We think that the total number of deals and the total amount of angel investment in Wisconsin in 2005 may be understated. The totals reported in Table 2 are based upon data from the Wisconsin Commerce Department and survey data compiled by NorthStar Economics. The Commerce data relates to investments qualifying for angel tax credits under Act 255. The NorthStar data covers organized angel group investing in Act 255 certified companies as well as investments in companies that don't qualify for Act 255 tax credits. What is missing is individual angel investments in companies that don't qualify for Act 255 tax credits. Those individual angel investors may be Wisconsin residents or they may be individuals who reside in other states and countries.

The NorthStar data shows that about \$1,340,159 worth of the reported angel group investments qualified for the Act 255 credit. That means that angel groups invested approximately \$4 million in deals that did not qualify for the Act 255 credit. Prior experience with group angel investing data would suggest that individual angels also invested in deals not covered by Act 255 reporting.

Individual and Group Angel Investing

Much attention has been paid to the rapid growth in the formation of angel investing groups in Wisconsin. In the year 2000, the first two angel groups in Wisconsin formed in Madison, Wisconsin. In early 2006, there were thirteen angel groups that have completed the formation stage and another 6-7 in the process of forming up.

But long before organized angel groups, individual angels were actively engaged in investing in start up companies. The data collected by the Wisconsin Department of Commerce and the NorthStar Survey suggest that individual angel investments are at least 3 to 4 times larger than the total investments of organized angel groups. Table 3 contains an estimate of group and individual angel investments in Wisconsin companies in 2005.

Table 3 Group and Individual Angel Investments in 2005:

Investments by Individual Angels	\$13,982,387
Investments by Organized Angel Groups	\$ 5,587,496
Total Reported Angel Investing	\$19,569,883

Source: Wisconsin Department of Commerce and NorthStar Economics, Inc.

Trends in Organized Angel Group Investing

Angel Group investing in 2005 far outpaced the number of deals and dollars invested in each of the three prior years. Table 4 shows the breakdown of angel deals and dollars invested in the period 2002-2005.

Table 4 Group Angel Deals and Investment in the Period 2002-2005

Year	Deals	Amount Invested
2002	10	\$1,545,000
2003	9	\$1,638,000
2004	9	\$3,392,500
2005	20	\$5,587,496

Sources: NorthStar Survey; Department of Commerce Data; NorthStar Angel Investment Database;

Investing by angel groups in 2005 was 65% higher than investment in 2004. Equally important was the fact that the number of angel deals more than doubled from 2004 to 2005.

The Impact of Act 255 on Angel Investing in Wisconsin

The Wisconsin Department of Commerce is responsible for administering much of the process for determining and certifying qualified new business ventures that are eligible for angel tax credits and awarding the tax credits to individual angels and organized angel groups. In 2005, over 40 companies were certified as qualified new business ventures.

Angel tax credits first became available on January 1, 2005. The State of Wisconsin allocated \$3,000,000 in angel tax credits and established rules and regulations governing those credits. The entire \$3,000,000 allocation of angel tax credits for 2005 has been used up as the result of over \$12,000,000 in eligible angel investment deals.

It should be noted that investing by organized angel groups (reported in Table 3) nearly doubled in 2005 and about a quarter of those investments qualified for angel tax credits.

The impact of Act 255 is difficult to determine precisely. Angel tax credits and the process surrounding them are very new to Wisconsin angel investors. The lack of prior year individual angel investment data makes it difficult to gauge the year over year increase or decrease in individual angel investments. The impact of tax credits on the willingness of individual angels to invest in a deal is likely to vary from investor to investor.

It does appear however that Act 255 has had a positive effect on angel investing and the climate for angel investing. Some of the positive effects of Act 255 include the following:

- Act 255 has drawn a useful focus on angel investing and start up companies.
- Act 255 has helped to define a market for investing in emerging Wisconsin companies.
- Act 255 reporting data has provided a partial picture of individual angel investing in Wisconsin.
- The tax credits in Act 255 help to offset some of the risk in investing in seed and early stage companies.
- Act 255 has created a positive climate for investing in Wisconsin start up companies.

Discussions with angel investors reveal few drawbacks to the provisions of Act 255. One possible drawback worth noting is the concern that qualified new ventures will use tax credits to enhance the valuation of the firm in any investment deal. Valuation is in general a difficult area for both angel and venture capital investing and it is not clear whether tax credits materially complicate that issue.

Angel Investing Metrics in 2006

Act 255 provides another \$3,000,000 in angel tax credits for 2006. Early indications are that the pace of angel investment deals in 2006 is matching the performance seen in 2005. As the number of angel groups and qualified new ventures continues to rise, the prospects for a robust year in angel investing in 2006 also rise.

The lack of any data on individual angel investing in prior years has limited the analysis of total angel investing in Wisconsin. Data from the NorthStar survey of 2006 angel investing and data related to Act 255 investment deals will give us a solid data baseline to measure year to year performance in the angel investing area. Data for 2006 will allow us to look at metrics for individual angel investment (in relation to Act 255) and angel group investing with respect to 2005.

Summary:

Overall angel investing in Wisconsin in 2005 amounted to over \$19 million. For the first time, thanks to data related to Act 255, we are able to get a partial picture of individual angel investing in Wisconsin. According to data reported under Act 255, individual angels invested nearly \$14 million in angel deals in 2005.

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For questions about the report, please contact

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