BLUEPRINT FOR ENTREPRENEURSHIP

Entrepreneurship as a Strategy for Economic Development and Community Renewal in West Virginia

Vision Shared Committee on Entrepreneurship:
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Executive Summary

This *Blueprint for Entrepreneurship as a Strategy for Economic Development and Community Renewal* is both a top-down and bottom-up approach to the development of a 'culture of entrepreneurship' for West Virginia. As best stated on April 26, 2003, by Governor John Baldacci of the State of Maine,

> "Innovation is the key to Maine's economic future, and I believe that entrepreneurs are at the heart of the innovation process. The role of the entrepreneur is to innovate and create economic opportunity for others, and the role of government and its partners is to create a culture that encourages entrepreneurship and builds a supportive environment for entrepreneurial activity."

It is well past time that West Virginia adopts a similar position with regard to creating this culture and supportive environment for entrepreneurs.

This *Blueprint* covers the key elements influencing entrepreneurship: general perceptions of entrepreneurship, entrepreneurial infrastructure, tax and regulatory climate, access to capital, and entrepreneurial education.

The intent of this *Blueprint* is to challenge conventional thinking with respect to economic development and to begin the process whereby West Virginia and its policy makers will focus the necessary resources toward entrepreneurship and small business.

The focus of the West Virginia Development Office has primarily been in trying to recruit new large employers and companies to West Virginia. This committee believes that an alternative focus would be more fruitful for economic development efforts. West Virginia must begin to develop its people and its communities from within through an emphasis on entrepreneurship and small business. Real, substantive economic revitalization will not likely occur through the attraction of large manufacturing concerns to the state. Rather, transformational economic development will occur through the development of an 'entrepreneurial culture' in West Virginia.

The recommendations included as part of this *Blueprint* are not unique. Rather, they are ideas and policies that have been successfully implemented by other states and nations as they struggle to grow economic opportunities in response to growing financial and community difficulties. They are recommendations with a proven track record.

We have not sought to recommend only easy and popular solutions to the problems that plague our communities. Rather we have sought to introduce a comprehensive entrepreneurial policy that, if implemented in whole, will lead to a more vibrant, growing West Virginia through the development of a 'culture of entrepreneurship.'

Our recommendations may not be easy to accept or adopt for public policy makers and elected officials, but the alternative is much worse – a continuation of our current policies that have not worked. Generation after generation of West Virginian has been raised with the promise of a 'better future' only to have been dismayed at the continuation of the status quo. Their cynicism is leading to a dangerous economic environment that threatens the very viability of West Virginia and its people. It is for these reasons that we are committed to the principals and the vision contained in this *Blueprint*.

A 'culture of entrepreneurship' is critical to the future of West Virginia. The intersection of two precepts—the value of entrepreneurship to the overall economy and the impact of state actions on the business climate – has significant implications for state officials and policymakers. To better understand the current state policy environment in which West Virginia entrepreneurs operate, we must understand entrepreneurial initiatives adopted by other states and the current state of the entrepreneurial infrastructure in West Virginia.

At one end of the spectrum are states that have a clearly articulated development objective that focuses on the emergence and success of entrepreneurial ventures. In contrast, many states have draped their existing economic development programs in a 'mantel' of entrepreneurship. West Virginia must do more than simply speak in wishful terms about its commitment to entrepreneurship for the development of our communities. West Virginia must act.

According to several recent studies, such as that of the *Global Entrepreneurial Monitor*, variations in rates of entrepreneurship may account for as much as one-third of the variation in economic growth across countries. This strong correlation between entrepreneurial activity and economic growth has been repeatedly demonstrated at the local, state, and national level.

West Virginia has a choice, either to continue to struggle economically or to boldly look to the future with a plan to develop and nurture an entrepreneurial culture that can unleash the potential of generations of West Virginians. This committee believes that incremental change is not an option. West Virginia must move as quickly as possible to promote a national perception of West Virginia as the "most entrepreneurial-friendly environment in the United States."

This committee believes that West Virginia must act quickly to capitalize on the opportunities that are currently present in our ever changing world. Increased global integration and rapid technological change have created a business climate with more opportunities than ever for new businesses and entrepreneurs. We must create a climate in which West Virginia entrepreneurs can move quickly to take advantage of these opportunities before we are left behind.

While the rapid rate of change in the global economy might be overwhelming, as Peter Drucker has noted, "entrepreneurs see change as the norm and as healthy. The entrepreneur always searches for change, responds to it, and exploits it as an opportunity." West Virginia entrepreneurs are no different. They are ready to tackle these challenges and opportunities. West Virginia must simply provide the climate and support necessary to allow these individuals to reach their full potential.

As MIT's Lester Thurow puts it:

> "In the century ahead the economic game will be played on three levels [at the national, company, and individual levels]. Companies will play the game based on the skills they employ, the capital investments they make, their technical prowess, and their ability to globally source and sell new products. New start-ups that rapidly grow to become big multinationals will be an important part of success. These new, rapidly growing start-ups won't appear without entrepreneurs. Social regulations and attitudes will have to permit industrial flexibility if entrepreneurs and new companies are to emerge. As the nation sorts out its priorities for the new century, fostering entrepreneurship must be a cornerstone of our economic policy. **<u>If we fail in this regard, the costs could be enormous.</u>**"

If West Virginia is to fundamentally alter its history with respect to economic development and it's economic heritage, West Virginia must have a clearly articulated development objective that focuses on the emergence and success of entrepreneurial ventures. This *Blueprint* sets forth that vision.

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I. Introduction

a. The West Virginia Economy

Since 2000, West Virginia has lost more than 25,000 jobs in the coal, manufacturing, chemical and steel industries. City Holding has eliminated more than 300 jobs; Dupont Co. more than 200; Dow Chemical more than 1,000; Flexsys more than 200; BB&T eliminated more than 350 jobs; Ames closed its operations; Cambridge Educational laid off its 46 employees; Clarksburg Casket Company is moving its operations out of state; Weirton Steel is in bankruptcy; Wheeling-Pittsburgh Steel Corp may need to cut its workforce by more than 25% next year; and so on. In the last year alone, West Virginia has lost about 3,000 manufacturing jobs, with 400 of those in the chemical industry. Between 1998 and 2002, more than 2,500 jobs in West Virginia's chemical industry jobs have been lost with more than 1,500 of those in Kanawha County alone. West Virginia's economy will continue to suffer until such time as our state and our state's leadership makes a determined effort to transform our economy from one focused on short-term reactive measures to one committed to long-term economic growth rooted and grounded in entrepreneurial activity.

b. Entrepreneurship and the Economy

Research continues to link entrepreneurial activity and economic prosperity. Entrepreneurship is a key determinant of economic growth. The recently published *Global Entrepreneurial Monitor* (GEM) is the first comprehensive study to articulate the value and importance of entrepreneurial activity. GEM states, "Variations in rates of entrepreneurship may account for as much as one-third of the variation in economic growth." The GEM study examined the culture and economic policies of ten nations to determine which factors either support or impede the emergence and growth of an entrepreneurial economy.

- Some experts attribute nearly 70 percent of economic growth to entrepreneurial activity and suggest that "one-third of the differential in national economic growth rates is due to the impact of entrepreneurial activity."
- About 35 percent of the companies on the Fortune 500 list are displaced every three or four years by new firms. Entrepreneurs ultimately propel the country's largest businesses; they do not just run small companies.
- The National Commission on Entrepreneurship has determined that the Inc. 500 firms grow at an average rate of 1,312 percent over five years.

Yet, despite the clear evidence, most state economic development efforts, including West Virginia's, continue to be organized around traditional business retention and incentive-based industry recruitment programs. This has led to an emphasis on programs to enhance labor force skills, invest in infrastructure, and create a competitive tax and regulatory climate, among other factors.

These programs and the underlying efforts to improve the ability of businesses to prosper in a state are still necessary, but they are no longer sufficient. They have become the expected base line rather than a competitive advantage.

Both the states and the federal government have important roles to play in creating an environment that supports entrepreneurship. Federal securities and intellectual property laws, research and development funding, monetary and trade policies, and a stable legal system provide the framework in which new companies grow and thrive across the nation. However, the state also plays a key role in determining the success or failure of entrepreneurial companies.

State government can play a significant role in supporting the emergence and success of entrepreneurial enterprises. Since states first became active participants in the economic development process in the 1950s, the majority of attention (and often scrutiny) has been on incentives and public programs that provide direct assistance to individual firms. However, the impact of these programs on a state's economy is relatively small compared to tax and regulatory policies that affect everyone who does business in the state. Similarly, state investments in education and public infrastructure determine the configuration and the quality of the "playing field" on which all economic activity occurs within individual jurisdictions.

Policy makers must remember that 'good-intentioned' government regulations and programs often stand in the way of economic progress. We too frequently enact policies that increase the costs of doing business or reduce the reward from entrepreneurial activity. The proper role for government is to provide the necessary environment for entrepreneurship to flourish on its own.

As noted economist Dwight Lee puts it:

> "**No matter how fertile the seeds of entrepreneurship, they wither without the proper economic soil.** In order for entrepreneurship to germinate, take root, and yield the fruit of economic progress it has to be nourished by the right mixture of freedom and accountability, a mixture that can only be provided by a free market economy."

The necessary conditions meant by the phrase 'free market economy' are well established – secure private property rights, low regulations, and low taxes. Entrepreneurship requires freedom – freedom from burdensome government policies. With a supportive entrepreneurial infrastructure in place, less government often means more prosperity.

The intersection of these two precepts—the value of entrepreneurship to the overall economy and the impact of state actions on the business climate – has significant implications for state officials and policymakers.

c. Saying 'Welcome' to Entrepreneurs and Small Businesses

Many West Virginia communities – like communities across the country – have developed well-honed strategies for industrial recruitment. These same communities, however, have generally invested little in the way of time, resources and energy in the development of their entrepreneurs and small business sectors.

Too often West Virginia entrepreneurs are faced with a climate that is, quite frankly, anti-business and anti-entrepreneur. The creation of wealth, the pursuit of profit, the creation of jobs, and the occupation of 'businessman' or 'businesswoman' are viewed too often as negatives by both policy makers and the general public. We must celebrate and reward our successful entrepreneurs, not resent them and covet their wealth.

According to a study by the Corporation for Enterprise Development, there is growing understanding that economic development strategies founded primarily on business recruitment are not in Appalachia's best interests and that there needs to be a greater emphasis on 'homegrown' development. We must encourage our own citizens to aspire to create their own new businesses. Promoting this diverse pool of 'homegrown' West Virginia entrepreneurs with different motivations is the challenge we face as a state.

The economy of West Virginia is driven by small businesses. Over 87% of West Virginia's businesses have fewer than 20 employees. There are currently over 21,130 small businesses with four employees or less in the state.

While no single small business is likely to energize the economy of an entire community, the total impact of small businesses can be significant. It is estimated that businesses with fewer than 100 employees create more than two out of every three new jobs in the United States.

It is our vision that in the future many of West Virginia's children will aspire to be entrepreneurs and business owners when they grow up. This can only happen when these children grow up in communities that reinforce and encourage this choice as a rewarding and promising career option.

d. The Changing Face of Entrepreneurs

According to *Entrepreneur* magazine (January 2004) 50 years ago, the typical entrepreneur was relatively homogenous and static. He was usually a white man, sometimes working together with his family, who owned a small Main Street retail shop or a local manufacturing company. He knew most of his clients, and his company focused on local goods and services.

Today, much has changed. America's entrepreneurs are much more diverse racially, gender-wise and age-wise, and an increasing number are starting service businesses rather than manufacturing or retail companies. Economists, sociologists and small-business experts say the key trends in American entrepreneurship—growing diversity, an aging work force, a preference for starting companies that fit personal lifestyles, and a move into higher-value, global industries—are only likely to accelerate in the coming years. It is believed that a decade from now entrepreneurs will be drastically different from today's business owners.

Not only is the U.S. workforce becoming more diverse, but it is also aging, as baby boomers reach their 50s, 60s and 70s. As a result, experts say, the entrepreneur of the future is likely to be older, more attuned to the older population's needs, and more willing to trade some income for a better lifestyle. An SBA study released in 2000, "The Third Millennium: Small Business and Entrepreneurship in the 21st Century," notes that the average age of a worker will increase from 35.9 years in 1988 to 40.7 years in 2008. What's more, corporate downsizing in the past 20 years has pushed many mid-career workers out of corporate jobs, enlarging the pool of potential entrepreneurs. The SBA believes that, between 1996 and 2006, the number of self-employed workers will grow by 50 percent, in part because of these older entrepreneurs.

Few future entrepreneurs are expected to start companies in manufacturing or even retail sectors of the small-business community that are in precipitous decline. Manufacturing alone has lost nearly 3 million jobs over the past five years, and small manufacturers have been particularly hard hit, as they have been unable to compete with low wages overseas. According to a 2000 study by the SBA, by 2010, "the relative shares of employment in the manufacturing and service sectors are expected to be just about opposite of the 1950 levels"; and by 2015, roughly 35 percent of American businesses will be in services. The most recent survey from the Global Entrepreneurship Monitor, says that over the next five years the most highly educated entrepreneurs, who more often start IT or service businesses, will have the most employees.

As entrepreneurs of the future increasingly move into higher-value service businesses, they will also have to attain higher levels of education and interact more with foreign suppliers and customers to succeed. Howard Aldrich, a professor of sociology at the University of North Carolina, Chapel Hill, who has studied entrepreneurship, says that today, education is the key predictor for business formation—people with more education are more likely to start a business. In addition, for a service business to compete in an increasingly global marketplace, future entrepreneurs in IT, biotechnology, customer service, consulting and other fields will have to outsource, sell and purchase abroad. The Department of Commerce estimates the number of small companies that export tripled between 1987 and 1997, and small business experts expect the trend to continue.

Tomorrow's entrepreneurs will have to be better educated. They will have to be willing and able to face a global business climate. By investing heavily in education (both K-12 and higher education) we can prepare the next generation of West Virginia entrepreneurs for this challenge.

e. The Dollars and Cents of Entrepreneurship

Research on the impact of entrepreneurship on low-income individuals has shown that it is one of the most effective ways to help alleviate poverty. Regarding small (micro) businesses in the United States, the Aspen Institute has found that:

- Low-income micro entrepreneurs were able to reduce their reliance on government assistance programs by 61 percent with the greatest reduction in the amount of cash benefits received. Average benefits fell by $1,679 per year.
- Seventy-two percent of low-income micro entrepreneurs experienced gains in household income over five years. The average gain was $8,485.
- Fifty-three percent of low-income entrepreneurs had enough household gains to move out of poverty, with the business being the major source of earnings.
- Average household incomes of low-income entrepreneurs grew by $15,909 over five years.
- Forty-nine percent of micro enterprises owned by low-income entrepreneurs survived after five years – a rate comparable to the national average of all small businesses.
- On average, micro enterprises create 1.5 full- and part-time jobs per business.

What this research makes clear is that areas of low income are not exceptions to the rule. A thriving entrepreneurial climate is a tide that raises all boats.

f. Defining Entrepreneurship

There are varying opinions about what constitutes entrepreneurship, especially the distinction between entrepreneurship and small business. The Kauffman Center provided the following definition of entrepreneurship.

> *Entrepreneurship is the ability to amass the necessary resources to capitalize on new business opportunities. The term is frequently used to refer to the rapid growth of new and innovative businesses and is associated with individuals who create or seize business opportunities and pursue them without regard for resources under their control. They build something from practically nothing and usually reinvest earnings to expand their enterprise or to create new enterprises. Other words that characterize entrepreneurship include innovative, creative, dynamic, risk-tolerant, flexible and growth-oriented.*

Entrepreneurship is thus not dependent on size. Many companies that meet the Small Business Administration's criteria for small or medium sized enterprises (SME) are very entrepreneurial. The distinction lies more in the desired outcome. Small businesses play a significant role in the overall economy. It is through small businesses that we obtain many basic products and services (e.g., gasoline for automobiles, accounting services). And many small business owners exhibit entrepreneurial qualities as they address product demand and customer satisfaction.

Simply put, an *entrepreneur* is a person who creates and grows an enterprise. The process through which these enterprises are created and grown is entrepreneurship. However, different individual entrepreneurs may have vastly different motivations and goals. Understanding these differences is necessary to design appropriate policy.

g. Types of Entrepreneurs

Individual entrepreneurs generally have different reasons for why they start their own business. Several of the most well recognized types of entrepreneurs are discussed below.

Aspiring entrepreneurs: those who are attracted to the idea of creating enterprises, including students and young people. These people are often innovators and risk-takers who do their homework and make things happen. Home-based businesses and franchises are good examples of enterprises run by aspiring entrepreneurs. One example of a successful, aspiring entrepreneur with a great message is Robin Hillenbrand, owner of Blue Smoke Salsa in Ansted.

Survival entrepreneurs: those who resort to creating enterprises to supplement their incomes. Most often, survival entrepreneurs are individuals or families that are tied to a place or a profession and creatively patch various economic activities together to maintain this tie. Examples of survival entrepreneurs would be family farmers in Monroe County. Prosperity is challenging and growth opportunities are limited.

Lifestyle entrepreneurs: those who create enterprises in order to pursue a certain lifestyle or live in a particular community. These are individuals that may have chosen a rural place to live and are able to generate a desired standard of living and quality of life. Part of the quality of life they are seeking tends to limit their growth orientation. These entrepreneurs are often very successful and contribute to their community's economy and society in meaningful ways. An example of a lifestyle entrepreneur would be a Bed and Breakfast owner in the Eastern Panhandle.

Growth entrepreneurs: those who are motivated to develop and expand their businesses that create jobs and wealth. These are the dynamos capable of generating growth enterprises that profoundly impact area and national economies. Their enterprises create jobs, careers, tax base and economic activity benefiting other enterprises. Dick Cabela would be an example of a growth entrepreneur. He and his wife created Cabelas – one of the largest outdoor goods retailers in the world and in some communities, the biggest employer.

Serial entrepreneurs: those who go on to create several growth businesses. Serial entrepreneurs make a habit—and a career—of starting companies. Sometimes the businesses relate to one another and sometimes they do not. Serial entrepreneurs are valuable not just for what they bring to the business world but for what they teach others about it. Because they try more things, they make more mistakes and learn more quickly from them. Because they walk through dozens of corporate environments, they leave more footprints behind. Clearly, something sets these people apart from those content to tread every day to the same office and eat the same cereal for breakfast.

Inter generational entrepreneurs: those who grow up in an entrepreneurial family and inherit a functioning business; continue to work in, maintain and grow the enterprise. Today's family business entrepreneurs face a demanding and stressful environment. Their concern over a slowing economy, perceived or real, feeds the fear that many entrepreneurs live by. Entrepreneurs fear that competition, cash flow, accounts receivables, bad debts, or the collapse of a marketplace will take them out of the game. These fears drive the entrepreneur to be highly focused on what is happening today in the business. Planning for the future can be seen as a feeble waste of time - you have to make today work or there will be no tomorrow! It is this drive and this focus that makes many entrepreneurs successful. It can also be the major reason why successful businesses can falter when it is time for transition to the next generation or to a new management team. In today's business environment, it is easy to stay focused, working **in** the business rather than to take time to work **on** the business. When a family business is in the throws of transition, either managerial or inter-generational, it is time to sit back and spend some time working on your business. We have found that three major fears surface when entrepreneurs are faced with a transition. These fears: the fear of conflict; the fear of loss of control; the fear of loss of wealth; are easy to ignore in light of the other "real" demands and stresses of running a competitive and successful business. However, ignoring these fears grinds successful transition to a standstill. It is imperative that they are addressed. In the past, inter-generational business transfers consisted of primarily one dynamic, white males passing businesses along to white males and there was a fair amount of trust and common understanding among everyone. Today's inter-generational entrepreneur rarely follows this model. One example of an inter-generational entrepreneur would be the Vision Shared committee member, Catherine Jones.

Gazelle entrepreneurs: entrepreneurial growth companies (EGCs) which are high-performing companies driven by an entrepreneur or entrepreneurial team. These entrepreneurs are considered a corner stone for America's dynamic economy. Gazelles are entrepreneurial organizations that grow at an explosive rate, often at 100% a year or more. Gazelles create the vast majority of new jobs (and new good jobs) and bring many technological innovations to market. (Cities with many gazelles will even have higher quality of life scores in the future.) Finally, high-growth firms even have longer life expectancy.

f. State Policies That Impact Entrepreneurship

Each of the following areas is critically important to encouraging entrepreneurship as a career option and to support entrepreneurial activity.

- General perspective of entrepreneurship.
- Tax and regulatory climate.
- Access to capital.
- Entrepreneurship education.
- Intellectual capital.

The compelling argument to invest state resources in support of entrepreneurs and small business is only now being made. Research such as the GEM analysis, which more clearly links entrepreneurship with strong economies, is only now achieving visibility among policymakers. Entrepreneurs contribute to state economic and social goals and it is in West Virginia's own long-term best interest to explore policy options that effectively promote and support an entrepreneurial economy.

II. General Perception of Entrepreneurship

a. Entrepreneurship and the State Development Strategy

In a study conducted by the Kauffman Foundation, thirty-four states indicated that they consider entrepreneurship part of the state economic development strategy. When asked to describe how entrepreneurship fits into the state strategy, four states indicated that they had a clearly articulated statement within the strategy document.

North Carolina is one state that has specifically targeted entrepreneurial firms as part of its economic development strategy. That state's Economic Development Board, which implements and monitors the state's development strategy, includes the following among its six primary goals.

> *"Goal Four: An Entrepreneurial Center—Create an economic climate that is conducive to the birth, attraction, and retention of innovative entrepreneurial firms that create new products and services and expand into new markets".*

Sometimes the focus on entrepreneurs is contained in legislation such as the South Carolina Technology Act of 1999. The Act resulted from a determination that the state had an insufficient supply of rapidly growing South Carolina-headquartered companies and needed stronger linkages between state universities and research institutions and the state's business sector.

Kentucky best articulated the goal of creating an entrepreneurial economy through the following objectives:

- Changing the culture from one that develops employment skills to one that develops the necessary skills to build new businesses;
- Creating an atmosphere of entrepreneurship throughout the education system for kindergarten through post-secondary institutions; and
- Developing the knowledge and skills to deploy technology resources in high-growth businesses.

b. Differentiating Entrepreneurs from Small Business

In a national survey of states and their treatment of entrepreneurs and small business, several states indicated a rationale for treating entrepreneurs differently from small businesses.

- Entrepreneurs have different capital needs. (California and Nebraska).
- Entrepreneurs add value to the economy and generate a higher rate of return on public investment. (Iowa).
- Entrepreneurial businesses expand rapidly and are more dependent on constantly changing technologies. (Massachusetts).
- Entrepreneurial support includes incubators and sources of equity financing. (Maryland).

- Entrepreneurial businesses have high-growth potential. (Michigan and New Jersey).

- Entrepreneurs are cash importers as a result of selling products and services outside of the state. (Missouri).

- Entrepreneurial companies are defined by revenue growth. Their resource needs differ from small business in magnitude and kind. (North Carolina).

- The state begins working with entrepreneurs at a pre-competitive stage. (South Carolina).

- Entrepreneurs need greater access to research and development resources. (South Dakota).

When one compares these statements against the initiatives identified by these states as supporting entrepreneurs, there is consistency between a state's view of entrepreneurs and the programs and policies it adopts to bolster that perspective. For example, California focuses on venture capital and research and development funding to address entrepreneurs' unique capital needs. Based on their view of entrepreneurs as a distinct segment of the state economy, Iowa and Massachusetts invest a higher percentage of their economic development funds in entrepreneurial development. This internal consistency between perspective and action suggests states with a better understanding of the contribution that entrepreneurship makes to the state's economic prosperity and the specific needs associated with entrepreneurship are more likely to take actions that more directly support entrepreneurs.

c. State Economic Development Expenditures

An important measure of the importance of entrepreneurship in state economic development strategies is the percentage of state funding that is devoted to entrepreneurial development. Each year the National Association of State Development Agencies (NASDA) conducts a state economic development survey. States are asked to distribute their economic development expenditures across 15 program categories including administration and program support (e.g., research). While the survey requests information on both federal and state funded expenditures, this study focuses the state funded activities.

In states where entrepreneurship is truly a central element of the economic development, development office expenditures committed to entrepreneurial endeavors are the highest.

d. Recognition of Entrepreneurs

The perception of entrepreneurs' contribution to a state's economy can also be gauged by the extent to which public officials recognize that contribution.

With some exceptions, most states do not distinguish between small business activities and entrepreneurs. Several states, in promotion of their strategies, have made a substantial commitment to the development of a cultural transformation:

- Utah, which reported the most comprehensive effort to recognize the value of entrepreneurs. The Utah program consists of three activities: co-sponsorship with Mountain West Ventures of a state entrepreneur of the year award, a Governor's Young Entrepreneur of the Year Award, and a competition for business plan of the year co-sponsored with the small business development center.

- Iowa indicated an emphasis on young entrepreneurs through two competitions: Invent Iowa and a business plan competition conducted through the five John Pappajohn Entrepreneurial Centers at the state universities. A unique aspect of Hawaii's "Exporter of the Year" award is one of the selection criteria that measures the extent to which candidates help others expand exports.

- The Maryland Technology Showcase provides an opportunity for Maryland businesses and citizens to communicate and educate themselves about the latest technological advances and how they effect their personal and professional lives. The showcase attracts over 12,000 attendees and is covered by Maryland Public Television, area newspapers, local radio stations and the local network affiliates.

- Tennessee and Texas referenced "Day on the Hill" events as one means of educating state officials about the contribution entrepreneurs make to the state economy. In Tennessee, locally recognized entrepreneurs meet with legislators and cabinet officials and attend an awards luncheon for the recipients of local awards. Tennessee adopted this approach to complement existing local award programs rather than to compete against or preempt them.

e. Summary and Implications

States that view entrepreneurs as a unique segment of the state economy tend to adopt policies and programs that directly support an entrepreneurial economy. States that do not make this distinction are more likely to adopt the perspective that entrepreneurs benefit from economic development policies and initiatives that are designed for a broader audience. This finding suggests that advocates of an entrepreneurial economy cannot expect major changes in public policies until state officials develop a more succinct view of the link between entrepreneurship and economic prosperity and the contribution that entrepreneurs make to society in general.

III. Entrepreneurial Infrastructure

The State of West Virginia and its related development agencies are well disposed to supporting and encouraging an enterprise culture and individual entrepreneurs. There is, however, a policy and coordination gap because West Virginia's entrepreneurial infrastructure is largely dependent on a loose connection of independent organizations.

This lack of coordination is a major stumbling block to maximizing the potential of resources devoted toward entrepreneurial support in West Virginia. Because the Claude Worthington Benedum Foundation funds many of these organizations, they have recently asked the Entrepreneurship Centers at West Virginia University and the University of Charleston to take over the administration of the West Virginia Entrepreneurship Initiative (funded by Benedum) in an attempt to redirect it toward fostering this type of cooperation. The WVEI will begin holding coordination meetings twice a year to bring together these many organizations, but much more needs to be done.

There is a need to develop an all-embracing entrepreneurship policy and to better coordinate the work of the many agencies and organizations focused on supporting entrepreneurs. There is no obvious champion of entrepreneurship who could propose or implement practical actions to make entrepreneurial development a reality.

a. Entrepreneurial Matrix

There are numerous organizations throughout West Virginia that are working in the areas of entrepreneurship and small business. The Entrepreneurship Committee of Vision Shared set forth to develop what we refer to as an Entrepreneurial Matrix ("Matrix") in an attempt to inventory the state's current entrepreneurial infrastructure.

The intent of the Matrix is to identify the major stakeholders in small business and entrepreneurship throughout the state of West Virginia. The Matrix is attached hereto as an Exhibit. The Matrix sets forth the relationship between the following entities:

1. **West Virginia Development Office**
2. **Entrepreneurial League System**
3. **Foundations and Private Support**
4. **Incubators**
5. **West Virginia Entrepreneurship Forum**
6. **Entrepreneurship Centers**
7. **Private Capital**
8. **Minority Business Development Center**
9. **Community Development and Economic Development Agencies**
10. **Micro-enterprise**
11. **West Virginia Jobs Investment Trust**
12. **Municipal Entrepreneurship Councils**
13. **Small Business Administration**
14. **West Virginia Entrepreneurship Initiative**
15. **Non profit Intermediaries focused on developing entrepreneurs**

IV. Tax and Regulatory Climate

Each state's tax and regulatory climate further differentiate states between general pro- business policies with supporting entrepreneurs and those states that recognize the unique needs of aspiring and high growth entrepreneurs. In particular, states in the latter category reported policies that deal with distinguishing characteristics of entrepreneurs. First, in an entrepreneurial setting, expenditures generally exceed revenues in the initial phase of the enterprise. Second, entrepreneurs tend to reinvest the gains from their initial business in successive enterprises.

The analysis of the municipal general revenue sources shows that business and occupation tax, property tax and total municipal charges, licenses and services fees are the three largest revenue sources according to a West Virginia Public Finance Program Project Report published in August 2003. The business and occupation tax, which is the largest single revenue source for municipalities, is found to perform poorly in terms of both neutrality and equity. According to the Project Report, it leads to high effective tax rates, putting substantial burdens on both businesses (within corporate limits of the city) and consumers. As a result, entrepreneurial efforts are suppressed due to the considerable regressive tax rates and coordinating costs to operate a business in the State of West Virginia.

a. West Virginia Municipal B&O Tax

B&O tax is a gross receipts tax imposed on business activities or occupations within jurisdictions. As a "turnover" tax, B&O tax leads to "pyramiding" of the tax since it is paid at each stage of the production of a good or service. Turnover taxes are thought to be inefficient and were replaced by alternative taxes in many countries. They lead to effective tax rates that can be significantly greater than the official nominal rates depending on the number of stages of production. Turnover taxes also give incentives to vertical integration and generate a competitive advantage to vertically integrated firms.

With such characteristics, B&O tax can affect business decisions significantly and put a greater than expected burden on businesses. However, this tax can be shifted on to consumers through higher prices. To the extent that it is shifted to consumers, it will increase the regressivity of the municipal tax systems. In addition, when the B&O tax is imposed on business activity within the corporate limits of a municipality, businesses that are located outside the municipal limits do not pay this tax. Hence, it violates horizontal equity by discriminating against businesses within municipal limits.

b. Tax Policy

States use tax policy is critical in the support of entrepreneurs in two ways: the general tax structure and tax incentives that reward specific business practices. Several states have instituted tax policies that specifically benefit entrepreneurs who are trying to build new companies.

- In 1999, Connecticut adopted two tax provisions that allow new companies to recoup some of their initial investment. The first allows businesses to sell unused research and development tax credits back to the state. The state also extended its Net Operating Loss Carry-Forward (NOL) from five to 20 years. The NOL extension gives small companies a longer time frame to recover losses they may have incurred during their initial years of operation.

- Hawaii also has made changes in its tax structure to support the growth of its entrepreneurial economy. Recognizing the importance of non-tangible assets to entrepreneurs, the state now excludes from taxation income derived from patents and copyrights. Additionally, the state does not tax employee stock options.

- Several states either apply a different rate of taxation to capital gains or partially excluded the gains. For example, Arkansas applies a maximum six percent tax rate on capital gains, while Idaho and Wisconsin exclude 60 percent of capital gains from state taxation. Massachusetts recently adopted a graduated exclusion based on the number of years the asset is held. When fully implemented in 2001, capital gains on assets held less than two years will be taxed at a five-percent rate. At the other extreme, assets held for more than six years will be totally excluded from capital gains taxes.

This year, the West Virginia Legislature enacted several pieces of legislation that are intended to grow investment and new business start-ups. Passed this past session were (i) a High Growth Business

Investment Tax Credit; (ii) a Strategic Research and Development Tax Credit which is a refundable tax credit to certain companies; (iii) a sales tax exemption for certain high technology companies; and (iv) the ability for companies to sell unused research and development tax credits. Each of these new acts will establish a more conducive business climate for high-technology businesses in West Virginia.

The goal of the of the High Growth Business Investment Tax Credit is to encourage investment in start-up and emerging high growth R&D business in the state. The details of the tax credit are as follows:

- The credit is equal to 50% of the investment made in a business certified as eligible for the "Strategic Research & Development Tax Credit" by the Tax Department.
- There is a cap of $50,000 on the amount of credit that can be obtained by an investor or investor group. Any research and development company may accept up to $1 million qualified investment in any taxable year. There is an overall cap of $1 million annually to be allocated by the Economic Development Authority.
- The credit can be used to offset business franchise tax, corporate net income tax, or personal income tax. Unused credit can be carried forward, but expires the fourth year after the initial investment.
- The credit is effective for investment made on or after July 1, 2005 and sunsets July 1,2008. There is a tax credit review report that will be issued in February, 2006 that will provide information on the cost effectiveness of the credit.

In order to be eligible for the credit the investor must invest in a business that:

- Is certified by the Tax Department as eligible for the "Strategic Research &Development Tax Credit"
- Has gross revenues of not more than $20 million and not more than $2.5 million in payroll.
- Maintains its primary corporate headquarters in WV

The goal of the Strategic Research and Development Tax Credit is to assist start-up and emerging R&D companies by allowing small R&D companies that do not yet have tax liability to utilize their R&D credits by making them refundable. The current R&D credit is available for 3% of all qualified expenses and qualified investment, or 10% of the excess of qualified expenses and qualified investment for the taxable year over the average for a base period. The new legislation provides that:

- Tax Credit may be used to offset up to 100% of the taxpayers annual liability for business franchise tax, corporation net income tax and personal income tax.
- New bill allows for R&D companies who have been certified by the Tax Department as R&D companies, and who have not more than $20 million in gross revenues and $2.5 million in payroll to obtain a refund of their R&D credit that is in excess of their tax liability, not to exceed $100,000 annually.
- Bill provides for a overall $1 million annual cap on total refundable R&D credit. The bill is effective for investment made on or after July 1, 2004 and sunsets July 1, 2008.

As the nature of the U.S. economy shifts from firms that are dependent on tangible assets (e.g., machinery and equipment) to businesses that measure their worth in terms of ideas and innovations, tax policy will continue to evolve. Otherwise, tax policies may constrain the growth of entrepreneurial businesses that will lead the national economy in productivity, job creation and general economic prosperity. The West Virginia legislature has enacted several tax incentives to encourage new business through high technology growth. We must be certain that not only high technology but rural entrepreneurship is provided the same opportunity and encouragement to grow West Virginia's future and to rebuild our local communities.

c. Regulatory Policy

These include one-stop service centers, unified reporting, paperwork reduction, electronic records, assistance teams, contracting assistance and publishing information on the Internet.

Of more significance may be regulatory changes that affect imposition of specific regulations or have a major cost impact on an emerging business. In 1995 New York Governor George Pataki created the Governor's Office of Regulatory Reform. Since its creation, the state has had a 59 percent decrease in new regulations with an estimated $1.9 billion annual savings to businesses and individuals.

Most recently, West Virginia Governor Bob Wise signed into law Executive Order 20-03 that requires a review of all state regulations affecting small business. Once implemented, this single executive order improves the regulatory climate in a dramatic manner in the State of West Virginia.

Summary and Implications

Policies that most benefit these businesses are those that defer expenses, allow companies to convert tax incentives into cash, and lower development costs.

V. Access to Capital

Historically, financial assistance programs have been a major element of state economic development efforts. Although West Virginia has committed substantial resources to the area, venture capital has not been critical to the development of an entrepreneurial culture.

Of all the myths and misunderstandings surrounding entrepreneurship, the role of venture capital is perhaps the most exaggerated. The venture capital phenomenon has received so much attention that it often appears to those looking in from the outside that most decent business ideas would receive venture backing. The media lavishes coverage on venture-backed startups, and has highlighted the massive growth in business "incubators" around the country.

In truth, venture capital is dominant in some industry sectors where capital requirements force companies to skip the early growth stages. For example, venture capital backing is a common feature among biotechnology ventures, some high-tech startups, and the Internet industry. For example, at the height of the boom, Internet startups received roughly $17 billion out of $21 billion (80 percent) in venture capital during the first quarter of 1999. But even after the "dot-com crash" (the third quarter of 2000) Internet companies still accounted for 45 percent of all venture capital investments.

And venture capital is an important part of the transition from a fledgling company to a more developed entrepreneurial company. Growth companies of all types require equity financing in order to grow. At the later stages, substantial resources are needed in order to capitalize on initial successes. Started with just $5,000 of Sam Walton's money in 1945, Wal-Mart supported its own growth until 1969, when it secured a large term loan and shortly thereafter completed a $4.6 million public offering.

In many cases, the search for outside funding and the conditions imposed by venture capital firms accelerate and enforce the transformation of initially successful startups into later stage growth companies. There are data, for example, that show that venture capital-financed companies perform better through entrepreneurial growth stages than entrepreneurial companies without such investors.

However, venture capital — or any other type of formal financial support — is surprisingly uncommon among most successful entrepreneurial companies at their early stages of development. In 1999, for example, fewer than 4,000 of the roughly 700,000 new businesses created were venture capital-funded. That means that less than one percent of all new businesses were backed by venture capital. In recent years, no fewer than half of all initial public offerings have involved companies without venture backing, according to the National Venture Capital Association.

While high-tech startups are often the exception to this rule, it is well worth noting that even Bill Gates and Paul Allen, founders of Microsoft, failed to secure venture capital when they started their company in 1975. Hotmail.com, the popular e-mail program, thrived without venture capital before it eventually received outside backing and was bought out by Microsoft for $400 million. And Cisco Systems, now one of the top providers of Internet routers and servers, was initially financed from the personal savings and borrowings of its two founders.

In fact, most growth companies start with limited means. One reason is that the resources required to start most growth companies are remarkably small. In the world of venture capital, backing usually starts at about $3 million – far more than most early-stage growth companies need or warrant. In most cases, there is simply no need for a massive influx of cash. Twenty-six percent of the successful businesses started with less than $5,000. Two out of three on the 1996 Inc. 500 started with less than $50,000.

The average funding required for these companies was just $25,000. Rolling Stone magazine was started with just $7,500 in the bank. Waste Management, Inc., a NYSE-listed waste management leader operating in more than half of the states, started out with a single truck and revenues of $500 a month. Bob Reiss founded Valdawn, which makes fashionable, inexpensive watches, with just $1,000 of initial funding. By 1994, Valdawn was an Inc. 500 company with $7 million a year in revenue.

At these funding levels, personal savings, and money from family and friends, are usually more than enough to do the job. In some cases, individual “angel” investors become involved at this point. Angels, many of whom are former entrepreneurs with industry experience, are often the first outsiders to look critically at an entrepreneurial company. Through the moderate amounts of funding they provide, angels frequently accelerate the transition between the early and later stages of entrepreneurial growth. A sound angel development policy in West Virginia can be critical to the development of entrepreneurial companies.

Moreover, venture capital is usually only awarded to initiatives that have features most entrepreneurial companies lack at the start — a strong business plan, and a solid track record, experienced staff, and an innovative or proprietary idea. They may acquire some or all of these things along the way, but, lacking most of these characteristics at the outset, three out of four entrepreneurs do not even attempt to secure venture capital. More than eighty percent of the Inc. founders bootstrapped their ventures with modest funds derived from personal savings, credit cards, second mortgages, and so on. The median start-up capital was about $10,000. Only 5 percent raised their initial equity from professional venture capitalists.

For those industries where venture capital is important and critical, there are regional discrepancies as many of the major venture capital companies operate out of the major urban centers. In these instances, state participation in equity investment funds is viewed as one way to overcome these geographic biases.

Several states have adopted plans to deal with limited resources and the need for entrepreneurial companies to finance necessary activity.

- The Delaware Innovation fund can be used to secure patents and test the technical feasibility of new products.

- The Maryland Enterprise Fund provides matching grants for the development of business plans.

Summary and Implications

Access to capital, especially equity investments in start-ups, continues to be a critical issue for entrepreneurs. However, the overwhelming majority of state financial assistance programs are in the form of loan guarantees, loan participations and direct loans. Less than 10 percent of these programs involve direct or indirect equity investments.

Although states recognize that the "capital readiness" of an enterprise is a key indicator of whether a firm can obtain the capital it needs, states focus more on increasing the supply of capital than working with entrepreneurs to address investor concerns about business planning and management. States might want to reassess their programmatic priorities, shifting resources from programs that increase the capital supply to activities that increase the number of quality deals.

States have made significant progress to implement uniform and reciprocal procedures associated with the regulation of marketable securities. Programs that standardize SCOR filings and facilitate interstate offerings have multiple benefits for entrepreneurs. First, they extend the reach of small businesses to raise capital through public offerings. Second, they reduce the costs associated with redundant registration filings in two or more states.

In terms of the development of entrepreneurial companies, West Virginia must adopt policies that encourage 'angel' investment into new companies. Such policies can serve to nurture the entrepreneurial pipeline and create a partnership between citizens and the ventures which are the foundation of a community.

VI. Entrepreneurship Education

Sustaining an entrepreneurial economy depends on nurturing successive generations of entrepreneurs. Therefore, it is important to understand the propensity of young adults to become entrepreneurs, and more importantly, to become successful entrepreneurs.

a. State Support of K-12 Entrepreneurship Education

It is never too early to instill the understanding, knowledge and confidence that support fulfillment of an individual's desire to be an entrepreneur. Therefore, the State of West Virginia should promote the development of entrepreneurial education in all schools, primary and secondary, throughout the State. The State of West Virginia must support the development of the personal characteristics and skills that are conducive to entrepreneurship.

For good or ill, there is a general belief that career guidance counselors, teachers and parents do not perceive entrepreneurship as a legitimate career option. Culturally, West Virginia has traditionally been a state associated with large industry including coal, steel, and manufacturing. Students are being steered to traditional and perceived 'safe' career choices in law, medicine, and other engineering. Reality, however, is that the average person will be employed with no fewer than five (5) employers over the course of his or her career and most lawyers, doctors and engineers will be self-employed at some point in the future.

Many states have instituted programs that deal directly or indirectly with the concepts of entrepreneurship and business. One of these programs is conducted by the State of Massachusetts.

- Students in Massachusetts can participate in the Youth Tech Entrepreneurs (YTE) program. This program prepares high school students for leadership and education achievement by developing entrepreneurial and technical skills. The YTE program offers a project-based curriculum. Participating schools work with the state Department of Education to develop and implement academic programs and extracurricular activities that pay for themselves. Students join the program in their sophomore year and make a three-year commitment that includes daily classes, monthly Saturday labs and after school technology-based projects. In a February 1999 press release announcing an expansion of the YTE program to three additional high schools, Massachusetts Commissioner of Education David Driscoll said, "YTE is far more than technology training. Students learn, but they also teach technical skills, they work with faculty and staff to maintain computer networks, and they provide technology support services to local companies. These students are entrepreneurs today, and you'll be hearing from them tomorrow, as well." Driscoll added, "The heart of the YTE is in involving students from diverse backgrounds in the project-based curriculum. In daily YTE classes, students master skills in problem-solving, communication and critical thinking by completing reading and writing assignments on a technology question of the day."

- Kauffman Center's Mini-Society, which has been implemented in school districts in 43 states. Mini-Society is specifically designed to teach entrepreneurship in ways children understand—through experiences, role-playing and careful instruction. This mini-society program has been run through the WVU Extension Service several times over the past few years in West Virginia when Kauffman funding was available.

There are many national and state based private efforts in the area of entrepreneurship in secondary schools. One example is West Virginia's Dreamquest Program that is conducted by Tim McClung and the University of Charleston. Dreamquest is a business plan competition for secondary school students across the State of West Virginia.

Another example is a week-long summer program currently offered through WVU that is fnanced largely by MeadWestvaco and several other forest products companies. This course exposes K-12 teachers to entrepreneurs in the forest products sector and helps them to make lesson plans for use in their own classrooms.

What is missing from K-12 Entrepreneurship Education in West Virginia is a state-level focus on support and content standards for entrepreneurial education in the classroom. What has been offered has been good, but simply done on too small a scale.

b. State Support of Post-Secondary Entrepreneurship Education

Entrepreneurship education programs are now critical resources for several state universities. West Virginia University and Marshall University should offer a masters in business administration (MBA) in entrepreneurship, a post-MBA program certificate in entrepreneurship, and a major in entrepreneurship at the undergraduate level.

Additional activities beyond formal education include an extensive adult education program in how to start and grow a business and a forum on family-run businesses.

Because of their newly created Entrepreneurship Center, West Virginia University is the most advanced in this regard. They have developed a student business plan competition, a student entrepreneurship club, an internship program to assist start-up businesses, and are working on expanding the course offerings in entrepreneurship available to students beyond the one class that is currently offered only to business students. WVU is also in the process of developing a center for family business. However, budgetary considerations over the past few years have significantly reduced the progress and scope of these activities. At the time of publishing this report, the status of Marshall University with respect to restrictions to program offerings is unknown.

The post-secondary education system appears to be lagging behind entrepreneurial realities. Students should be equipped with the personal skills and characteristics to open up the possibility of an entrepreneurial career as an attractive career option. If they choose to pursue this route, they should find support and encouragement.

Beyond the presence of an entrepreneurship curriculum and internship program, West Virginia's colleges and universities must promote entrepreneurship through two additional activities.

- Business plan competitions that encourage students to apply their academic training to a potential enterprise.

- Formation of collegiate entrepreneur clubs or forums in which students that are contemplating a start-up or are already operating a business can share information and experiences.

c. State Support of customized technical assistance and training provided by non-profit intermediaries

The State of West Virginia should promote and support non profit intermediaries' provision of custom designed technical assistance and training for their targeted entrepreneurial clients.

West Virginia's Non profit Intermediaries for Entrepreneurs play a vital role in providing a learning environment for entrepreneurs of all ages and business aspirations. Intermediaries help their client base of entrepreneurs develop skills, knowledge and confidence that to help them achieve the success that they determine. The style is usually not academic and relies on principles of adult education and informal learning techniques.

Examples of customized educational services provided by non profit intermediaries: The Center for Economic Options provides knowledge services for small scale manufacturers including training market access, test market learning, product assessment and feedback, and related technical assistance and training; Tamarack and Mountainmade.com provide feedback on the craft jurying process and offer training related to arts and crafts; and Unlimited Futures offers processed food-specific technical assistance and related business training.

Summary and Implications

Entrepreneurship education is essential for the creation of a strong entrepreneurial climate in West Virginia. There is a framework and infrastructure already in place to deliver these programs, and individuals in the state with the experience to help expand these programs. While initial progress has been made, further development these types of programs have suffered substantially with the budget reductions to higher education in recent years. Financing these efforts as part of a development strategy, with the funding being directed toward specific centers or institutes, rather than as part of general education funding is the only way to ensure further progress.

VII. Intellectual Capital

One area in which states are making substantial contributions to an entrepreneurial economy is through investment in, and policies related to, the utilization of intellectual capacity, primarily through state universities and colleges. In Iowa, the governor and legislature enacted increased budgetary support for the three regents institutions including endowed chairs, incubators and matching funds for public/private partnerships.

The costs of patenting and protecting intellectual property rights is prohibitive for most fledgling entrepreneurs. The development agencies and the State Legislature must be pro-active in putting together a standardized system that will greatly reduce the costs for the entrepreneurs involved to commercialize and protect intellectual properties.

a. Faculty and Cooperative Research Policies

There is a widespread belief among most entrepreneurial stakeholders in West Virginia that commercialization of academic research has never been given a high priority in West Virginia and attempts to commercialize applications have not been effective. The commercialization gap must be addressed through a rigorous commercialization strategy. Every effort should be made to partner our major research universities with experts in the field of commercialization of academic research and development. Besides the missed opportunity that this represents, in terms of a failure of to leverage publicly funded research for entrepreneurial purposes for the further benefit of the State, it also contributes to the reluctance of large research organizations to locate their research and development in West Virginia.

The long-standing weakness regarding the effective transfer of research and development should be tackled as a matter of priority. The poor performance may be a result of an inadequate incentive system and the associated cultural and social norms.

States are encouraging collaboration between state universities and the private sector through changes in university policies that (1) reward faculty for their contribution to commercialization of university-based research and (2) promote cooperative research with for-profit entities. In 1997, as part of a new collective bargaining agreement with its faculty, the University of Hawaii increased a faculty member's share of the revenues from intellectual property licensing and commercialization to fifty percent (50%). While Hawaii's policy is the most generous in terms of the faculty member's share of revenues, other states including California, Mississippi and Rhode Island have also liberalized their faculty research policies.

In terms of cooperative research, the Arizona Board of Regents has adopted new policy that allows state universities to negotiate cooperative arrangements with companies that want to use university facilities to commercialize new technologies. In particular, it encourages companies to sponsor research with an assurance the private sector partner can acquire the rights to any technology that might result from the cooperative effort.

West Virginia University's Entrepreneurship Center has begun a program that uses student interns to help in commercialization efforts. Not only does this help students learn the entrepreneurial process, but it also leads to many post-graduation job opportunities. While this program is still too young to assess in terms of commercial outcomes, it is an example of a creative solution that helps to improve the usage of intellectual capital in West Virginia.

Summary and Implications

States clearly recognize the important contribution that universities and related institutions make to an economy that relies on innovation and technology. This is evidenced by both a range of activities—direct investment, leveraging public funds, and policies that encourage private sector collaboration and faculty participation—that expand the states' intellectual infrastructure. State investment in intellectual capacity increases in importance as federal research and development investments either decline or remain static. The remaining question is the extent to which this trend results in the development and commercialization of new technologies. If they have not done so, states might consider methodologies for benchmarking and evaluating the benefits associated with state investment in intellectual capacity.

VIII. Legislative and Public Policy Recommendations

In order to compete with neighboring states and to begin the development of a culture of entrepreneurship in West Virginia, the Entrepreneurship Committee of Vision Shared has identified and adopted several legislative and public policy recommendations. The legislative and public policy considerations contained below address the areas of critical importance to entrepreneurs – (a) the perception of entrepreneurship in West Virginia; (b) the entrepreneurial infrastructure; (c) a cluster-based economic development approach (d) the tax structure; (e) education; and (f) intellectual capital.

a. Perception of Entrepreneurship

- The Governor should establish the ***Governor's Award for Entrepreneurial Excellence and Development*** and additional rewards and recognition to promote and recognize entrepreneurial talent around the State. The effort should be structured by age, so that K-12 students, post-secondary students, and adults can compete and collaborate with peers with regional awards to include all parts of the State of West Virginia.

- Raising the profile of successful entrepreneurs is critical in both sparking interest among those thinking about starting a new venture and creating a supportive environment in which entrepreneurship can flourish. Through a direct effort to market West Virginia's efforts in the area of small business and entrepreneurship, we will become identified as a state friendly to business and entrepreneurial development. We will market our successes to newspapers throughout the region, the Wall Street Journal and other industry and business trade publications. Perception is eighty percent of the challenge and a focused, strategic effort to grow the perception that WV is business friendly will move the state a great deal closer to a realization of better jobs and retention of critical state assets.

b. Entrepreneurial Infrastructure

- **Governor's Council for Entrepreneurship and Re-naming the WVSBDC as the WVESBDC** – The Governor should (i) establish a Governor's Council for Entrepreneurship and (ii) work with the legislature and the Council for Community and

Economic Development to rename the Small Business Development Center as the Entrepreneurship and Small Business Development Center ("ESBDC").

- **a)** The Governor's Council would be headed up by the Governor or his designate and staffed by the ESBDC. The ESBDC would be responsible to ensure that all relevant state departments and agencies recognize the importance of entrepreneurship as a strategy for long-term economic development and that activities therein are coordinated and results oriented.

- **b)** The ESBDC would marshal state resources, foster inter-departmental collaboration, keep the legislature informed of progress in implementing the strategy, and be a member of various statewide economic development commissions. Such a "champion" of entrepreneurship and small business issues could constantly keep the entrepreneurial agenda at the fore; provide leadership in strengthening the supportive cultural norms by emphasizing the values of entrepreneurship and entrepreneurs within all facets of West Virginia; identify any blocks to the attainment of the full contribution of entrepreneurship the to economy of West Virginia; and set outcome measures and certify entrepreneurial development organizations in West Virginia. A key aspect to this position shall be an ongoing government reform aspect to streamline regulations and other reporting requirements for entrepreneurs and small business.

- **Entrepreneurship Alliance -** In order to provide coordination, increase communication, and encourage regional and statewide entrepreneurial development plans, an Entrepreneurship Alliance should be established, and organized by Vision Shared. The State Entrepreneurship and Small Business Director and the Governor's Council on Entrepreneurship should coordinate the Entrepreneurship Alliance activities. This Alliance will be inclusive of all entrepreneurial stakeholders. The intent of such an Alliance shall be to serve as a communication mechanism among West Virginia entrepreneurial stakeholders, to develop regional and statewide plans with respect to entrepreneurial development, and to coordinate necessary activities with the State Entrepreneurship and Small Business Director. The State Entrepreneurship and Small Business Director shall serve as the Chairperson of the Alliance and an annual Entrepreneurship Alliance Conference shall be called to develop and integrate entrepreneurial development efforts with the State Entrepreneurship and Small Business Director through the develop of an Annual Report on Entrepreneurship in West Virginia.

- **Nonprofit Social-Purpose Intermediaries** – Social Purpose Intermediaries serve entrepreneurs through a variety of mechanisms including commercial kitchens, marketing services, capital access, business incubators, customized training and technical assistance, and through a variety of advocacy roles. The State should provide matching grants (to a maximum permitted annual amount) to all nonprofit social-purpose intermediaries that provide these services.. In order to qualify for matching grant funding, each intermediary must meet the needs of entrepreneurs within a specific market segment. For instance, The Center for Economic Options meets the market access and market-related training needs of the state's small-scale manufacturers. Funding support would be limited to activities expressly stated in each intermediary's business plan.

- **Entrepreneurial League System -** The Entrepreneurial League System should be adopted by the WVSBDC and incorporated into its statewide effort with respect to training entrepreneurs and small business persons.

- **Local Entrepreneurship Councils –** A local framework of entrepreneurship councils should be established. Such councils shall work through and be coordinated by the State Entrepreneurshipand Small Business Director. It may be that a framework is presently in place that could be adapted to satisfy this policy point.

- **Workforce Development Grants** – Workforce Development Grant process must be amended to support entrepreneurship training the same way that it provides funding to train for other skills. For example, if an employee is downsized, the downsized employee should be eligible to take a curriculum that helps them start a small business. These grants are currently being used to support entrepreneurial training in some of the WIB Regions. All the WIBs must adopt such training. Under federal law and regulation, the seven local WIBs are independent organizations that are not controlled by the WVDO - WVDO is merely the funding mechanism. The purpose of this independence is to allow the WIBs to tailor their training deliverables to local needs. Entrepreneurship training must be coordinated into all WIB regions.

c. Cluster-based Economic Development Approach

The cluster-based approach represents a major shift in economic development planning. This is a shift from an individual firm oriented approach to a plan based on the benefits of building upon industry-focused benefits. Popularized by Harvard Economist Michael Porter, he argues that competition is the key driver behind cluster development. As one competitive firm grows, it generates demand for other related industries. As a cluster develops, it becomes a mutually reinforcing system where the benefits flow backwards and forwards throughout the industries in the cluster. Porter argues that it is competition between rival firms in the cluster drives growth because it forces firms to be innovative and to improve and create new technology. This, in turn leads to new business spin-offs, stimulates R&D, and forces the introduction of new skills and services.

Michael Porter defines clusters this way:

> *Clusters are geographic concentrations of inter-connected companies and institutions in a particular field. Clusters encompass an array of linked industries and other entities important to competition. They include, for example, suppliers of specialized inputs such as components, machinery, and services, and providers of specialized infrastructure. Clusters also often extend downstream to channels and customers and laterally to manufacturers of complementary products and to companies in industries related by skills, technologies or common inputs. Finally, many clusters include governmental and other institutions - such as universities, standard-setting agencies, think tanks, vocational training providers, and trade associations - that provide specialized training, education, information, research, and technicalsupport.*

"On Competition", by Michael E. Porter, Harvard Business Review Books, 1998.

Many states have made a commitment to defining and implementing a Cluster-based Economic Development plan that is based on leveraging existing strengths combined with a definitive understanding of emerging industries worthy of investment and focus. More strategic longer-term economic development in this form is a critical component of the infrastructure needed to stimulate a "pipeline" of new business creation and innovation. Many states have committed to such plans. An example of one such study is the "State of the Industry Report" produced by the Pittsburgh Technology Council in 2000 which focuses on the 13 county Southwestern Pennsylvania region.

A Cluster-based Economic Development approach that recognizes existing investments and strengths in certain research and development technologies of West Virginia University and Marshall University and enforces long-term commitment of focused future investments would reap substantial benefits. West Virginia is a state of limited resources and it is vital that these resources are invested in directions that are aligned to support proven strategic economic development efforts such as cluster development.

d. Tax Policy

- **Patent and Copyright Tax Exclusion -** Recognizing the importance of non-tangible assets to entrepreneurs, all business income derived from patents and copyrights created in West Virginia should be excluded from corporate income taxation. Hawaii adopted this as part of their effort to attract high-technology jobs and similar proposals are being considered by at least two other states.

- **Capital Gains Tax Rate Reduction -** Currently the state of West Virginia taxes capital gains at the federal tax rate (15%). Seventeen states either do not tax capital gains on the state level or they have adopted a modified lower rate. Arkansas applies a maximum 6% rate on capital gains while Idaho and Wisconsin exclude 60% of capital gains from state taxation. Massachusetts adopted a graduated exclusion based on the number of years that an asset is held. As implemented in Massachusetts, capital gains on assets held less than two years are taxed at a 5% rate while assets held more than 6 years are excluded from capital gains taxes. Capital gains taxes are critical because entrepreneurship is characterized as the continuous reinvestment of wealth in new businesses and building additional enterprises is partially a function of an entrepreneur's ability to retain income from previous endeavors.

- **Angel Investment Tax Credit -** The State should enact an angel investment personal income tax credit for investors in small technology businesses. Early stage or seed investors in technology businesses are most often drawn from seasoned entrepreneurs and wealthy individuals. Venture capital firms often do not come into the seed funding stage because they are focused on growing, high potential technology businesses rather than still unproven business concepts. A personal income tax credit for angel investors should be set as a percentage of investment and capped at a certain dollar value. Virginia enacted a 25% credit up to a total contribution dollar value of $50,000 thereby allowing an investor at the maximum level to attain a $12,500 state tax credit. The credit should be limited to investments in companies with 25 or fewer full time equivalent employees, should be nonrefundable, but would be allowed to roll over any unused credit for a maximum of five (5) years. The Legislature enacted a High Tech Investment Tax Credit this year. Although the overall legislation is a big step in the right direction, the annual cap on the tax credit is $1 million and it is limited to certified research and development companies. We must move for a larger tax credit that is available to all sectors of the entrepreneurial community.

- **Student Employment Tax Credit –** West Virginia companies with gross revenues less than or equal to $1,500,000 should receive a tax credit for hiring students from West Virginia based colleges and universities. The credit shall be limited to students in highly sought fields of science, math and technology. The incentive is to encourage West Virginia business to retain our best and brightest and to strengthen that effort through financial incentives. (This is similar to the tax credit for veteran's set forth in WV Code Section 11-21-42 and 21A-2C-1).

- **Exemptions from municipal Business and Occupation Taxes for Small Business or Home Rule with the development of a West Virginia Municipal Certification Board -** Cities such as Charleston, Morgantown and Huntington should create exemptions to local taxation to encourage the development of small business and new economic engines. The result would be increased revenues through the development of a larger tax base and a growing economy. Additional, the exemption would provide additional incentives for the formation of local businesses. As mentioned earlier, B&O tax performs poorly in terms of efficiency and equity. The B&O tax, however, is the single largest revenue source for most municipalities in West Virginia. Therefore, the B&O tax should be eliminated for those cities and municipalities that are certified by a West Virginia Municipal Certification Board and those related revenues replaced by local sales and use taxes and local income taxes.

- **Manufacturing and R&D Equipment Property Tax Exclusion -** West Virginia must exempt equipment purchased for manufacturing and for research and development from personal property tax assessments. Such a position would give West Virginia a leg up on many of our neighboring states. This would remove an inherent tax on capital formation. The tax exemption should be phased in over three years to minimize the effect of the exemption on an annual basis. WV Code Chapter 11 Article 6 deals with this in a similar mode. There is an exemption for manufacturing tools and dies which stems back to the steel industry that would be comparable to what we are seeking today – to be friendly as a State to high technology and small business.

e. Education

- **Post-Secondary Entrepreneurial Education –** To encourage the development of entrepreneurial oriented courses at West Virginia schools of higher education, the State should offer a maximum award of $15,000 for the development of new courses or related business plan competitions that teach entrepreneurship. Courses must include basic business planning fundamentals, result in student projects that are reviewed by business professionals, and the course must be available across all student academic disciplines.

- **Entrepreneurship Centers –** The State should provide matching grants (to a maximum permitted annual amount) to all higher education institutions (universities, colleges and community colleges) for Entrepreneurshipand Small Business Development Centers. In order to qualify for matching grant funding, each Center must be open and available to all student disciplines and all citizens of the community and each center must conduct an annual business plan competition open to all students across all disciplines. The concept is simple. If Fairmont State College can raise or commit $100,000, the State of West Virginia should match that funding with a grant in the amount of $100,000. Funding support would be limited to certain types of expenditures and all funding would be limited to an annual maximum funding rate.

- **Faculty Research Revenues –** West Virginia University and other state research performing universities must work to strengthen the incentives for faculty researchers for intellectual property licensing and commercialization. The University of Hawaii increased a faculty member's share to 50% of commercialized revenues. Other states' too have been aggressive in the attempt to grow intellectual property development through faculty member incentives. West Virginia University, for example, limits a faculty member's share to approximately 30% with respect to patents. Faculty research policies should be liberalized and loosened to create incentives for the development and commercialization of intellectual property. Additional faculty research support should also be offered to those doing academic research on entrepreneurship and its role in economic development.

- **West Virginia Board of Trustees Commercialization Policies –** The West Virginia Board of Trustees should adopt a policy that allows state universities to negotiate cooperative agreements with companies that want to use university facilities to commercialize new technologies. In particular, companies should be encouraged to sponsor research with an assurance that the private sector partner can acquire the rights to any technology that might result from the cooperative effort.

- **Entrepreneurship Education (K-12) and Director of Entrepreneurship Education -** The West Virginia Department of Education should commit to incorporating entrepreneurial education programs in all West Virginia school districts. The education programs should be incorporated into elementary, secondary, and vocational education programs. Additionally, the West Virginia Department of Education should appoint a Director of Entrepreneurship Education to foster and develop entrepreneurship programs.

- **Summit on Entrepreneurship and Education –** The integration of entrepreneurship and education is critical to the development of a 'culture' of entrepreneurship in West Virginia.

f. Intellectual Property

- **West Virginia Enterprise and Innovation Fund -** Development of a West Virginia Enterprise and Innovation Fund to provide matching grants for the development of business plans and to secure patents and test the technical feasibility of new products. This proposal is really a melding of activities in the States of Maryland and Delaware. Many small companies lack the resources to test the validity of a patent and many fewer companies have the resources to secure patent rights with the necessary patent search to establish the legal basis for the patent. The fund would be established to offset private patent firm expenses to secure patents and test the technical feasibility of new products.

- **Patent and Copyright Tax Exclusion –** see above.

- **Regional Cluster Development Plan –** In the event that West Virginia University and Marshall University begin to leverage their ability to commercialize and develop certain research and development technologies, the State of West Virginia can reap substantial benefits. Upon an institutional turnaround from West Virginia University and a recognition of an institutional obligation to the State and the region, north-central West Virginia will be in a position to capitalize of high technology in the biotech, energy, and applied sciences. West Virginia is a state of limited resources and it is vital that these resources are concentrated in particular directions rather than being spread too thinly. It is not possible for West Virginia to have a competitive advantage in all sectors, even in all high tech or energy sectors.

g. Miscellaneous

- **Support for Entrepreneurs in the National Guard and Reserves** – West Virginia has one of the nation's highest percentages of its population serving in the National Guard and Reserves. If West Virginia is attempting to drive its economy by developing entrepreneurism, then it needs to develop mechanisms that will protect entrepreneurs and microbusiness-owning Guard and Reservists during times of deployment. This protection should also extend to small-scale business owners that lose critical numbers of employees due to deployment. Guard members and Reservists that work for themselves are hard-pressed to maintain their business interests while deployed, and have few, if any, resources available to them to help rebuild their businesses upon their return. The state should develop an affirmative plan to help entrepreneurs impacted by deployments to reactivate their businesses upon return, and provide a financial safety-net to protect these entrepreneurs from devastating losses.

- **Development of a Statewide Health Insurance Plan for Small-business Owners -** Many state policies can benefit both entrepreneurs and small business operators. Following the lead of the Missouri General Assembly, West Virginia legislators should introduce bills that would allow businesses with 50 or fewer employees to participate in a pooled health insurance plan. The state would use its purchasing power (associated with the government employees insurance program) to obtain better rates and terms than individual businesses could obtain on their own. The ability to purchase reasonably priced health insurance is critical to establishing a culture that supports and promotes entreprenuerism.

- **State and Local Government Procurement Policies –** There is no legal requirement from the state and local units of governments to follow any particular method of procurement. This lack of methodology simply perpetuates the traditional 'good-ol' boy' perception of government contracting. The State of West Virginia and its University procurement systems have no method or process for tracking the types of business (small, woman-owned, minority, etc.) are its vendors. To work well, a software tracking system must be connected to the State's payment system, something that has not been accomplished to date. The current methodology is simply a voluntary effort by vendors for purchases over $10,000. In addition to tracking procurement activity, the State of West Virginia must provide procurement incentives for utilizing West Virginia based businesses. Any efforts by the WV Development Office to recruit out of state entities should require good faith efforts on the part of the incoming company to use West Virginia based vendors.

- **Immigration -** West Virginia must be proactive in the areas of progressive immigration policies. A study conducted of the Silicon Valley indicated that almost one-third of all high-technology businesses were run by Chinese-born or Indian-born engineers with companies employing more than 58,000 employees and sales of almost $17 billion. More than half of the immigrants who have been in the U.S. less than ten years had founded or run a start-up company. West Virginia must be active in its recruitment of immigrants moving to the United States. Population is an important factor in municipal financing. It provides the tax base and justifies the provision of public services. West Virginia has a low population density due to its rural landscape. It has had very low population growth rates in recent decades with periods of actual population losses. Municipalities in all population classes suffered population losses between 1990 and 2000. Absent an overnight turnaround in domestic population growth and demographic trends, West Virginia's population stagnation threatens the ability of its economy to grow and sustain its workforce. At the present rate of national demographic trends, in 2010, West Virginia will lose an additional Congressional seat to faster growing south and southwest states.

IX. Conclusion

To date, West Virginia's commitment in support of entrepreneurs is poor. While West Virginia funding for entrepreneurial development lags behind other economic development activities, many states have created programs or adopted policies that have a positive impact on entrepreneurs.

As research continues to make the connection between entrepreneurial activity and economic prosperity, West Virginia should re-examine its strategies, policies and programs to maximize the return on state economic development expenditures. State action is critical to entrepreneurs and to promote public innovations that contribute to the realization of a truly entrepreneurial economy. The literal transformation of West Virginia's economy into an entrepreneurial culture will only occur in a environment that promotes and develops entrepreneurs.

Policies with respect to perception, entrepreneurial infrastructure, tax, education and intellectual property must be addressed in a concerted effort in a bold and systematic fashion. Incremental change in the area of entrepreneurship will continue to leave West Virginia lagging its neighboring states. West Virginia must move as quickly as possible to promote a national perception of West Virginia as the "most entrepreneurial-friendly environment in the United States." There is simply no time for delay.