

JUNE 2010

Tax Credits for Angel Investors Will Become Available July 1, 2010

On May 6, 2010, Governor Jodi Rell signed into law a new tax credit for “angel investors” who invest in Connecticut start-ups.

The new law authorizes personal income tax credits for individuals who, along with other angel investors in the investor group, invest at least \$100,000 in Connecticut start-up businesses in specified sectors. The credit equals 25% of the cash investment, up to \$250,000.

The law limits the total credits all angel investors may claim to \$6 million per year in fiscal years 2011 and 2012 and \$3 million per year in each subsequent fiscal year until fiscal year 2019, when the credits will expire. Connecticut Innovations, Incorporated (“CII”) will administer the credits. Angels cannot claim credits against income earned on or after July 1, 2014.

Eligible Investors

An investor qualifies as an angel investor if he or she is an “accredited investor” under SEC rules (or a network of such accredited investors), so long as the investor is not:

1. someone who controls 50% or more of the business receiving the investment;
2. a venture capital company; or
3. any bank, savings and loan association, trust, insurance company, or similar entity for activities that are part of its normal business.

If the angel investor is an S Corporation or another entity treated as a partnership for federal income tax purposes, the credits may be claimed by the equity owners.

Businesses Eligible for Angel Investments

The bill specifies criteria a business must meet before an angel can invest in it and claim a credit. The business must engage in bioscience, advanced materials, photonics, information technology, clean technology, or any other “emerging technology,” as determined by the Commissioner of the Department of Economic and Community Development.

In addition, the business must have its principal place of business in Connecticut and have:

1. gross revenues under \$1 million in its most recent income year;
2. fewer than 25 employees, at least 75% of whom are Connecticut residents;
3. operated in Connecticut for less than seven consecutive years; and
4. received less than \$2 million in eligible investments from angel investors.

Lastly, the business’ managers and their families must be the primary owners and, as described below, the business must have been identified by CII as eligible for angel investment.

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Applying for Investment Credits

The act creates a mechanism for connecting businesses seeking angel investments with potential angel investors. A business seeking such an investment must apply to CII for approval. CII must create and maintain a list of such businesses and make it available to angel investors for review. In order for CII to approve an eligible business and add it to its list, the business must provide:

1. its name and a copy of its organizational documents;
2. a business plan describing the business and its management, product, market, and financial plans;
3. a description of its innovative and proprietary technology, product, or service;
4. a statement of its potential economic impact, including the number, types, and location of jobs it expects to create;
5. a description of the qualified securities to be offered and the amount of cash investment sought;
6. the amount, timing, and projected use of the proceeds from the sale of these securities; and
7. any other information CII requires.

CII's executive director will compile the list monthly, beginning by August 1, 2010.

Accessing the Credits

An angel investor who plans to invest in an eligible business must apply to CII to reserve tax credits. In doing so, the investor must identify the business and the amount he or she plans to invest.

The investor may claim the credit only for cash investments in the business's qualified securities, which can be any form of equity, including general or limited partnership interests, common stock, or preferred stock with or without voting rights and without regard to seniority position that must be convertible into common stock.

Using or Transferring Credits

Credits can be applied up to the total income tax an investor owes in a given year. The investor must claim the credit in the same year he or she invested the funds, but can carry forward unused credits for up to five succeeding years. Taxpayers receiving the credits cannot transfer them to other taxpayers.

Questions or Assistance?

If you have questions regarding the angel investor tax credit law, please contact any of the attorneys listed below:

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