



## [Startup America Suggestion of the Day: Angel Investment Tax Credits \(Installment 10\)](#)

By [Joe Wallin](#)

February 16, 2011

Senator Mark Pryor has introduced legislation that would give angel investors in qualifying small businesses (broadly defined) a federal income tax credit equal to 25% of the amount invested. You can find the text of the proposed legislation [here](#) and quoted in full below.

Senator Pryor's bill is a great idea. However, there are certain things about it that I would suggest changing.

First, the way the bill is currently drafted companies will have to apply to participate in the program. There is an overall cap on the dollar amount of the tax credits available under the program per year, and the government is going to play a role in deciding which companies qualify, including taking into account geographic areas that have traditionally been underserved by angel and venture capital investment. I would change this to a per taxpayer limit, to avoid the government having to run an application and approval process that will undoubtedly be very political.

Second, I would not limit the credit to only "accredited investors."

Third, I would take this opportunity to define "accredited investor" very broadly, and repeal the Dodd-Frank provisions which make it harder to qualify as an accredited investor.

### **S.256 — American Opportunity Act of 2011 (Introduced in Senate – IS)**

S 256 IS

112th CONGRESS

1st Session

**S. 256**

To amend the Internal Revenue Code of 1986 to allow a credit against income tax for equity investments in small business concerns.



## IN THE SENATE OF THE UNITED STATES

February 2, 2011

Mr. Pryor introduced the following bill; which was read twice and referred to the Committee on Finance.

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### A BILL

To amend the Internal Revenue Code of 1986 to allow a credit against income tax for equity investments in small business concerns.

*Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,*

### SECTION 1. SHORT TITLE.

This Act may be cited as the “American Opportunity Act of 2011.”

### SEC. 2. ANGEL INVESTMENT TAX CREDIT.

(a) In General- Subpart B of part IV of subchapter A of chapter 1 of the Internal Revenue Code of 1986 is amended by adding at the end the following new section:

#### SEC. 30E. ANGEL INVESTMENT TAX CREDIT.

(a) Allowance of Credit – There shall be allowed as a credit against the tax imposed by this chapter for the taxable year an amount equal to 25 percent of the qualified equity investments made by a qualified investor during the taxable year.

(b) Qualified Equity Investment – For purposes of this section –

(1) IN GENERAL – The term “qualified equity investment” means any equity investment in a qualified small business entity if –

(A) such investment is acquired by the taxpayer at its original issue (directly or through an underwriter) solely in exchange for cash, and



(B) such investment is designated for purposes of this section by the qualified small business entity.

(2) EQUITY INVESTMENT – The term “equity investment” means –

(A) any form of equity, including a general or limited partnership interest, common stock, preferred stock (other than nonqualified preferred stock as defined in section 351(g)(2)), with or without voting rights, without regard to seniority position and whether or not convertible into common stock or any form of subordinate or convertible debt, or both, with warrants or other means of equity conversion, and

(B) any capital interest in an entity which is a partnership.

(3) REDEMPTIONS – A rule similar to the rule of section 1202(c)(3) shall apply for purposes of this subsection.

(c) Qualified Small Business Entity – For purposes of this section –

(1) IN GENERAL – The term “qualified small business entity” means any domestic corporation or partnership if such corporation or partnership –

(A) is a small business (as defined in section 41(b)(3)(D)(iii)),

(B) has its headquarters in the United States,

(C) is engaged in a high technology trade or business related to –

(i) advanced materials, nanotechnology, or precision manufacturing,

(ii) aerospace, aeronautics, or defense,

(iii) biotechnology or pharmaceuticals,

(iv) electronics, semiconductors, software, or computer technology,

(v) energy, environment, or clean technologies,

(vi) forest products or agriculture,

(vii) information technology, communication technology, digital media, or photonics,



(viii) life sciences or medical sciences,

(ix) marine technology or aquaculture,

(x) transportation, or

(xi) any other high technology trade or business as determined by the Secretary,

(D) has been in existence for less than 5 years as of the date of the qualified equity investment,

(E) employs less than 100 full-time equivalent employees as of the date of such investment,

(F) has more than 50 percent of the employees performing substantially all of their services in the United States as of the date of such investment, and

(G) has equity investments designated for purposes of this paragraph.

(2) DESIGNATION OF EQUITY INVESTMENTS – For purposes of paragraph (1)(G), an equity investment shall not be treated as designated if such designation would result in the aggregate amount which may be taken into account under this section with respect to equity investments in such corporation or partnership exceeds –

(A) \$10,000,000, taking into account the total amount of all qualified equity investments made by all taxpayers for the taxable year and all preceding taxable years,

(B) \$2,000,000, taking into account the total amount of all qualified equity investments made by all taxpayers for such taxable year, and

(C) \$1,000,000, taking into account the total amount of all qualified equity investments made by the taxpayer for such taxable year.

(d) Qualified Investor – For purposes of this section –

(1) IN GENERAL – The term “qualified investor” means an accredited investor, as defined by the Securities and Exchange Commission, investor network, or investor fund who review new or proposed businesses for potential investment.

(2) INVESTOR NETWORK – The term “investor network” means a group of accredited investors organized for the sole purpose of making qualified equity investments.



### (3) INVESTOR FUND -

(A) IN GENERAL – The term “investor fund” means a corporation that for the applicable taxable year is treated as an S corporation or a general partnership, limited partnership, limited liability partnership, trust, or limited liability company and which for the applicable taxable year is not taxed as a corporation.

### (B) ALLOCATION OF CREDIT -

(i) IN GENERAL – Except as provided in clause (ii), the credit allowed under subsection (a) shall be allocated to the shareholders or partners of the investor fund in proportion to their ownership interest or as specified in the fund’s organizational documents, except that tax-exempt investors shall be allowed to transfer their interest to investors within the fund in exchange for future financial consideration.

(ii) SINGLE MEMBER LIMITED LIABILITY COMPANY – If the investor fund is a single member limited liability company that is disregarded as an entity separate from its owner, the credit allowed under subsection (a) may be claimed by such limited liability company’s owner, if such owner is a person subject to the tax under this title.

### (4) EXCLUSION – The term “qualified investor” does not include –

(A) a person controlling at least 50 percent of the qualified small business entity,

(B) an employee of such entity, or

(C) any bank, bank and trust company, insurance company, trust company, national bank, savings association or building and loan association for activities that are a part of its normal course of business.

### (e) National Limitation on Amount of Investments Designated -

(1) IN GENERAL – There is an angel investment tax credit limitation of \$500,000,000 for each of calendar years 2011 through 2015.

(2) ALLOCATION OF LIMITATION – The limitation under paragraph (1) shall be allocated by the Secretary among qualified small business entities selected by the Secretary.

(3) CARRYOVER OF UNUSED LIMITATION – If the angel investment tax credit limitation for any calendar year exceeds the aggregate amount allocated under paragraph (2) for such year,



such limitation for the succeeding calendar year shall be increased by the amount of such excess. No amount may be carried under the preceding sentence to any calendar year after 2020.

(f) Application With Other Credits -

(1) BUSINESS CREDIT TREATED AS PART OF GENERAL BUSINESS CREDIT – Except as provided in paragraph (2), the credit which would be allowed under subsection (a) for any taxable year (determined without regard to this subsection) shall be treated as a credit listed in section 38(b) for such taxable year (and not allowed under subsection (a)).

(2) PERSONAL CREDIT -

(A) IN GENERAL – In the case of an individual who elects the application of this paragraph, for purposes of this title, the credit allowed under subsection (a) for any taxable year (determined after application of paragraph (1)) shall be treated as a credit allowable under subpart A for such taxable year.

(B) LIMITATION BASED ON AMOUNT OF TAX – In the case of a taxable year to which section 26(a)(2) does not apply, the credit allowed under subpart A for any taxable year (determined after application of paragraph (1)) by reason of subparagraph (A) shall not exceed the excess of –

(i) the sum of the regular tax liability (as defined in section 26(b)) plus the tax imposed by section 55, over

(ii) the sum of the credits allowable under subpart A (other than this section) and section 27 for the taxable year.

(C) CARRYFORWARD OF UNUSED CREDIT – If the credit allowable under subsection (a) by reason of subparagraph (A) exceeds the limitation imposed by section 26(a)(1) or subparagraph (B), whichever is applicable, for such taxable year, reduced by the sum of the credits allowable under subpart A (other than this section) for such taxable year, such excess shall be carried to each of the succeeding 20 taxable years to the extent that such unused credit may not be taken into account under subsection (a) by reason of subparagraph (A) for a prior taxable year because of such limitation.

(g) Special Rules -

(1) RELATED PARTIES – For purposes of this section –



(A) IN GENERAL – All related persons shall be treated as 1 person.

(B) RELATED PERSONS – A person shall be treated as related to another person if the relationship between such persons would result in the disallowance of losses under section 267 or 707(b).

(2) BASIS – For purposes of this subtitle, the basis of any investment with respect to which a credit is allowable under this section shall be reduced by the amount of such credit so allowed. This subsection shall not apply for purposes of sections 1202, 1397B, and 1400B.

(3) RECAPTURE – The Secretary shall, by regulations, provide for recapturing the benefit of any credit allowable under subsection (a) with respect to any qualified equity investment which is held by the taxpayer less than 3 years, except that no benefit shall be recaptured in the case of –

(A) transfer of such investment by reason of the death of the taxpayer,

(B) transfer between spouses,

(C) transfer incident to the divorce (as defined in section 1041) of such taxpayer, or

(D) a transaction to which section 381(a) applies (relating to certain acquisitions of the assets of one corporation by another corporation).

(h) Regulations – The Secretary shall prescribe such regulations as may be appropriate to carry out this section, including regulations –

(1) which prevent the abuse of the purposes of this section,

(2) which impose appropriate reporting requirements, and

(3) which apply the provisions of this section to newly formed entities.

(b) Credit Made Part of General Business Credit- Subsection (b) of section 38 of the Internal Revenue Code of 1986 is amended –

(1) in paragraph (35), by striking “plus”;

(2) in paragraph (36), by striking the period at the end and inserting “, plus”; and



(3) by adding at the end the following new paragraph:

“(37) the portion of the angel investment tax credit to which section 30E(f)(1) applies.”

(c) Conforming Amendments –

(1) Section 1016(a) of the Internal Revenue Code of 1986 is amended by striking “and” at the end of paragraph (36), by striking the period at the end of paragraph (37) and inserting “, and”, and by inserting after paragraph (37) the following new paragraph:

“(38) to the extent provided in section 30E(g)(2).”

(2) Section 24(b)(3)(B) of such Code is amended by striking “and 30D” and inserting “30D, and 30E”.

(3) Section 25(e)(1)(C)(ii) of such Code is amended by inserting “30E,” after “30D,”.

(4) Section 25A(i)(5)(B) of such Code is amended by striking “and 30D” and inserting “, 30D, and 30E”.

(5) Section 25A(i)(5) of such Code is amended by inserting “30E,” after “30D,”.

(6) Section 25B(g)(2) of such Code is amended by striking “and 30D” and inserting “30D, and 30E”.

(7) Section 26(a)(1) of such Code is amended by striking “and 30D” and inserting “30D, and 30E”.

(8) Section 30(c)(2)(B)(ii) of such Code is amended by striking “and 30D” and inserting “, 30D, and 30E”.

(9) Section 30B(g)(2)(B)(ii) of such Code is amended by striking “and 30D” and inserting “30D, and 30E”.

(10) Section 30D(d)(2)(B)(ii) of such Code is amended by striking “and 25D” and inserting “, 25D, and 30E”.

(11) Section 904(i) of such Code is amended by striking “and 30D” and inserting “30D, and 30E”.



(12) Section 1400C(d)(2) of such Code is amended by striking “and 30D” and inserting “30D, and 30E”.

(d) Clerical Amendment – The table of sections for subpart B of part IV of subchapter A of chapter 1 of the Internal Revenue Code of 1986 is amended by adding at the end the following new item:

“Sec. 30E. Angel investment tax credit.”

(e) Effective Date – The amendments made by this section shall apply to investments made after December 31, 2010, in taxable years ending after such date.

(f) Regulations on Allocation of National Limitation – Not later than 120 days after the date of the enactment of this Act, the Secretary of the Treasury or the Secretary’s delegate shall prescribe regulations which specify —

(1) how small business entities shall apply for an allocation under section 30E(e)(2) of the Internal Revenue Code of 1986, as added by this section,

(2) the competitive procedure through which such allocations are made,

(3) the criteria for determining an allocation to a small business entity, including –

(A) whether the small business entity is located in a State that is historically underserved by angel investors and venture capital investors,

(B) whether the small business entity has received an angel investment tax credit, or its equivalent, from the State in which the small business entity is located and registered,

(C) whether small business entities in low-, medium-, and high-population density States are receiving allocations, and

(D) whether the small business entity has been awarded a Small Business Innovative Research or Small Business Technology Transfer grant from a Federal agency,

(4) the actions that such Secretary or delegate shall take to ensure that such allocations are properly made to qualified small business entities, and

(5) the actions that such Secretary or delegate shall take to ensure that angel investment tax credits are allocated and issued to the taxpayer.



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(g) Audit and Report- Not later than January 31, 2014, the Comptroller General of the United States, pursuant to an audit of the angel investment tax credit program established under section 30E of the Internal Revenue Code of 1986 (as added by subsection (a)), shall report to Congress on such program, including all qualified small business entities that receive an allocation of an angel investment credit under such section.

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