Angel Investor Tax Credits

by Norton Francis

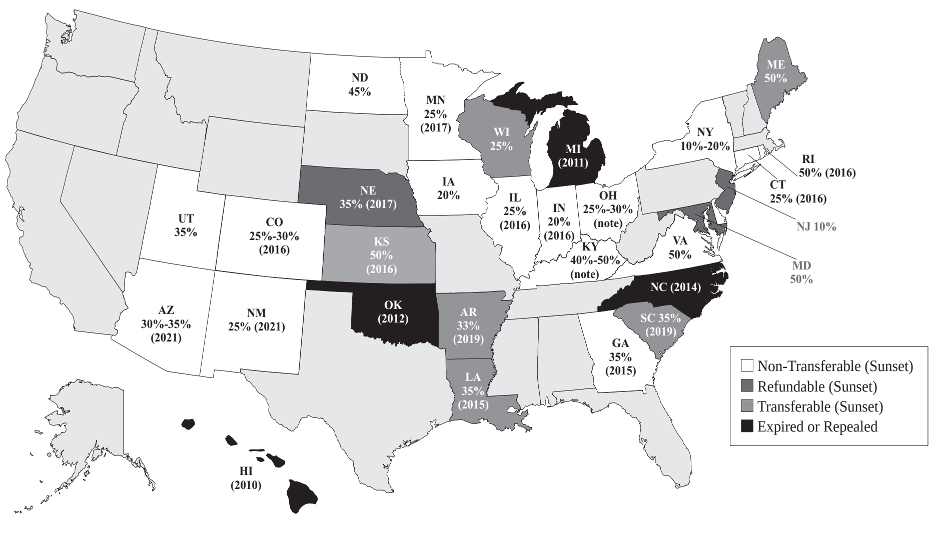
Hoping to attract investment dollars, 29 states have enacted so-called angel investor tax credits since 1988. Eligible investors generally are high-net-worth individuals, referred to as "angels," able to judge and accept the high level of risk associated with direct investments in new companies. Most states base eligibility for the credit on the federal definition of accredited investor as someone with a net worth of more than $1 million, excluding primary residence, and annual income of more than $200,000 for the two most recent years. Pooled investment funds and businesses can also be eligible, but rules vary by state.

Most credits share common features. They generally range from 25 to 50 percent of the amount invested, with limits on the types of investment (for example, high-tech). Most states either cap the total annual amount of credit the state can provide for all investors (totals vary widely), have a sunset date when the credit will expire, or set a cap on the total amount of the credit. Most of the credits are still within the sunset period, but three states have let their credits expire and Michigan repealed its credit.

If the credit exceeds liability, it can be carried forward in most states to offset future tax liability. In nine states, the credit is either refundable (the amount above liability is refunded to the investor) or transferable (the credit can be transferred to another taxpayer), attractive features for out-of-state investors who have little or no in-state tax liability.

Angel investor credits are seen as an economic development tool for attracting local investment, with hopes that high-tech centers will develop into miniature Silicon Valleys. However, some research suggests investment might have occurred even without the credit, raising questions about whether the benefits exceed the costs.[1] ✰

[1] Scott Shane, "The Problem With Tax Credits for Angel Investors," *Bloomberg Businessweek,* Aug. 20, 2010.



Note: Kentucky credit expires when lifetime aggregate value reaches $40 million; Ohio credit expires when lifetime value reaches $45 million.
Source: Tax Policy Center.