



CLIENT ALERT

GEORGIA ANGEL INVESTOR TAX CREDIT

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The Georgia Angel Investor Tax Credit (“AITC”) went into effect on January 1, 2011. The AITC allows certain qualified investors in Georgia start-up and early-stage companies a tax credit of up to \$50,000 annually. Georgia-based start-up and early-stage companies interested in raising capital may find the AITC helps court investors, while investors may be attracted to the tax benefits under the credit for qualifying investments. This client alert will provide key information on the mechanics of the AITC for interested companies and investors.

The Credit

The AITC equals 35% of the amount invested in a qualified start-up company and is available for investments made in 2011, 2012, 2013, 2014 and 2015. The credit can be used beginning with the second year following the year a qualified investment is made. In other words, an investor who makes a qualified investment in 2011 is eligible to first utilize the AITC in the 2013 tax year.

An investor can make an unlimited number of investments, though the aggregate amount of credit that may be awarded and applied against his taxable income under the AITC is \$50,000 annually. Thus, the annual maximum tax credit of \$50,000 can be obtained by investing at least \$142,857 into one or more eligible businesses per year. At this level, the credit will offset \$833,333 in Georgia taxable income at the 6% tax rate.

Georgia law provides a limit of \$10M in AITC credits that can be awarded annually to investors who invested in years 2011, 2012 or 2013, taking all qualified investments in the aggregate. The limit for investments made in 2014 or 2015 is \$5M. The credits will be prorated among investors in case of excess applications. If the investor does not use an entire credit in any one year, it may be carried forward five years from the close of the year the qualified investment was made. However, the credit cannot be carried backward.

	Investor Limit per Year	Total AITC per Year	Total AITC for 3 Years
Maximum investment	\$142,857	\$28,571,429	\$85,714,286
Maximum credit available	\$50,000	\$10,000,000	\$30,000,000
Income to offset with credit	\$833,333	\$166,666,667	\$500,000,000

Qualifying Investors

In order to be eligible for the AITC, angel investors must be “accredited investors” as defined by the Securities and Exchange Commission in Regulation D. The investor must also be either (a) an individual who is obligated to pay Georgia income taxes or (b) a pass-through entity (S-corporation, limited liability company or partnership) owned by individuals that is formed for investment purposes, has no business operations and has committed capital under management of no more than \$5 million. Venture capital funds, hedge funds, and commodity funds with institutional investors do not qualify.

Qualifying Investment

To be eligible for the AITC, a qualified investor must make a cash investment in a qualified business in exchange for (a) common or preferred stock or other equity interest, or (b) an unsecured subordinated note with a maturity of less than 5 years. The funds cannot have been raised as a result of another tax incentive program. Further, no commissions or other remuneration may be paid directly or indirectly for solicitation of the investment.

Qualifying Businesses

In order for a business to qualify as an eligible investment under the AITC, the business must register with the Georgia Tax Commissioner using Form IT-QBR (a copy of which is attached) prior to receiving the investment capital. Upon approval (not upon filing the application), the business is considered an eligible investment for the purposes of the AITC for 12 months. To qualify, a business:

- must be a corporation, LLC, or partnership located in Georgia;
- must be organized no more than three years before the investment is made;
- cannot be engaged substantially in retail sales, real estate and construction, professional services, gambling, natural resource extraction, investment activities, insurance, or entertainment, amusement, recreation, or athletic or fitness activity for which an admission or membership is charged (a business is deemed to be substantially engaged in one of the above activities if its gross revenue from the activity exceeds 25% of its gross revenues in any fiscal year or it is established pursuant to its articles of incorporation, articles of organization, operating agreement or similar organizational documents to engage as one of its primary purposes such activity);
- must have its headquarters located in Georgia from the time the investment is made through the entire duration that an investor benefits from the credit;
- must employ 20 or fewer people at the time of registration;
- cannot have gross revenues that exceed \$500,000 in any prior fiscal year;
- cannot have obtained more than \$1 million in gross cash proceeds from issuing debt or equity instruments (not including commercial loans); and
- cannot have utilized the Georgia film tax credit.

A business may renew its registration with the Tax Commissioner as long as it remains a qualified business at the time of renewal.

Application and Approval

A qualified investor seeking to claim the AITC must submit an application on Form IT-QI-AP to the Georgia Department of Revenue (the "Department") between September 1 and October 31 of the year for which the tax credit is claimed. The credit is claimed two years after the investment is made. For example, for an investment made in 2013, the credit will need to be claimed between September 1 and October 31 of 2015. The Department will notify each qualified investor of the tax credits that have been tentatively approved and allocated to the investor by December 31 of the year in which the application was submitted. In the event the credit amounts on applications filed with the Department exceed the maximum aggregate \$10 million limit of tax credits, then the tax credits will be allocated among the qualified investors who filed a timely application on a pro rata basis.

Credit Recapture

Investors who have qualified for the AITC must follow certain provisions in order to retain the credit. For instance, credits must be recaptured if a qualified investor transfers any securities received in a qualifying investment to another person or entity within two years of the qualifying transaction. Additionally, credits must be recaptured if a qualified business redeems a qualified investor's stock or pays principal on any subordinated debt within five years of the date the qualifying investment was made. Recapture is not triggered if a qualified investor dies, transfers to a spouse incident to divorce, or if a merger, conversion, or sale of the qualified business occurs where the qualified investor does not receive cash or tangible property. Finally, a qualified investor or his/her immediate family may not participate in any operation of the qualified business for compensation within two years of the date the qualified investment was made. Compensation does not include stock or stock options.

In sum, the AITC provides a powerful incentive for investing in early-stage and start-up companies in Georgia. While the AITC has the potential to serve as a catalyst for start-up companies in Georgia, qualifying businesses and investors should take great care to comply with applicable AITC rules and conditions in order to avoid recapture.

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Michael Horten is a US and European educated lawyer with over 40 years' experience as a practicing attorney. Mr. Horten began his legal career with Sullivan & Cromwell in New York and Paris. He then spent 25 years with King & Spalding in Atlanta. At the end of 1999, he retired from the King & Spalding partnership to launch Horten CC, a virtual law firm that focuses on the needs of small to medium size companies, with particular emphasis on entrepreneurial growth companies.

Horten CC employs a non-traditional practice model that is based on two key philosophical underpinnings: First, Mr. Horten founded the firm on the premise that top-rate legal services do not have to be bundled with the "marble" and "mahogany" environment that typically is associated with those services. The firm has no central offices, no paper files and it uses the latest technology to create efficiencies. As a result, the firm's fees are considerably lower than those

charged by firms of comparable ability and quality. Second, Horten CC bills its clients for the value delivered and not for the time spent by the attorney. The firm does not keep track of every "six minutes," as is the norm in most law firms. The firm believes that its clients purchase its lawyers' skill, not their time. The firm's work is typically performed for a fixed fee.