



First Rhode Island Startups Closing in on Tax Credit Under New Stimulus Program

Henry Johnson 1/16/08

If Massachusetts is the New England innovation economy's Goliath (and we'd argue that it is), Rhode Island is David. And the state has a new weapon in hand as it goes up against its much larger neighbor: a targeted tax credit of up to \$100,000. Rhode Island hopes the credit will encourage investment in its up-and-coming high-tech and life sciences companies and help counter any temptations for them to head across the border to what's often viewed as more startup friendly Massachusetts (or anywhere else for that matter).

Will it work? Some answers might be coming soon. The six companies preliminarily approved for the Innovation Tax Credit Program last November will have their first opportunity to show proof of fulfilling the requirements later this month. Rhode Island will issue the first set of tax break certificates promptly after this review is complete, according to Melissa Withers, director of communications and market development at the Rhode Island Economic Development Corporation (RIEDC), whose organization oversees the program.

All of which means it's showtime for the ambitious effort, which is targeted specifically at encouraging investment in companies in health and life sciences, information technology and digital media, financial services, marine trades and defense technology, technical and educational services, and consumer and industrial products. Initially proposed by the Rhode Island Science and Technology Advisory Council, the program was signed into law back in 2006. But given the required public hearing process and other steps needed to put the law into operation, the first few eligible companies are only now coming up for final approval.

The idea behind the program is to offer investors or companies up to a 50 percent credit on any seed, venture, or equity investment in a startup (or fairly young) company in the target areas—with a maximum credit of up to \$100,000. To qualify, investments must be made in companies that produce traded goods or services and have had annual gross revenues of less than \$1 million in the previous two calendar years. And the firms themselves must be pre-approved for the program, meaning that RIEDC has reviewed the companies to make sure they fall into the required fields and fit the revenue parameters. Firms are also reviewed on the strength of their business plan and how well qualified the applicant is to accomplish it, the perceived economic impact of their business, how well the business supports a culture of entrepreneurship, and their potential for advancing Rhode Island's agenda of fostering an innovation economy, Withers says.

Presuming all goes well, the program provides a credit against tax liability on business corporation tax, franchise tax, or personal income tax: the company receiving the investment gets to stipulate (presumably in consultation with its investors) how the credit will be distributed. “The company could retain it for themselves, give it entirely or in part to the investor, or even give it to a subset of executive employees...or any combination thereof,” says Withers. Some investors, she notes, may not have a Rhode Island tax liability, or might just determine that the best way to support their investment is to use the credit to offset the company’s tax liability.

However the credit is to be used, being pre-approved is seen as attractive for startup companies as they seek investment, because it provides a keen incentive to potential investors to go ahead and take the plunge.

And so far, so good. A small wave of applications arrived last year as the program went into action, and the first half-dozen preliminary approvals were issued in November. The next phase of the process is set to begin on January 28. That’s when the RIEDC board of directors meets to start determining whether any of the firms approved in November have received investments in their businesses that qualify for the tax break. Firms have six months from the time of pre-approval to come before the board for this review, which involves submitting bank statements, cancelled checks, and so on to prove that a bona fide investment was actually made in the firm. Presuming all is well, says Withers, RIEDC will issue a certificate verifying that the investor or company is due the tax credit.

At least four, and possibly more, of the six companies pre-approved in November will be going before the board this month to try and win the certification. One might be Bionica, a four-person life sciences startup that launched last year to develop a state-of-the-art hearing aid. Co-founder Ralph Beckman said the funds raised under the auspices of the credit incentive should help cover the cost of developing various prototypes of the device, which is known as the Clio. He actively sought out the incentive when it was first publicized last summer, and said the state was smart to pass the program. “It raises the profile of young startups like ours,” Beckman said. “It’s good to know that the state is behind you and helps sell your project.”

Beyond Bionica, the other firms pre-approved in November for the tax credit are: Lighthouse Security Group of Lincoln, an IT security-consulting company; Ocean State Solutions, a North Kingstown tech company developing a system that lets customers use cell phones to pay bills or wire money; Providence Health Solutions, a Providence company developing software to promote wellness programs; Public Display, another Providence software firm that’s developing web applications to help organize data; and Tizra, a Providence-based company trying to help publishers price, package, market, and sell content on the web.

Withers says additional applications will be taken on a rolling basis and considered about four times each year. She adds that Rhode Island hopes to see companies from all of the qualifying industries apply for the credit in the coming months, and that “time will tell” if

it helps grow emerging sectors such as biotechnology, which has become a highly coveted industry in other states and around the world.

Indeed, Rhode Island has become increasingly active in growing—and luring—firms in biotechnology and other tech fields, most significantly through tax incentives. For example, tax incentives helped encourage biotechnology giant Amgen to continue to expand in Rhode Island after purchasing a drug manufacturing facility in West Greenwich in 2002. Employment has grown since then to beyond 1,700 people.

But does the newest tax credit program do much to tilt the balance much toward Rhode Island, especially as Massachusetts legislators consider a mammoth, \$1 billion biotechnology economic stimulus bill that would include tax credits, development grants, and other incentives? (Some legislators are balking at focusing the bill only on life sciences, so a final version could be geared at helping a variety of industries in order to get the measure passed.) And that's on top of other Bay State legislative advances in recent years that include streamlined permitting, which allows cities and towns to designate zones for quick industrial development and more efficient permitting processes—a major issue for many high technology and life sciences companies.

“It’s a great start,” is the early take from Kathie Shields, director of the Tech Collective in Providence, an industry association whose membership includes 180 companies in the high technology and biotechnology spaces. Shields cautions, though, that more enticements are needed soon to enable Rhode Island to more rapidly grow its own reputation as an innovation leader. “We need incentives in place not only through tax incentives, but also through areas of training dollars and support programming and workforce development,” she says.

Withers seems to be in agreement. “Many of our incentive programs are outdated and reflect old assumptions about the kind of economy we need to create greater prosperity for our citizens,” she says. “The Innovation Tax Credit directs resources toward innovative companies that are poised to create new, higher wage jobs. This program is a strategic investment for Rhode Island and one that is in line with our economic development strategy.”

Rhode Island may not become an innovation Goliath overnight, but it plans to bulk up.