

Provisions for
“THE ANGEL
TAX”
for start-ups
under Income
Tax Act

Summary of the latest amendments to Rule 11UA (2)

1. Flexibility to use issue price of an investment by a VCF or notified persons as the FMV
2. The above investment should have been made within + or - 90 days
3. 5 New Valuation Methods introduced **only** for investments by **Non- Residents**
4. Flexibility of variation of 10% from the FMV
5. CCPS recognized as a separate instrument and flexibility provided to company to value it separately from the equity shares of the company
6. Flexibility to use a report issued by a Merchant Banker within 90 days prior to the investment

Section 56(2)(viib):

If a private/unlisted public company issues shares to a person for a consideration which exceeds the FMV of the shares, then the *excess amount* shall be chargeable under the head ‘Income from Other Sources’.

How to determine FMV

Higher of –

- Value as determined under Rule 11UA (2) [*Sub Clause (i) of Clause (a) of Explanation to Section 56(2)(viib)*]
- Value substantiated to the satisfaction of the AO based on the value of assets (including intangible assets) [*Sub Clause (ii) of Clause (a) of Explanation to Section 56(2)(viib)*]

Value under Rule 11UA(2) Resident Investor

- At the option of the assessee, any of the following method can be used:
 1. $FMV = Net\ Assets\ at\ Book\ Value \times \frac{Paid-up\ value\ of\ equity\ shares\ to\ be\ issued}{Total\ amount\ of\ paid-up\ equity\ share\ capital}$
 2. FMV determined by a Merchant Banker as per DCF Method.
 3. FMV to be equal to issue price of investment made by a VCF or a VC company or AIF Fund in the Venture Capital Undertaking
 4. FMV to be equal to issue price of investment made by notified persons

Value under Rule 11UA(2) Non-Resident Investor

- At the option of the assessee, any of the following method can be used:
 1. $FMV = Net\ Assets\ at\ Book\ Value \times \frac{Paid-up\ value\ of\ equity\ shares\ to\ be\ issued}{Total\ amount\ of\ paid-up\ equity\ share\ capital}$
 2. FMV determined by a Merchant Banker as per DCF Method.
 3. FMV to be equal to issue price of investment made by a VCF or a VC company or AIF Fund in the Venture Capital Undertaking within 90 days
 4. FMV determined by a Merchant Banker on the basis of the following additional methods
 - a. Comparable Company Multiple Method
 - b. Probability Weighted Expected Return Method
 - c. Option Pricing Method
 - d. Milestone Analysis Method
 - e. Replacement Cost Methods
 5. FMV to be equal to issue price of investment made by notified persons within 90 days

Calculation for Net Assets at Book Value

Net Book value of assets = A – L

Where,

A= BV of Assets less Any TDS/TCS paid less Any IT refunds receivables less Deferred Expenditure

L= BV of liabilities excluding the following amounts, namely

- (i) The paid-up capital in respect of equity shares;
- (ii) Dividends Payable or any provision for Dividends;
- (iii) Reserves and surplus, excluding depreciation reserve;
- (iv) Any Provision for Income Tax or IT Payables;
- (v) Provisions for liabilities, other than ascertained liabilities;
- (vi) Any amount representing contingent liabilities other than arrears of dividends payable in respect of cumulative preference shares;

Exemption from applicability of Section 56(2)(viib)

Section 56(2)(viib) is not applicable if the consideration for issue of shares is received

BY a Venture Capital Undertaking
FROM a Venture Capital Company or a Venture Capital Fund or Category I or Category II AIF

BY a company
FROM a class or classes of persons as may be notified by the Central Government

BY a start-up company recognised by DPIIT and fulfils certain conditions.

Some Definitions

1. **Venture Capital Undertaking** – a domestic company which is not listed on a recognized stock exchange in India
2. **Venture Capital Company** – a company which is recognized
 1. as a venture capital fund and regulated under the Securities and Exchange Board of India (Venture Capital Funds) Regulations, 1996
 2. as a venture capital fund as a sub-category of Category I Alternative Investment Fund and is regulated under the Securities and Exchange Board of India (Alternative Investment Funds) Regulations, 2012
3. **Venture Capital Fund** – a fund operating under a trust deed which has been recognized
 1. as a venture capital fund and regulated under the Securities and Exchange Board of India (Venture Capital Funds) Regulations, 1996
 2. as a venture capital fund as a sub-category of Category I Alternative Investment Fund and is regulated under the Securities and Exchange Board of India (Alternative Investment Funds) Regulations, 2012

Some Definitions

4. Class or classes of persons notified by the Central Government to be excluded from applicability of section 56(2)(viib)
- a) Government and Government related investors such as
 - i. central banks,
 - ii. sovereign wealth funds,
 - iii. international or multilateral organizations or agencies including entities controlled by the Government or where direct or indirect ownership of the Government is 75% or more
 - b) Banks or Entities involved in Insurance Business
 - c) Following entities resident of any country or specified territory
 - i. entities registered with SEBI as Category-I FPI
 - ii. endowment funds
 - iii. pension funds
 - iv. Broad Based Pooled Investment Vehicle or fund where the number of investors in such vehicle or fund is more than fifty and such fund is not a hedge fund or a fund which employs diverse or complex trading strategies

Terms and Conditions for qualifying as a START-UP

Formation

Should be

- Incorporated as a private limited company or as a partnership firm or as Limited liability partnership

Should not be

- formed by splitting up or reconstruction of an existing business

Period

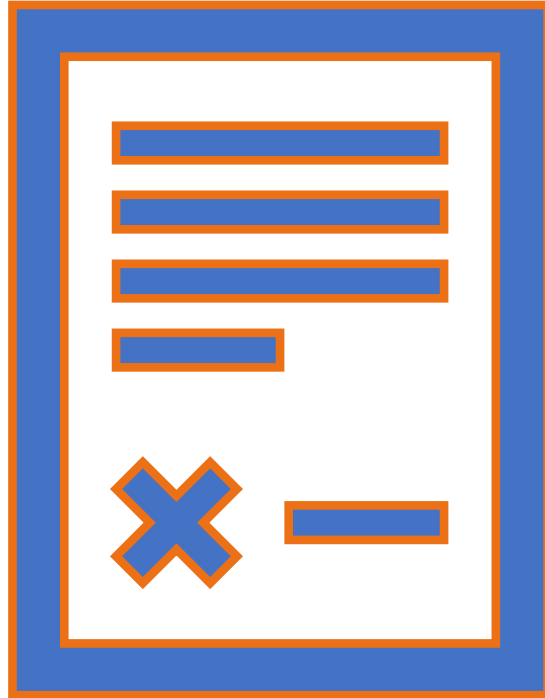
Eligible up to a period of ten years from the date of incorporation / registration.

Turnover

Turnover of the entity for any of the financial years since incorporation/ registration has not exceeded 100 crore rupees.

Purpose

Entity is working towards innovation, development or improvement of products or processes or services, or if it is a scalable business model with a high potential of employment generation or wealth creation.



CONDITIONS TO BE
FULFILLED BY START-
UPS RECOGNIZED BY
DPIIT FOR AVAILING
EXEMPTION.

Paid Up Share Capital + Share Premium \leq 25 crores



Non Resident



Venture Capital
Company or Venture
Capital Fund



Frequently traded
listed entity whose
networth exceeds 100
cr or turnover exceeds
250 cr

Investments Not included for calculation of 25 cr

Investment Criteria

Qualifying Startup should not invest in the following:

1. A residential house, which is not in the ordinary course of business of that start-up;
2. Other Land or building, other than that occupied by the Startup for its business or used by it for purposes of renting or held by it as stock-in trade, in the ordinary course of business;
3. Loans and Advances, other than loans or advances extended in the ordinary course of business by the Start-up where the lending of money is substantial part of its business;
4. Capital contribution made to any other entity;
5. Shares and securities;
6. A motor vehicle, aircraft, yacht or any other mode of transport, > 10 lacs, other than that held by the Start-up for the purpose of plying, hiring, leasing or as stock-in-trade, in the ordinary course of business;
7. Jewellery, other than that held by the Start-up as stock-in-trade in the ordinary course of business;
8. Any other asset, whether in the nature of capital asset or otherwise, of the nature specified in sub-clauses (iv) to (ix) of clause (d) of Explanation to clause (vii) of sub-section (2) of section 56 of the Income Tax Act.

About us

Founded in 2011, we are a boutique consulting firm focused on providing world class financial consulting, valuations and corporate finance services.

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- Valuation of intangible assets, ESOPs,
- Valuation for Purchase Price Allocations
- Fair Value Valuations as per Ind AS and Companies Act
- Valuations for Regulatory requirements for SEBI, RBI and Income Tax
- Valuation of Securities for M&A and Fund Raising

Investment Banking Solutions

- Preparing IMs and Financial Models
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- M&A Transactions and Deal Structuring
- End to end solutions for Fund Raising
- Stressed Asset Consulting

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