DNA

Start-ups seek wings for their angel investors

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With the Budget around the corner, start-ups in India are expecting clarity on angel tax, which continues to weigh high on their agenda.

Angel tax, levied on start-ups for raising funds exceeding their fair market value (FMV), is still the bone of contention despite government exempting innovative start-ups from this tax in the last Budget. Only start-ups recognised by the government could avail of this exemption, which was the condition put forward in the Budget 2017-18 and many could not access the benefits because of this.

Experts tracking the industry say that there is a lack of clarity around taxation issues, which has also led to a decline in angel investment in the start-ups across the country.

As per Nasscom, the levy of this tax has resulted in a 53% decline in angel funding during the first half of 2017.

Angel investors are affluent individuals who invest their personal wealth. It's a synonym for informal investors/private investors/seed investors. Angel tax stands at around 30%.

Many start-up firms expect the government to resolve this issue in the upcoming Budget on February 1 and further ease norms for doing business, especially in e-commerce/start-up space.

Paytm CEO and founder Vijay Shekhar Sharma told DNA Money the biggest concern for start-ups is angel investments, which have been identified as capital gains.

"The government needs to take care of this issue in the Budget. Many start-ups are taking such investments. This should be corrected. The government had launched a great Startup India initiative which offers good opportunity for the players in this segment," Sharma said.

Echoing similar views, CashKaro.com co-founder Swati Bhargava said angel funding is the first source of encouragement for a start-up and tax levied on the same is a major deterrent to its growth.

"Early-stage investors should be spared these old policy measures. A popular scheme to take inspiration from is the UK's Enterprise Investment Scheme (EIS). It protects 61.5% of investors' investment through generous income tax reliefs as well as an exemption of capital gains tax on returns. If a similar tax relief comes to India, it will encourage investments in Indian start-ups," she said.

A clarity on the eligibility criteria for a start-up is also required on many fronts. First, to claim exemption on angel tax, one has to fit into the definition prescribed by the government. Second, even for accessing money from Fund of Funds for Start-ups (FFS) one has to register and then be eligible for such grants, which at times is a cumbersome process.

This fund was launched in January 2016 with a corpus of Rs 10,000 crore and was launched in line with the Start-up India action plan of the government. Till now, only Rs 600 crore has been distributed. The government also launched a Startup India Hub, which has been established as a single point of contact for the entire start-up ecosystem for knowledge sharing and access to funding.

Bhagava said, "Entrepreneurs struggle with basics like, how the government defines a start-up. The rules around eligibility to claim these benefits are unclear and the approval process is tedious. The new Budget should create an environment conducive to business."

According to the information from commerce and industry ministry released in December last year, about 5,350 start-ups have been recognised by the government for availing benefits under the Startup India initiative. Under the Fund of Funds for Startups, 75 start-ups have received funding to the tune of Rs 337.02 crore. Another 74 start-ups have been recognised to avail tax exemption under the Income Tax Act. Under the Fund of Funds for Startups, Rs 500 crore was released to Sidbi (Small Industries Development Bank of India) in 2015-16 and Rs 100 crore in 2016-17.

There is also a need for consistent and predictable taxation policies, which will encourage growth of the digital economy.

Digital economy includes several start-ups and small and medium-sized enterprises who need funding, which makes it important that taxation of the difference between share premium and fair market value (FMV) is exclusively applied in conditions where there is actual use of unaccounted money or other collateral purposes, a recent report by IAMAI and Nishith Desai Associates -- 'Taxation of the Digital Economy: Impact analysis for India,' said.