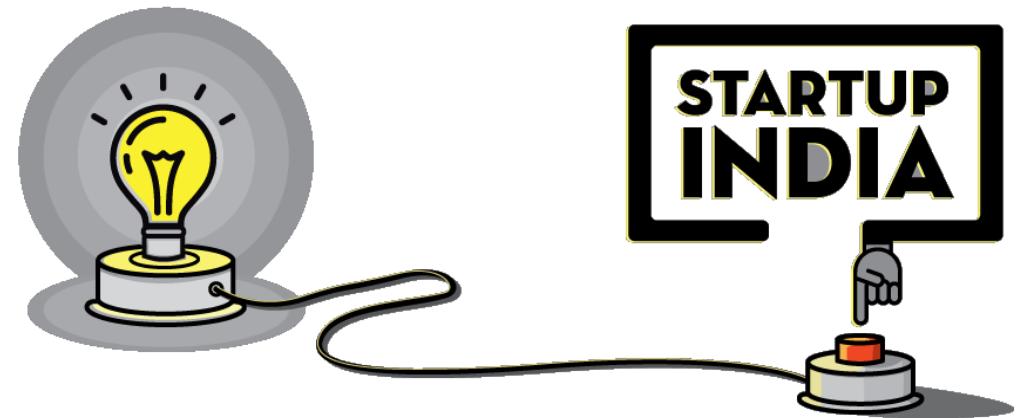


De Jure

July 1, 2016

It's raining sop for Startups!!



Startup can now issue unsecured Optionally Convertible Debentures (Conditions apply)

Other companies cannot issue unsecured OCD, though they can issue CCD or secured NCD or unsecured listed NCD.

In an attempt to give momentum to the Startup Action Plan that was unfurled in January this year, Government, inter alia, amended Section 56(2) (viib) of the Income Tax Act whereby no tax will be levied on capital raised by start-ups from domestic investors which exceeds the fair market value of the startup's shares. The Startup Action Plan already boasts of a number of special exemptions for start-ups with a view to breed entrepreneurs and turn India into a job creating nation.

On June 29, 2016, Government released a notification which has the potential to further strengthen the government's resolve to foster entrepreneurship. The Government of India has notified Companies (Acceptance of Deposits) Amendment Rules, 2016 whereby any advance of more than Rupees 25 lakh raised by a start-up shall be exempted from being considered a deposit (Of course, this comes with caveats!). The definition of deposits under the Companies Act 2013 is an inclusive one with specific exemptions. Apart from the exemptions set out under the meaning of the word deposits, monies raised in any other manner is construed as deposits and consequently companies have to follow stringent deposits rules.

The caveat to this relaxation is that the amount of Rs.25 lakhs or more should be received by the start-ups:

- by way of a convertible note which is convertible in equity shares or repayable within a period not exceeding five years from date of issue; and
- the monies should be received by way of bullet payment.

"Convertible note" has been defined to mean an instrument that evidences the receipt of money, initially, as a debt but which is repayable (at the option of the holder) or which is convertible into such number of equity shares of the start-up company, upon occurrence of specified events and as per the other terms and conditions agreed to and indicated in the instrument.

Even though a new term 'convertible note' has been coined, it is more or less similar to widely known optionally convertible debentures. When companies issue convertible debentures, it has to be either (i) a secured debenture with a charge on the assets of the company; or (ii) compulsorily convertible debenture to be converted into shares within ten years, or (iii) unsecured listed non-convertible debentures. However, in the light of this amendment, a startup will be able to raise finances by way of the convertible note which has the option to be converted in to shares without any statutory requirement of creating a charge. This is a welcome move as they often struggle to obtain funds and due to which many of them die down even before their wings start to grow.

Money does not change anything it just helps one expand horizons! Well, in here, we are referring to budding startups. A little money made available to them might as well facilitate a new silicon valley in our country!

Please look out for our next "Dejure" which will be providing the highlights of the recent amendments to the Companies (Acceptance of Deposits) Rules, 2014.

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