Tax Implication for Venture Capital Funds – Union Budget 2012

1) In order to enhance availability of equity to MSME sector, the Finance Minister has proposed to set up a INR 5,000 crore India Opportunities Venture Fund with SIDBI. *We strongly believe that apportion of the same will go towards building a self sustaining eco system in the Early stage investment space.*

2) Amendment to section 10(23FB) and section 115U of the Income Tax Act, 1961 w.e.f assessment year 2013-14 so that

   i) The venture Capital undertaking shall have same meaning as provided in relevant SEBI regulations and there would be no sectoral restriction. Accordingly the pass through benefit is extended across to all sectors provided the Fund is SEBI registered.

   ii) Income accruing to VCF/ VCC shall be taxable in the hands of investor on accrual basis. Further, the payment by VCC to the investor is exempted from Dividend Distribution Tax (DDT)

   iii) The exemption from applicability of TDS provisions on income credited or paid by VCF/ VCC to investors is proposed to be withdrawn.

3) The tax rate on long term capital gains for Non Resident Indian is already at 10%. And it is not necessary for NRI to furnish a return of his income as per section 115G read with section 115C if—

   (a) his total income in respect of which he is assessable under this Act during the previous year consisted only of "investment income" or "income by way of long-term capital gains" or both; and

   (b) the tax deductible at source under the provisions of Chapter XVII-B has been deducted from such income.

4) As per section 112 of the Income Tax Act, 1961 w.e.f assessment year 2013-14, long term capital gain for Non-Resident Investors including Private Equity Investor arising from sale of unlisted securities has also been reduced from 20% to 10% and brought parity with Tax Rate applicable to FIIs.

5) With effect from 1.7.2012, Securities Transaction Tax (STT) at the rate of 0.2 per cent shall be levied on sale of unlisted equity shares by any holder of such shares under an offer for sale to the public included in an initial public offer and where such shares are subsequently listed on a recognised stock exchange. Consequently as per section 10(38) of the Income Tax Act , there will be total Tax exemption on long term capital gains arising from sale of such unlisted equity shares.

6) It was earlier proposed in the Finance Bill 2012, that any consideration received by a closely held company in excess of the fair market value of its shares would be taxable. Considering the concerns raised by 'angel' investors who invest in start-up companies, the enabling provision in the clause (viib) of section 56 of Income Tax Act now provides exemption w.e.f assessment year 2013-14 from this rule where the consideration for issue of shares is received—

(i) by a venture capital undertaking from a venture capital company or a venture capital fund; or

(ii) by a company from a class or classes of persons as may be notified by the Central Government in this behalf.