'IMPACT' EVALUATION OF THE VENTURE CAPITAL FINANCING AND REGULATIONS IN INDIA

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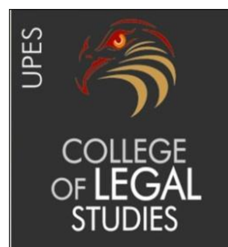
This dissertation is submitted in partial fulfillment of the degree of B.B.A., LL.B. (Hons)



College of Legal Studies
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CERTIFICATE

This is to certify that the research work entitled **"IMPACT EVALUATION OF THE VENTURE CAPITAL FINANCING AND REGULATIONS IN INDIA"** is the work done by Aadep Singh Sethi under my guidance and supervision for the partial fulfillment of the requirement of B.B.A., LL.B. (Hons) degree at College of Legal Studies, University of Petroleum and Energy Studies, Dehradun.

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DECLARATION

I declare that the dissertation entitled **“IMPACT EVALUATION OF THE VENTURE CAPITAL FINANCING AND REGULATIONS IN INDIA”** is the outcome of my own work conducted under the supervision of Mr. Sujith P. Surendran, at College of Legal Studies, University of Petroleum and Energy Studies, Dehradun.

I declare that the dissertation comprises only of my original work and due acknowledgement has been made in the text to all other material used.

Aadep Singh Sethi

Date

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- SEBI (Venture Capital Funds) Regulations, 1996

ABBREVIATIONS

&	And
§ /S. /s.	Section
Govt.	Government
Anr.	Another
Art.	Article
Comm.	Commercial
Doc.	Document
Ed.	Edition
Intl.	International
Inc.	Incorporation
Corp.	Corporation
Ltd.	Limited

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It gave me an opportunity to learn about Venture Capital Financing and Regulations which is a contemporary topic across the globe in today's world and one of the most sought after issues delving in the corporate Law Regime.

Finally, an honorable mention goes to our families and friends for their understanding and support on us in completing this project.

INTRODUCTION AND BACKGROUND

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EXORDIUM

When Christopher Columbus had begun his voyage westwards from Europe to reach India, his unwarranted venture did not find any support with the King of Portugal and he was denied funds to assist him in his venture. It was then the Queen Isabella of Spain who funded his venture, undoubtedly the risks associated were great but the rewards turned out to be greater.

The concept of 'venture capital' can be traced from here. In contemporary context it can be said that such ventures which are unconventional and untried and have a high risk high return potential, which are sure not to be financed by the usual more driven ways of funding are sure to find venture capitalists contributing to such prospects[1].

Venture Capital is a term coined for the capital required by an entrepreneur to 'venture' into something new, promising and untried. Investing in a budding Company has always been a risky option for any financier. The risk of the business failure and the apprehensions of an all together new project clicking, weigh down the small entrepreneurs to get the Initial Push. The Venture Capitalists or the angel investors here come to the forefront with an appetite for risk and willingness to fund the ventures[2].

Venture capitalists are professional managers of funds who provide risk associated capital to businesses. Venture capitalists are found in various forms and specialize in many different ways, but all of them share this common trait of making investments at an early stage in privately held companies that have the potential to provide them a very high rate of return on such investments[3].

Private equity investments are investments which are made in rather relatively more matured companies at their expansion stage. Private equity firms focus on active investments and target to acquire a large or controlling interest in companies with

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[1] Nidhi Bohra, Venture Capital Regulations- India, Vinod Kothari & Co.
[2] Ibid
[3] Nishith Desai Associates, Venture Capital at Crossroads, September 2003.

solid growth potential. As a result, private equity firms usually oversee, assist and, if necessary, redirect the company's activities or its management.

Venture Capital can be understood as money granted by qualified or holders of expertise who advance and look after swiftly increasing companies that have the potential to emerge as mega economic contributors to the economy. It is the catenation of investing private equity in companies to offer considerable scope to grow to a large extent and reward investors in market[4].

Venture Capital firms supervise pools of funds formed over a period of several years. Funds are categorically illiquid but as companies in the portfolio go public or are sold, the investors realize their returns. A broad general rule for the breakdown of returns among VC Company investments can be assumed as 40% complete losses, 30% can be categorized as "living dead," with the remaining 30% actually generating substantial returns on the original investment. The big winners yield up to 10 or more times the original investment[5]. Venture capital can also be defined as investment in small or medium sized unlisted companies with the investors playing a role to a certain degree in the management process as well.

The venture capital industry usually in global context is seen as "independently coordinated, dedicated pools of funds that focus on equity or equity oriented investments in privately controlled, high-growth companies." Venture capital is often thought of as only "the initial stage financing of budding and young companies looking forward to grow at a rapid pace"[6].

While, given its wide range of activities, an all - encompassing definition of venture capital would not be possible, although a brief description of it could be like : "a minority and temporary equity and/ or quasi - equity investment, in a growth focused small or medium size business controlled by a highly motivated entrepreneur. The

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[4] Maneesh Yadav, Regulatory Aspects of Venture Capital In India, (March 11th 2015), http://www.legalservicesindia.com/article/article/regulatory-aspects-of-venture-capital-in-india-265-1.html.

[5] Asian Venture Capital Journal, Guide to Venture Capital in Asia, Hong Kong, 1992-1993.

[6] The SEBI Committee Report on Venture Capital set up under the chairmanship of K.B. Chandrashekhar, 2000.

investment is often accompanied by management assistance. For his investment, the investor expects to receive a minority share holding in the company or the irrevocable right to acquire the same."

Venture Capital as understood from economic/financial perspective is investment of long term risk associated finance in virgin untried enterprises that lack in stability. Which means an investment in such business ventures where uncertainties are yet to be deduced and to that effect risk that is subject to rational criteria of scrutiny analysis[7].

Venture Capital in a wider perspective is not merely infusion of funds into a new firm, it also involves input of skills required to set-up the firm, formulate its strategy, manage and organize it. Venture capital is more of active rather than passive finance. Depending upon the relevant business situations, venture capitalists get engaged in activities like management, production process, marketing or accounting or provide training to firm's staff in multiple operational areas, or sometimes depute their staff to supervise certain activities[8].

Venture Capital funding should be demarcated from traditional sources of funding. Venture capitalists finance innovative business ideas which have high potential for growth, but with it, inherent few uncertainties. This makes it a high-risk, high return investment.

Along with finance, venture capitalists also provide hands - on management assistance and other skills that help convert the entrepreneurial vision into marketable products[9]. Venture capital is a form of equity financing based on the principle that the partnership can be bridged and worked out between the entrepreneur and the investors.

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[7] Satish Taneja, Venture Capital in India, 2002, Golatia Publishing Company.
[8] Ibid
[9] The SEBI Advisory Committee Report on Venture Capital set up under the Chairmanship of Dr. Ashok Lahiri, 2003.

So, any proposed business prospect whether involving high, low or no technology qualifies for (money to small business) support. A very important difference between (people who loan money to small businesses) and ordinary financers is that (people who use money to make more money) add value to their investments through provision of active managerial help to its associates. The money to small business industry this way represents a successful attempt to (make a behavior acceptable) new and interesting business thinking, and especially small-business starting connected with invention of new things (not mandatorily technical invention of new things).

In worldwide venture capital industry, investors and investee firms work together closely in an enabling environment that permits entrepreneurs to focus on value creating ideas and venture capitalists to drive the industry with ownership of the levers of control in return for the provision of capital, skills, information and complementary resources. This very blend of risk financing and hand holding of entrepreneurs by venture capitalists creates an environment particularly suitable for knowledge and technology based enterprises[10].

BASIC WORKING

Trip/business Capital financing is a method in which money is combined in for a period of around 10 years and invested in (money to small business) difficult projects for a period ranging from 3-5 years with an expectation of high return. To get the money of the (people or business who give money to help start businesses) against the risk of losses, (money to small business) fund provides its (ability to do things very well), begin/try (like a recommendation, but not an order) function and invest in the 'patient capital' of the undertaking - equities.

Kinds of Venture Capital Investments[11]:

[10] The SEBI Committee Report on Venture Capital set up under the chairmanship of K.B. Chandrashekhar, 2000.

[11] The Planning Commission Report of the Committee on Technology Innovation and Venture Capital set up under the chairmanship of Mr. Nitin Desai, 2006.

"With a broader outlook, the venture capital investments in various ventures can be put under the following heads:

a) **Seed financing**: to the technologist/ entrepreneur to prove a concept.

b) **Start-up financing**: for the product development and initial marketing to a few customers.

c) **First stage financing**: to initiate commercial production and marketing.

d) **Second stage financing**: for expansion of scale.

e) **Later stage financing**: for expansion of an enterprise that is already profitable".

HISTORICAL DEVELOPMENT AND EVOLUTION

HISTORICAL DEVELOPMENT AND EVOLUTION

THE INITIAL PUSH

India has always had a history of being driven for institutional development by majorly state oriented policies. (Related to ideas or beliefs), the Indian government had a very honest state of being hateful to (a system where people own money and valuable things). The government's powerfully tangled up slow-working government department(s) closely controlled the economy and had a reputation for (dishonest actions that ruin your trust).

India with its air tight rules controlling markets and high trade taxes/import taxes ranked pretty low in the list of (person or business who gives money to help start a business) friendly legal controls on this globe. The idea of protectionism also reflected in the half - hearted attempts while encouraging the idea of (money to small business) in India.

The idea of venture capital financing in India budded in the year 1972 when a need was felt to have separate source of financing to support new unconventional budding business ideas and new entrepreneurs. In fact, the requirement for venture capital was first showcased by the 'committee on development of small and medium entrepreneurs' under the chairmanship of Mr. R.S. Bhatt popularly known as R.S. Bhatt committee[12].

"In 1975, risk capital foundation was established and was financed by Industrial Finance Corporation India ("IFCI") to assist promoters' equity with the objective of providing funds to new technologies and business professionals and to promote upcoming industries".

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[12] Dr. JK Singh, Venture Capital Financing in India, Dhanpat Rai Publishing Company, 2nd Ed.

During 1976, the seed capital scheme was brought on floor by Industrial Development Bank of India ("IDBI"). The concept of venture capital was known in the form of "Risk Capital" and "Seed Capital" till 1984. Under Risk Capital and Seed Capital, the monies were majorly meant for initial stages of financing. Later stages were not within the ambit of such fund support then.

The initial steps to formalize venture capital were taken in the year 1987, when the Government of India issued its very first guidelines on legalizing venture capital operations in the country. Pan India public sector financial institutions, State Bank of India and other scheduled banks, foreign banks or such other private investors were allowed to establish venture capital funds to support firms that were involved in technology that was "new, relatively unconventional, very closely held or being taken from pilot to commercial stage, or which reinstated certain vital improvements over the existing ones in India".

The pooled monies were restricted for investment in small amounts per firm (less than Rs. 10 crore). It was also specified that the recipient firm's founders should be "relatively new, professionally or technically qualified, and with inadequate resources or support to finance the project" There were other bureaucratic barriers like at least one of the two government-sponsored development banks, ICICI and IDBI, were to vet every portfolio firm's application to ensure that it met the requirements. Fund raising was permitted through public issues as well as private placements.

LATER DEVELOPMENTS

The year 1995 witnessed the next major development in regime of Venture Capital. Guidelines which were earlier issued by the erstwhile Controller of Capital Issues were repealed by the Indian Govt.[13] & a new set of regulations were issued by the Securities and Exchange Board of India ("SEBI") to govern the domestic venture capital investments in India. Moreover, it was made compulsory for a person carrying on the business of venture capital funds to be registered with SEBI[14].

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[13] SEBI (Venture Capital Funds) Regulations, 1996.
[14] See Section 12 (1B) of The Securities and Exchange Board of India Act, 1992.

"As per the SEBI Venture Capital Fund Regulations, 1996 ("VCF Regulations") a venture capital fund could be established either as a company or a trust. A venture capital fund could gather funds through loans, donations, issue of securities or units as the case may be"[15].

The Indian Govt. in the same year came out with guidelines to control the offshore (money to small business) money making investments in India. As per these guidelines, offshore (money to small business) (people or business who give money to help start businesses) could soak (in) their investments either by investing in a domestic (money to small business) fund that would (after that) invest in unlisted Indian companies or they could invest directly in the equity shares of unlisted Indian companies. There was no restriction as to the limit up to which foreign (thing that's given/work that's done) to the capital of the domestic fund could be made.

Contribution in domestic venture capital funds was considered as a single act of foreign investment by the offshore investor and required only one-time approbation from the Foreign Investment Promotion Board ("FIPB"). Followed up investments by the domestic fund in Indian companies did not require any further approval from FIPB and were only barred with basic restrictions relevant to domestic funds.

Offshore (people or business who give money to help start businesses) also had an option of beginning and building on a valuable thing management company (with prior approval from FIPB) to manage the money. The offshore (people or business who give money to help start businesses) investing straightaway in the unlisted equity shares of the Indian companies had to take permission from FIPB for every such investment made by them as each of them were considered a separate act of outside (thing that's given/work that's done).

[15] Regulation 2(m) of the SEBI (Venture Capital Funds) Regulations, 1996 prior to its amendment in 2000 read as follows:
"Venture capital fund means a fund established in the form of a company or trust which raises monies through loans, donations, issue of securities or units as the case may be, and makes or proposes to make investments in accordance with these regulations."

"Following the establishment of regulatory framework mentioned above, some domestic VCFs were registered with SEBI. Some offshore investment had also come. However, the venture capital industry as understood globally "independently coordinated, specific pools of capital that focus on equity or equity-oriented investments in privately held, high-growth companies" ("The Venture Capital Cycle", Gompers and Lerner, 1999) was relatively in budding stage in India".

"Figures from the Indian Venture Capital Association (IVCA) show that, till 1998, around Rs.30 billion had been invested by domestic VCFs and foreign funds which were members of IVCA [Not all foreign venture investors and domestic funds are members of the IVCA.] Other Figures from private sources indicate that overall funds contributed were around US$ 1.3 billion"[16].

Funds actually available for investment were less than 50% of the total contributed funds. At the same time, as a result of economic liberalization and increasing global outlook in India, there was awareness and interest of domestic as well as offshore investors in venture capital.

SEBI thereafter started interactions with market players and experts in early 1999 to figure out the key areas crucial for the development of this industry in India. The Finance Minister, in his 1999 budget speech had announced that "for boosting high-tech sectors and supporting first generation entrepreneurs, there is an acute need for higher investment in venture capital activities."

He also declared that guidelines for registration of venture capital activities with Central Board of Direct Taxes would be harmonized with those for registration with the Securities and Exchange Board of India. SEBI, at this juncture finalized to set up a committee on Venture Capital to figure out the hurdles and suggest suitable ways to facilitate the growth of venture capital Industry in India.

Keeping in view the need for a global perspective it was finalized to involve and coordinate Indian entrepreneurs from Silicon Valley in the committee. The committee

[16] Supra 10

was headed by K.B. Chandrasekhar, Chairman, Exodus Communications Inc., California, USA and consisted of market experts, professionals and representatives from various financial institutions and RBI.

This committee was set up primarily to motivate the need of playing a facilitating role in accordance with the mandate of SEBI, to control as well as develop the market. The first meeting of the Committee took place on August 5, 1999 which was followed by further deliberations by the Working Groups formed in the committee to evaluate the issues related to Structure and Fund Raising, Investment Process, Exit and Vision for the Venture Capital market in India.

"The draft recommendations of the committee were formed in the meeting of the committee held on December 8, 1999. The draft recommendations were released for public review and after considering the feedback, report was finalized in the meeting of the Committee held on January 8, 2000".

Bird's Eye View of the K.B. Chandrashekhar Committee

The committee after various deliberations found that the venture capital industry in India was still at a budding stage. In order to foster innovation, enterprise and conversion of scientific technology and knowledge based business ideas into commercially viable production; it is inevitable to promote venture capital activity in India. India's success in the area of information technology had shown that there was amazing scope for growth of knowledge based industries.

This scope was not only limited to information technology but was equally (clearly connected or related) for (more than two, but not a lot of) areas such as bio-technology, drugs and drugs, farm-related, food processing, (related to sending and receiving phone calls, texts, etc.), services, etc. Having built-in strength of skilled and cost competitive (related to workers in general), technology, research and small-business starting, with appropriate/smart (surrounding conditions) and proper policy support, India can (accomplish or gain with effort) money-based growth at a fast pace and competitive worldwide strength in an (able to last/helping the planet) way.

A successful venture capital industry in India will bridge the gap between the capital needs of knowledge and technology driven startup business units and monies available from conventional institutional lenders such as banks. The gap exists as such startups are necessarily driven by intangible assets such as human resource and on a technology-based mission, often with the spirit of changing the world.

However, they were able to raise funds from independently organized venture capital funds that focus on equity or equity-linked investments in privately held, high-growth companies. Along with these funds came intelligent business advice, hand-on management support and other skills that helped these innovative business ideas to be converted to marketable products.

Initiating with considering wide role of venture capital to include not just information technology, but all high-growth technology and knowledge-driven business units, the effort of the Committee was to make recommendations that would facilitate the growth of a flourishing venture capital industry in India.

Factors Crucial for Success of Venture Capital Industry[17]

While making the recommendations the Committee felt that the following factors are critical for the success of the VC industry in India:

(A) The overall regulatory environment including all the legal issues such as tax etc., should be more easy going and facilitating one, operationally neutral policies should be used and a boost should given to this industry as a whole.

(B) All the procedural activities encompassing raising of funds, management of the activities of the startup and exit, all should be structured in an easy setup.

[17] The SEBI Committee Report on Venture Capital set up under the chairmanship of K.B. Chandrashekhar, 2000.

(C) The entire industry of venture capitalists should foster confidence in the investors as well as budding business professionals looking for support and should be a protection based agency enabling smooth functioning of the entire regime.

(D) "In view of increasing global integration and mobility of capital it is important that Indian venture capital funds as well as venture finance enterprises are able to have global exposure and investment opportunities".

Recommendations[18]

1. Harmonization of Multiple Regulations

The need was to consolidate and substitute all these into one umbrella regulation of SEBI to provide for uniformity, hassle free single window clearance. There was already a pattern available in this regard; the mutual funds have only one set of regulations and once a mutual fund is registered with SEBI, the tax exemption by CBDT and inflow of funds from abroad was available automatically.

The above examples paved the way for corporate thinking in this particular direction. Such already existing legal structures boosted and instilled the required confidence by this upcoming business friendly industry and thus came this recommendation.

2. Tax Exemption for Venture Capital Funds

One of the major lucrative incentives which could actually enhance the growth of foreign and domestic investments was the exemption from taxation, or the tax pass through. Already existing successful examples in the case of mutual funds further supported this thought. As such this recommendation came and proved quite fruitful at later stages instilling confidence in investors, simplifying regulatory process and smoothening the entire venture capital regime.

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[18] Ibid

Since like mutual funds VCF is also a pool of capital of investors, it should to be treated as a tax pass through. Once registered with SEBI, it should be entitled to automatic tax pass through at the pool level while maintaining taxation at the investor level without any other requirement under Income Tax Act.

3. Integrated movement of Global and domestic Venture Capital Funds

(A) Foreign Venture Capital Investors (FVCIs):

During committee deliberations it was highlighted that FII's investment route is much simpler. No prior permissions from RBI or FIPB were required to bring in such investments as such the same was suggested for FVCIs as well in order to enhance foreign investments in this particular regime.

Various data oriented examples ere cited as to how much of International investment has been routed because of these easy going regulatory framework. This further paved the way for more flexible structure of the FVCI industry in our Nation.

One of the important issues that were encompassing the entire working of the committee was the concern regarding foreign investments for the budding business and its development in India. Already existing simple procedures for the FII's fascinated the thought of having similar investment routes for FVCIs as well.

FVCIs therefore should be provided tax exemption. This provision would put all FVCIs, whether investing through the Mauritius route or not, on the same footing. This would then help the development of a vibrant India-based venture capital industry with the advantage of best international practices, thus enabling a jump-starting of the process of innovation.

The hassle free entry of such FVCIs on the pattern of FIIs is even more necessary because of the following factors:

(i) "Venture capital was a high risk area. In out of 10 projects, 8 either fail or yield negligible returns. It was therefore in the interest of the country that FVCIs bear such a risk".

(ii) "For venture capital activity, high capitalization of venture capital companies was essential to withstand the losses in 80% of the projects. In India, we do not have such strong companies".

(iii) "The FVCIs were also more experienced in providing the needed managerial expertise and other supports"

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(B) Enhancing the In-Home Resources:

Various deliberations highlighted the fact the most of the investment coming in for venture capital industry was coming mostly from foreign investors and domestic investors were to be given a fillip in all possible ways in order to enhance that sector with contributions as well.

As at the time of these deliberations the majority of the funds were being channelized for venture capital industry through foreign investment, steps were required to boost domestic investments as well. The most efficient way to implement this was to increase the various institutions and instruments for such investments, allowing more parties would enhance domestic contributions with great effect.

"However, investing in venture capital funds could be a valuable return-enhancing tool for such investors while the increase in risk at the portfolio level would be minimal. Internationally, over 50% of venture capital comes from pension funds, banks, mutual funds, insurance funds and charitable institutions".

4. More easy investment and exit routes:

(A) Allowing multiple flexible structures:

"Eligibility for registration as venture capital funds should be neutral to firm structure. The government should consider creating new structures, such as limited partnerships, limited liability partnerships and limited liability corporations. At the time of

committee deliberations, venture capital funds could be structured as trusts or companies in order to be eligible for registration with SEBI".

The structures in certain forms that were allowed to operate in the ambit of venture capital were limited. International experience showed the way to allow more such contemporary structures such limited liability partnerships etc. The committee through its deliberations tried to conclude and foster this thought in the then regulatory setup.

(B) Reducing the cap on investments and reducing the restrictions:

The committee also tried to relax the regulations by reducing the cap for investments. The Idea was to develop more investor friendly setup in order to attract as much as funds possible. Also in order to maintain the authoritative integrity negative list was proposed which could include certain sectors not permitted operate in the given regime.

It was proposed that investments in subsidiary companies must not be allowed at all and only 25% of the total share of the sector specific dedicated collection of money should be allowed to be invested in one particular unit. It was also suggested that off late as time progresses and VCF Matures investors could develop a reign of their own restrictions and conditions for venture capital undertakings.

(C) More Flexible IPO Norms:

"The IPO norms of 3 year track record or the project being funded by the banks or financial institutions should be relaxed to include the companies funded by the registered VCFs also. The issuer company may float IPO without having three years track record if the project cost to the extent of 10% was funded by the registered VCF".

Those companies which were funded by Venture capitalists and their securities were listed on the stock exchanges outside the country; those companies should be permitted to list their shares on the Indian stock exchanges.

(D) Issue of Shares with Differential Right with regard to voting and dividend:

It was highlighted in committee deliberations that a way in which investments could be boosted were to allow unlisted companies to issue shares with differential rights regarding voting and dividend, similar system already existed for private companies which were not subsidiary of public companies.

(E) NOC Requirement: In the case of transfer of securities by FVCI to any other person, the RBI requirement of obtaining NOC from joint venture partner or other shareholders should be dispensed with.

(F) RBI Pricing Norms: During the time of committee deliberations, investment/disinvestment by FVCI was subject to approval by RBI which prevented operational ease and was suggested to be removed.

5. International Opportunities:

(A) Employee oriented incentives:

Suggestions were made in the committee discussions regarding increment in the limit for investment by Indian Resident foreign employees. Similarly Indian company having foreign employees should be allowed to invest up to greater limits than those which were applicable at that time.

(B) Incentives for Shareholders:

Successful international practice of stock swapping enabled various new budding ventures to swap shares with bigger foreign corporations resulting in financial stability and strengthening of economy. Similar practice should be carried in India as well for better business environment.

6. Infrastructure and R&D:

International examples from various parts of the world and specifically from the United States suggested that infrastructure requirements were the most eminent for any budding economy. As such steps were to be taken in order to enhance the then existing infrastructure of the nation. Similarly a lot of stress should be given on the technological aspects and laboratory based researches which were a great help for upcoming startups.

CURRENT REGIME OF THE REGULATORY SET-UP

CURRENT REGIME OF THE REGULATORY SET-UP

Historical Tax Framework under the IT Act, 1961 till the year 2000

Certain relaxations and exemptions from tax on income from dividend and long - term capital gains from equity-based investments made by SEBI registered venture capital funds in unlisted companies in some sectors were introduced in the Finance Act, 1995, in order to promote and foster venture capital industry in India.

"However, income at the hands of the unit holders/ shareholders of the fund was fully taxable. As a result, Section 10 (23F) was brought in The Income Tax Act, 1961 (the "IT Act") which exempted any income in the form of dividends or long-term capital gains of a venture capital fund coming from investments made into equity shares of a venture capital undertaking".

A gripping aspect of the section was that it had restricted the sectors for investments only to unlisted home companies involved in the business of 'generation or generation and distribution of any form of power or telecommunication services or in the business of maintaining, developing and operating any infrastructure facility or engrossed in making of any article or things (including computer software) as may be notified by the Government'[19].

So, although there was no restriction by SEBI in choosing parts/areas for investment, but to get/help (not having to pay taxes) one had to restrict its investments to the abovementioned parts/areas. This surprising and weird state continues even till the current day with certain more parts/areas added now.

There was an additional requirement to avail the afore mentioned tax benefits, that the venture capital funds were required to take prior permission from the Director of

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[19] Explanation (c) to Section 10 (23F) of the IT Act, 1961.

Income-tax (Exemptions) having jurisdiction over the venture capital fund.[20] The Income Tax Rules also provided for certain restrictions on the investments made by the fund which had put a cap on investments up to 20% of the capital of the funds in one venture capital undertaking and a maximum investment up to 40% in the equity share capital of one venture capital undertaking[21]. As such, along with the restrictions imposed by SEBI, a fund had to comply with the aforementioned requirements in order to account for the income tax benefits.

The above mentioned sectors for investments by a fund were substituted by seven new sectors with an amendment to the IT Act in 1999[22].

"These sectors included the upcoming knowledge oriented enterprises of that time including (a) software; (b) information technology; (c) production of basic drugs in the pharmaceutical sector; (d) biotechnology; (e) agriculture and allied sectors; (f) production or manufacture of any article or substance for which patent has been granted to the National Research Laboratory or any other scientific research institute approved by the Department of Science and Technology; or (h) such other sectors as may be notified by the Central Government on this behalf".

Investment conditions were also changed to the effect that a fund was now permitted to contribute up to 25% of its total capital in one venture capital undertaking and the cap on maximum contribution of to 40% in the equity share capital of a venture capital undertaking was removed.

Bird's Eye View of the Ashok Lahiri Committee[23]

Aftermath of successful achievements in information technology, the time had come for grasping ample opportunities in various other sectors like bio-technology,

[20] Rule 2D (1) of the Income Tax Rules.
[21] 2D (5) of the Income Tax Rules.
[22] Section 10(23FA) of the IT Act.
[23] The SEBI Advisory Committee Report on Venture Capital set up under the Chairmanship of Dr. Ashok Lahiri, 2003.

Pharmaceuticals and drugs, agriculture, food processing, telecommunications, Call centers, business process outsourcing (BPO) and services.

The huge pool of excellent and cost competitive manpower, technology and research institutes, and new and interesting business ideas needed to be helped produce through appropriate/smart policy support and proper financing of risk capital for (accomplishing or gaining with effort) this goal. Startup money was critical in this big picture. In the life-span of almost every business, in any part/area, (money to small business) money could play a very important role in solving such problems of the pre initial public offering (IPO) money/giving money (to).

Securities and Exchange Board of India (SEBI) had set up an Advisory Committee on Venture Capital under the Chairmanship of Dr. Ashok Lahiri, Chief Economic Advisor, Ministry of Finance, Government of India for advising SEBI in Matters relating to the development and regulation of venture capital funds industry in the country.

Terms of Reference for Advisory Committee on Venture Capital were –

1. To advise SEBI on issues related to development of Venture Capital Fund industry.
2. To advise SEBI on matters relating to regulation of Venture Capital Funds and Foreign Venture Capital Investors.
3. To advise SEBI on reforms required to be undertaken for changes in legal framework / amendments.

Recommendations[24]*:*

I. Operational issues

(A) Issues common to Venture Capital Funds (VCF) and Foreign Venture Capital Investors (FVCI).

1. Lock-in of shares after listing:

[24] Ibid

The requirement of lock-in of shares after listing may be removed.

2. Investment in listed companies:

The committee in furtherance to the K.B. Chandrashekhar committee and to keep pace with the changing dimensions of the economy suggested further relaxation in the capping earlier prevalent in terms of listed companies. Further the entire strata of investment could be break down and was allowed to be invested in the entire life span of the so dedicated fund.

3. Type of instruments of investment:

"Some kind of hybrid instruments which are optionally convertible into equity may be permitted as a class of investment instruments under the 66.67 per cent (then recommended) portion of the investible funds".

4. Special Purpose Vehicles (SPV):

"SPVs which are mandated for promotion/investment of a Venture Capital Undertaking (VCU) may be permitted up to a maximum of 33.33 per cent portion of investible funds".

5. Investment in Non Banking Financial Services:

VCFs/FVCIs may be permitted to invest in NBFC in equipment leasing and hire purchase.

6. Investment in Real Estate:

VCFs/FVCIs may be permitted to invest in real estate.

7. Investment in Gold Financing:

Gold financing should be removed from negative list for VCF/FVCI. However, such financing should be restricted to gold financing for jewelry alone and not pure trade and speculation in gold.

(B) Issues relating to venture capital funds

1. Investment in offshore VCUs:

"VCF should be permitted to invest in offshore VCUs. RBI could be requested to periodically announce the overall limit for investment by the VCFs and inform SEBI accordingly".

2. Flexibility to distribute in-specie:

The in-specie distribution of assets may be permitted at any time, as per the preference of investor(s).

(C) Issues relating to foreign venture capital investors:

1. Appointment of custodians:

The appointment of custodian by FVCI may be continued to facilitate the maintenance of records and a smooth transition when the VCU's shares get listed.

2. Investment Limits:

The restriction of not investing more than 25 per cent of the investible funds of a FVCI in a single VCU should be removed.

II. Tax related issues

1. Section 10(23 FB):

"If clause (c) of Explanation I of Section 10(23FB) is deleted, no further amendments to this Section will be required whenever SEBI changes the definition of 'Venture Capital Undertaking'. After deletion of this clause, all VCFs which are formed as trust/company duly registered with SEBI would be eligible for exemption under Section 10(23FB). Alternatively, the definition of 'Venture Capital Undertaking' under clause (c) of Explanation I of Section 10(23FB) may be aligned with definition of 'Venture Capital Undertaking' as defined under SEBI Regulations".

Certain amendments were suggested to resolve tax related issues completely; such re-defining of the venture capital unit and so enabling tax pass through status.

2. Exits:

"For the sake of clarity and for the removal of ambiguity, a suitable clarification may be issued through a Central Board of Direct Taxes (CBDT) circular. Alternatively, in line with Explanation 2 under section 10(23FB), Explanation 3 may be added providing that VCFs would continue to enjoy tax exemption even after they receive foreign securities in lieu of domestic securities held by them in a Venture Capital Undertaking".

3. Section 115U:
For the sake of clarity and uniformity, a suitable illustration may be issued through a CBDT circular.

4. Procedural matters:
CBDT may clarify on the procedural matters through issue of a circular. As regards Form 64, clause nos. 5, 6, 8, 10 and 12 need to be changed to 'Income of Venture Capital Funds'.

III. Foreign exchange control related issues

Wholly owned Indian subsidiaries of FVCIs registered with SEBI may be exempted from the minimum capitalization requirement of an Indian company.

Presently Applicable Venture Capital Law in India

Before the year 2000, any venture capital fund doing business in India was supposed to comply with huge no. of regulations at various stages and go through multiple approvals.

To ease down such complex requirements and simplify the law relating to venture capital investments in India, it was decided to make SEBI a single point nodal agency for registration and regulation of both domestic and offshore venture capital funds.

Further, laws related to taxation were amended and 'pass through statuses' was introduced for the income which was earned by a venture capital fund.

The VCF Regulations have been amended at regular time intervals to bring in certain changes to the law applicable regarding venture capital funds in India. Endeavors were made by SEBI to define the sectors of investments for a fund broadly by including a definition of a 'venture capital undertaking'[25] and by providing a negative list of sectors for investment. The conditions for investment were also changed to increase the ambit of available investment options to a fund. Domestic funds were also allowed to invest in offshore venture capital undertakings.

"The ambits of legal framework within which encompasses the venture capital funds, are broadly included in these Acts and Regulations:

a) The Companies Act, 1956;

b) The Income Tax Act, 1961;

c) The Indian Trusts Act, 1882;

d) The Securities Contracts (Regulation) Act, 1956;

e) The Securities and Exchange Board of India Act, 1992 (the "SEBI Act");

f) SEBI (Venture Capital Funds) Regulations, 1996 ("VCF Regulations");

g) SEBI (Foreign Venture Capital Investor) Regulations, 2000 ("FVCI Regulations");

h) Foreign Exchange Management (Transfer or Issue of Security by a Person Resident outside India) Regulations, 2000;

i) Foreign Exchange Management (Transfer and Issue of any Foreign Security) Regulations, 2004;

j) SEBI (Substantial Acquisition of Shares and Takeover) Regulations, 1997 (the "Takeover Code"); and

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[25] A 'venture capital undertaking' is defined under Regulation 2 (n) of the VCF Regulations as follows:
"Venture capital undertaking means a domestic company-
(i) whose shares are not listed on a recognized stock exchange in India;
(ii) Which is engaged in the business for providing services, production or manufacture of article or things or does not include such activities or sectors, which are specified in the negative list by the Board with the approval of the Central Government by notification in the Official Gazette in this behalf.

k) SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009 (the "ICDR Regulations")".

Domestic Venture Capital Fund

"As per the regulations, it is compulsory for a domestic fund to get registered with SEBI. In accordance with the latest version of VCF Regulations, a fund can be established either in the form of **(a)** a company incorporated under the Companies Act, 1956/2013; or **(b)** a body corporate[26]; or **(c)** a trust established under the provisions of the Indian Trusts Act, 1882 or under an Act of Parliament or State Legislation"[27].

It is mandatory for a venture capital fund to have a specifically co-ordinated pool of money and to invest that as per the provisions of the VCF Regulations. It is germane to note that a venture capital fund registered with SEBI is not permitted to engage in any other activity than those of a venture capital fund.

A venture capital fund can raise money from any of the following investor's, namely Indian residents, foreigners or non-resident Indians by issuing of units through private placement. Any scheme started or a fund set up under venture capital regulations should mandatorily have minimum contribution of at least Rs. 5 crores before initiating the operations as an established venture capital fund. The contribution made by the venture capital funds shall be subject to the following restrictions and conditions[28]:

a) Conditions:

i) At least 66.67% of the investible funds shall be invested in the unlisted equity shares or equity linked instruments of a venture capital undertaking;

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[26] 'body corporate' is defined under Section 2(7) of the Companies Act, 1956 as-
"body corporate or corporation includes a company established outside India but does not include-
a) a corporation sole;
b) a co-operative society registered under any law relating to co-operative societies; and
c) any other body corporate (not being a company as defined under this Act), which the Central Government, may, by notification in Official Gazette, specify in this behalf."

[27] Regulation 2(m) read with Regulation 2(c) and 2(k) of VCF regulations.

[28] Regulation 12 of the VCF Regulations.

ii) "Not more than 33.33% of the investible funds may be invested by way of:

a) Subscription to initial public offer of a venture capital undertaking whose shares are proposed to be listed;

b) Debt or debt instrument of a venture capital undertaking in which the venture capital fund has already been invested by way of equity;

c) The preferential allotment of equity shares of listed company subject to lock in period of one year;

d) The equity shares or equity linked instruments of a financially weak company or sick industrial company whose shares are proposed to be listed;

e) Special purpose vehicles which are created by the venture capital fund for specifically facilitating or promoting investment as per the VCF Regulations".

iii) "A venture Capital fund may invest up to 10% of the investible money in unlisted shares of a foreign company ("Offshore Venture Capital Undertaking") having an Indian connection (i.e. a company having a front office overseas, while back office operations here in India) subject to an overall limit of USD 500 million".

Offshore investments by a domestic venture capital fund can be done only in compliance with the requirements laid down by RBI and under the Foreign Exchange Management (Transfer and Issue of any Foreign Security) Regulations, 2004.

b) Restrictions:

i) "A fund has to disclose the funds contribution strategy at the time of making an application to SEBI;

ii) A fund cannot invest more than 25% corpus of the accumulated monies in any one venture capital undertaking;

iii) A fund cannot invest in associated companies;

iv) A fund has to disclose the proposed life span of the fund to SEBI;

v) Lock-in-period – a fund is not allowed to get its units listed on any recognized stock exchange till the expiry of three years from the date of issuance of units by the venture capital fund".

C) Prohibited Sectors:

"A venture capital fund registered with SEBI cannot invest in unlisted equity shares or equity linked instruments of a venture capital undertaking which are engaged in the business of:

a) Non - banking financial services excluding those non - banking financial companies which are registered with the Reserve Bank of India ("RBI") and have been categorized as equipment leasing or hire - purchase companies;

b) Gold financing excluding those companies which are engaged in gold financing for jewelry;

c) Activities not permitted under industrial policy of Government of India; and

d) Any other activity which may be specified by the SEBI in consultation with the Government of India from time to time".

Off- Shore Venture Capital Fund

"The guidelines for Offshore Venture Capital Investors issued by the Indian Government were taken back and were replaced by the SEBI (Foreign Venture Capital Investor) Regulations, 2000 ("FVCI Regulations"). The FVCI Regulations just defines a 'foreign venture capital investor' as an investor who is incorporated and established outside India, without any information about the detailed structure of the investor".

However, a little importance and focus is given under Rules 4(c) and 4(d) of the FVCI Rules on this particular aspect. As per the previously-mentioned rules, before considering any application for registration from a possible/likely foreign (money to small business) (person or business who gives money to help start a business), SEBI will bury - alia consider the fact that whether the proposed (person or business who gives money to help start a business) is an investment company, investment trust, investment partnership, (money paid regularly after retirement) fund, (way of investing money), gift (of money) fund, university fund, helpful institution or any other thing/business incorporated outside India or whether the (person or business who gives money to help start a business) is a valuable thing management company, investment manager or investment management company or any other possible way to make money incorporated outside India.

Any investor, who desires to get itself registered with SEBI under the FVCI Regulations, needs to have an assured commitment for contribution of an amount of at least USD 1 million while submitting the application seeking registration as foreign venture capital investor. A foreign venture capital investor is also supposed to appoint a domestic custodian to act as custodian of securities for the overseas fund[29].

Investment Conditions for an offshore Fund:

A foreign venture capital investor registered with SEBI can either invest in a venture capital undertaking or in a scheme or unit of a domestic fund which in turn invests directly into a venture capital undertaking.

A foreign venture capital investor has an option to invest its total funds commitment in a single domestic fund. Other investment conditions applicable on a foreign venture capital investor are similar to those of a domestic venture capital investor (including the prohibited sectors) as given in VCF Regulations.

A foreign venture capital investor is supposed to obtain prior permission of the RBI to invest in any scheme or unit of a domestic fund or in the equity shares/ equity linked instruments/ debt/ debt instruments/ debentures of a venture capital undertaking.

Investment into portfolio companies by a foreign venture capital investor is usually carried out under the automatic route as per certain sector specific cap on foreign direct investment. A foreign venture capital investor can acquire by purchasing or otherwise or sell shares/ convertible debentures/ units or any other investments held by it in venture capital undertakings or schemes/ funds set up by the domestic venture capital funds at a price reached by mutual consent among the buyer and the seller/ issuer[30].

[29] Regulation 14 of FVCI Regulations

[30] The pricing guidelines issued by SEBI or the erstwhile Office of Controller of Capital Issues are not applicable to a SEBI registered Foreign Venture Capital Investor.

The foreign venture capital investor also has an option to receive proceeds arising out of the liquidation of venture capital funds or schemes/ funds set up by the venture capital funds.

Benefits Enjoyed By VCF and Registered FVCI:

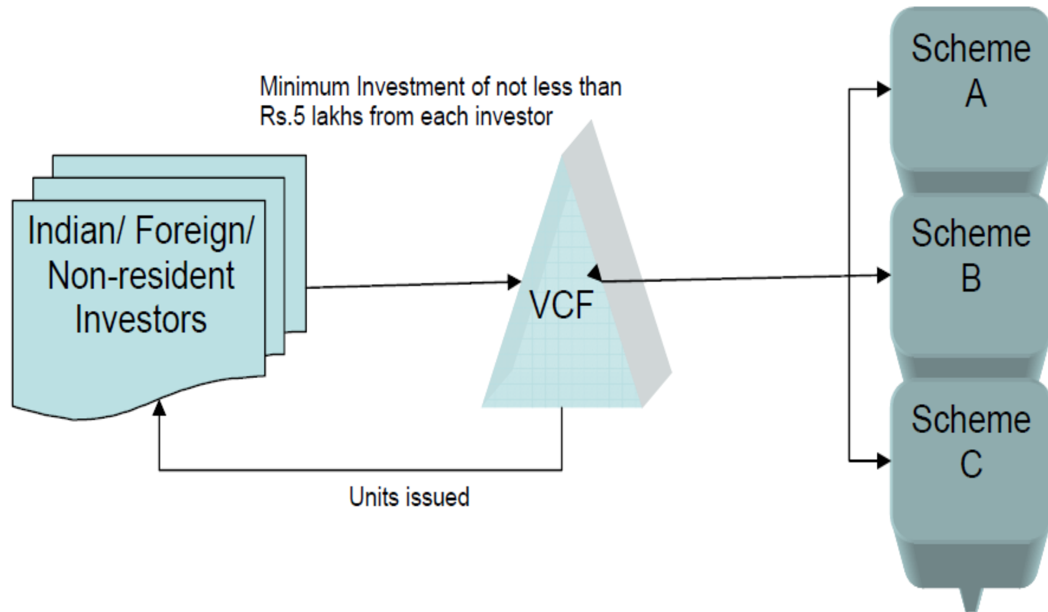
- "Prior approval is not required from the Foreign Investment Promotion Board (FIPB) for making contributions into Indian Venture Capital Undertakings (VCUs).

- In accordance with the Reserve Bank of India Notification No. FEMA 32 /2000-RB dated December 26, 2000, an FVCI can purchase/ sell securities/ investments at a price mutually acceptable to the parties and there is no ceiling or restriction applicable on them.

- A FVCI which has been registered with SEBI also enjoys the status of Qualified Institutional Buyer (QIB), which enables them to subscribe to the share capital of a VCU at the time of initial public offer. A lock-in period of one year is applicable to the shares subscribed in an IPO".

- The lock-in period provided for the pre-issue share capital from the date of Allotment, under the SEBI (Disclosure and Investor Protection) Guidelines, 2000 is not on a registered FVCI and VCF.

- In accordance with the SEBI (Substantial Acquisition of Shares and Takeover) Regulations, 1997 if the promoters want to buy back the shares from FVCIs; such a scheme would not come under the public offer requirements".



[31]

Mechanism[32]

A VCF raises monies in the form of "units." Regulation 2(l) defines "units" as "beneficial interest of the investors in the scheme or funds floated by a trust or issued by a company including a body corporate.[33]" Chapter III of the regulations provide that this money can be raised from Indian, foreign or non-resident investors by issuing such units.

As given in Chapter VI public offers for inviting subscription or purchase of units from the public is prohibited. From above two things can be construed 1) the units are the "beneficial interest" of the investors and that the VCF holds only legal interest and 2) that the VCF is a channel of investing the investors' money in various "schemes."

[31] Nidhi Bothra, Venture Capital Regulations in India, Vinod Kothari and Co.
[32] Ibid
[33] SEBI, (Venture Capital Funds), Regulations, 1996

The regulations have elucidated in a very crisp manner the core substance of the VCF. The regulations provide that the VCF can be formed either as a trust or company including a body corporate but have given the beneficial interest to the investors and merely legal interest is vested in the hands of the managers of the pooled funds. As such, in case of a trust form of VCF, it is very much clear that the funds collected are held by the trustees and that they have just legal interest in the raised money, so this raises no second thoughts about this structure.

In almost the same way, in case of a company/ body (related to big business) as well the company holds only a little legal interest in the combined money. Not very much like the usual structure of a company, money raised is big plan/layout/dishonest plan specific and cannot be invested by the company in any other way or for any other trip/business apart from those specified and that the unit holders are the real (people who receive something valuable), by that/in that way reducing the status of the company as to having only (related to trusting someone with something valuable) interest in the fund. So, it does not matter, what form a VCF is formed in the real center would be that of a trust.

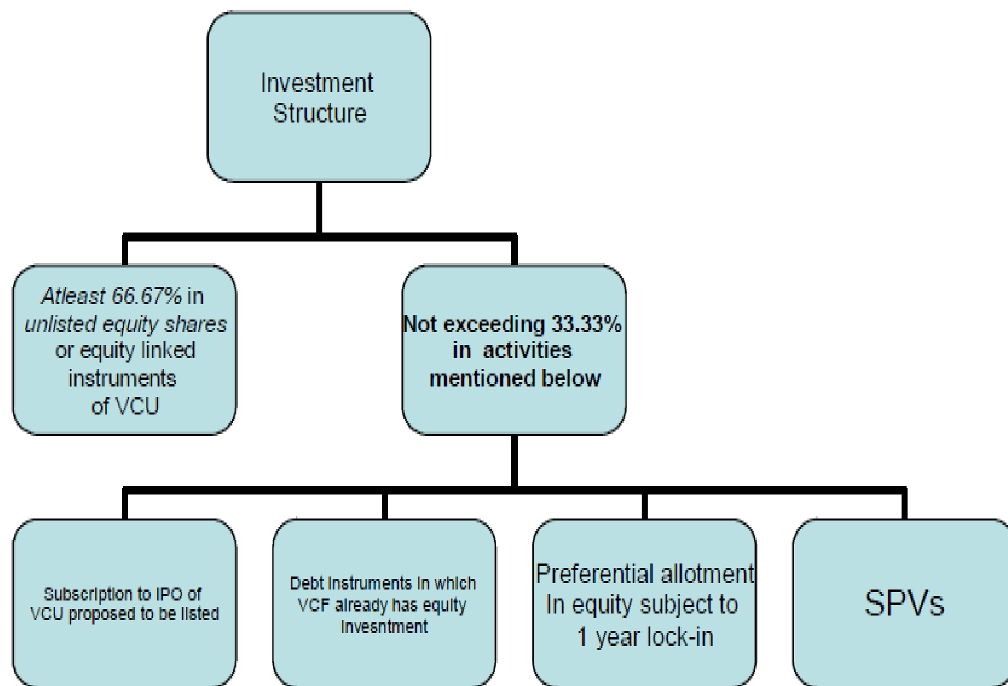
__Pictorial View of the Current Investment Structure[34]:__

[34] Supra, 34.

Not more than 25% of the corpus can be invested in one VCU

Investment in Foreign Companies subject to RBI guidelines

Shall not invest in associate companies



Current Tax Framework

With The Finance Act of 2000 came the concept of the "pass through status" for incomes arising out of a venture capital fund. Section 10(23FB) of the IT Act, 1961 read with Section 115U of the IT Act provides that such income of a venture capital fund will be taxable only for the investors of the fund.

In crux it can be construed that, the entire income of the venture capital fund is actually distributed to its beneficiaries without any suffrage of tax liability at the level of entity of the venture capital fund. Only Investors are subject to tax on income earned by them through such venture capital investments. Moreover, a venture capital

fund is not supposed to obtain any approbation from any authority in order to become eligible for the pass through status.

"The pass through status of the income of a venture capital fund is however limited for incomes arising out of investments made in a domestic unlisted company which is involved in business in the following nine sectors –

a) Nanotechnology;

b) Information technology relating to hardware and software development;

c) Seed research and development;

d) Bio-technology;

e) Research and development of new chemical entities in the pharmaceutical sector;

f) Production of bio-fuels;

g) Building and operating composite hotel - cum - convention centre with seating capacity of more than three thousand; or

h) Developing or operating and maintaining or developing, operating and maintaining any infrastructure facility as defined in the Explanation to clause (i) of sub-section (4) of Section 80-IA of the IT Act .

i) Dairy or poultry sector".

The suffrage of tax by the investors is dependent upon the form of income which becomes accrued for the investors of the fund. Generally, the income arising out of such funds can be in the form of dividends, capital gains, and interest on securities.

However, a benefit arising on receipt of such pass through status is not available on investments made by a foreign fund directly in a portfolio company. But, if the offshore investor is a resident of a jurisdiction having a Double Taxation Avoidance Agreement with India, it can avoid the potential double taxation of income in India along with its home country[35].

[35] Under Section 90(1) (b) of the IT Act, the Government of India has the power to enter into agreement with the Government any other country for inter - alia avoidance of double taxation of income under the IT Act and any other corresponding law in that country or specified territory. Pursuant to this, the Government of India has entered into agreements for avoidance of double taxation with a large number of countries. While some treaties provide for lower withholding tax on interest, some provide for concessions on dividend, withholding tax and some on capital gains. Further, Section

However, if the offshore fund has a "permanent establishment" in India, then the income cannot be avoided from being taxed, at the prevalent income tax rates in India.

Available Exit Routes:

Any venture capitalist has as the ultimate motive to realize the investment made by selling off the same at a substantial capital gain. Therefore, a venture capital firm endeavors to strive for options available in order to convert the appreciation in the value of its investments into cash.

The money which is received through this way is again invested in supporting new trips/businesses. After the unit which was helped reaches a settled state and reaches money-making working and the business/project is in a position to raise money through traditional useful things/valuable supplies like capital markets, banks or commercial banks, the (people who loan money to small businesses) close and turn into cash their investment and make an exit from the investee company.

Venture capital firms usually follow the motto of 'exiting at maximum profit or minimum loss in case of a failed venture'. Exits can be voluntary or involuntary, following options are available for disinvestment in case of a voluntary exit.

a) **"An Initial Public Offering** ("IPO") enabling listing of the shares of the venture capital undertaking at a recognized stock exchange in India: A venture capital fund has an option to exit by offering their entire or a part of the shareholding of the portfolio company during listing of the equity shares of the portfolio company at a recognized stock exchange in India".

b) **A Further Public Offer ("FPO"):** A venture capital fund also has an option to exit by offering their shareholding of a listed portfolio company at the time of a

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90(2) of the IT Act adds that where the Central Government has entered into an agreement with the Government of any country outside India or specified territory outside India under sub- section (1) for granting relief of tax, then, in relation to the assessee to whom such agreement applies, the provisions of the IT Act shall apply to the extent they are more beneficial to that assessee.

subsequent public offer made by the portfolio company to the public for subscription of shares.

c) **Sale of shares on stock exchange after listing of shares**: A venture capital fund has an option to disinvest its share of the portfolio company by trading them on the stock exchange after the shares of a portfolio company are listed at a recognized stock exchange. It should be noted that a registered venture fund has been given certain advantages in the existing law applicable to IPOs.

d) **Buy back of the shares held by the venture capital fund**: Buy back or share repurchase has following different alternatives:

i) *Buy back by the portfolio company*: The portfolio company may buy back its own shares from the venture capital fund.

ii) Buy *back by the promoter or promoter group of the portfolio company*: The promoters or the promoter group of the portfolio company have an option to buy back the equity stake of the venture capital fund enabling an exit.

e) **Sale of shares to a new investor**: The venture capital fund may also exit by selling its entire shareholding in the portfolio company to a strategic investor.

CONTEMPORARY DEVELOPMENTS

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Venture capitalism as a funding mechanism has seen various deliberations in the recent times all over the world. India being one among the nations who are striving for economic superintendence has evolved its regulatory setup to attract as much as foreign investment possible also domestic endeavors in this regime is fastened to support the objective of pink financial health of the country.

According to EY (Consultancy Firm), there were 189 early-stage deals in the first nine months of 2014—total worth of Rs 6,764 crore, or $1.09 billion. This is significantly higher than deal flow for all of 2013, when there were 179 deals worth Rs 3,900 crore or $630 million[36].

As willingness and interests of Indians are increasing in the e-commerce sector with ever booming online transactions entrepreneurs are coming up with more and more innovative business ideas which are being fueled by foreign investments and venture capitalists support in particular.

Indian online retail is expected to reach Rs 50,000 crore by 2016 from about Rs 12,000 crore in 2013. Over the past 18 months, the venture industry has begun to see several breakout companies driven by the significant growth and adoption of internet in India[37].

Various other sectors where VCs are backing startups include healthcare, education, financial services and food or agriculture ventures. This year, the likes of online test preparation portals Embibe and Toppr, financial services portals like Policybazaar and BankBazaar, agriculture equipment maker MITRA and supply chain firm Allfresh have all raised funds through VC funding.

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[36] Madhav Chanchani, Venture capitalists put $1 billion into early-stage projects in 2014 on back of rising ecommerce deals, ET Bureau, Oct 3, 2014.

[37] IBID

Investors with enhance economy traits and better investing environment have realized that currently India is going through once in a life time phase of building up and as such are more keen in making contributions to this growth.

This trend of immense investments into internet is expected to continue in the next year driven by increased confidence of VC funds, strong growth, the coming-of-age of ecommerce companies and increased interest from overseas and strategic investors. However, any major declines in global tech markets could likely impact this trend adversely in India.

The recent budget by the Indian Govt. surely shows traits of being investment friendly with specific earmarked funds for start-ups. A separate fund of Rs.10, 000 Croes has been dedicated for this purpose. According to Finance Minister Mr. Arun Jaitley, it will be "equity, quasi-equity, soft loan and other risk capital for start-ups[38]."

Agriculture has come up as a new sector attracting a lot of angel investors. This has been fuelled by the realization that food security is a vital, long-term necessity. Studies suggest that in future, for every Rs 100 increase in GDP, Rs 41 will be spent on food[39].

At the recently held Global AgInvesting Conference, data released indicated that agro businesses would provide better returns of about 11%, compared to 3-5% yield from bonds and equities.

Another trigger for anticipating healthy foreign investments is that India and China are the two top growing economies and relaxed policies and investor friendly environment has paved a rosy way for venture capitalism in India.

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[38] Preetam Kaushik, Rise Of Venture Capital In India: Nothing Ventured, Nothing Gained, Business Insider India, July 21, 2014.
[39] Ibid

A very latest discuss paper from SEBI has been out recently which focuses on various issues related to startups and the entire regime of regulations governing venture capital Industry and related fund seekers and investors.

The most important concern which has been highlighted is related to increase the exit options for angel investors and enhance operational ease for the same. A proposal has been approves by the SEBI Board in its meeting held in June 2013, allowing small and medium sized industries(SME) to list in institutional trading platform(ITP) without having issued initial public offer(IPO).

Recent interactions with professionals from software industry brought issues regarding funding for startups in this particular sector and in order to resolve certain issues in the entire framework and facilitate funding the concept of ITP has to be taken to a different level and enhanced in order to make operations of these budding professionals.

Other recommendation with respect ICDR includes reducing the 3 year lock in period for investors. The requirement of initial contribution of 20% of the capital for lock in period has been a barrier for various startups and as such ways are being deliberated to do away with this requirement.

Moreover ITP has to be modified in order to facilitate the operations of startups raising funds through this mechanism.

It has been proposed that two categories of investors must be allowed for investors through this new and modified platform of investment namely QIB- Qualified Institutional investor and NII- Non-Institutional investor. The caps for investment have been decided to be at 75% and 25% respectively.

Further proposals are related with redefining of QIB's and other requirements such as the lock in period and disclosing of objectives before the issues in this particular platform. Similar measures are suggested for disclosures regarding the group companies and disclaimer clauses etc.

As such all these deliberations by the ultimate nodal agency for securities and investments in India i.e., SEBI indicate towards enhancing of the entire thought process guiding the venture capital industry.

These progressive measures along with investor friendly environment that has been fostered by the Govt. surely assures coming up of an era of increased investments, more risk taking investors and happy budding business professionals who can now dare to realize their dreams.

CONCLUSION

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Growth is a process which can only be materialized and realized in the desired form if the untried is tried and unconventional way of thinking is implicated over the orthodox ways. Angel Investors or Venture Capitalists are certainly that sacred channel for entrepreneurs with innovative business Ideas which have the potential for immense growth to turn their prospective plans into reality.

The Venture Capital Industry in India has come a long way since its inception as an idea in the 1970's and 80's. The then alien concept of providing aid to the untried and backing on the unconventional has now become one of the driving forces for one of the fastest growing economies of the world.

The earlier protective environment has now been converted into an arena for the world leaders of different economies to provide the required fillip to the prospective business honchos who have inspiring and innovating business ideas capable of changing the world and perspectives the way business world look at them.

The initial period when the concept of venture capital financing was being conceived had plethora of restrictions and barriers in terms of the regulatory set up and govt. perspective. However, gradually amazing growth trends are being witnessed signaling towards enormous economic growth of the country with more and more budding business dreams being converted into reality for the prospective business leaders.

During 90's when various deliberations were being made in the entire economic arena of our country as a result liberalization, privatization and globalization venture capitalism as concept and idea got amazing support from around the world especially from the Indians engaged in the IT Industry in Silicon Valley which furthermore strengthened the foundation for an amazing industry of angel investors.

The most tremendous and powerful booster for this industry was that of SEBI being appointed as its coordinator and regulator i.e. the single nodal agency looking after all the aspects encompassing this entire regime of venture capitalists.

During 90's various laws applicable for venture capital investments were readdressed by the respective authorities and the most important organ of this regulatory setup i.e. the Venture capital regulations were formed. This codification and overall efforts to consolidate the facilitating mechanisms for this industry proved fruitful later on.

As part of all these deliberations various committees were setup to delve into various issues eminent from various perspectives for the industry. K.B. Chandrashekhar committee paved the way for smoothening of transaction in the venture capital arena. Various restrictions and barriers were done away with in the year 2000 with amendments in the Domestic Venture Capital regulations based on the recommendations of this committee.

Also most importantly Venture Capital Regulations for offshore investors were codified in the same year. This step has proved to be the most encouraging one for the venture capital industry as it eased the foreign investments in our country and gave support to the developing economy from offshore investments.

Another important development while sketching the historical development for this sector which cannot be ignored are the recommendations by the Ashok Lahiri Committee. The result of appointing SEBI as the single nodal agency proved fruitful with its regular attempts to enhance the environment of venture capital investments. Recommendations of the above mentioned committee are perfect example of the same.

Based on these recommendations various restrictions on investments both domestic and offshore were done away with. Also the caps for investment were altered and relaxed. Not just the venture capital regulations these recommendations covered relevant aspects from various laws including the tax concerns and suggested amendments in the IT, Act.

One of the major incentives which boosted the investments in this particular sector is the tax exemptions provided. The introduction of the 'pass through' status seemed lucrative to various investors and brought in a lot of funds.

Furthermore if the limitation of sectors is removed which is currently limited to nine sectors investments from around the globe can be multiplied with amazing pace. This would facilitate easy tax structures, more exemptions there by making such investments all the more lucrative.

The proposed Direct Tax Code, has provisions relating to the above mentioned and the way current Govt. is operating with all their attempts to make the Indian business environment all the investor friendly one can anticipate such changes being applicable in the Indian tax structures pretty soon.

Certain other recommendations which have been made in the past and are not yet implicated include increment in the exit routes available with the investors which for example can be reduction in the lock in period etc. Such progressive amendments would instill more confidence among the investors and would make the investment mechanism more simplified and easy to apply.

The efforts being made by the Govt. along with the major players of the corporate world deserve ovation as the recent figures evidently bring out the picture of enhanced investments across all sectors in the country. Although IT Sector remains the favorite with much of the investments being targeted at e-commerce ventures various other sectors are now receiving plethora of funds. To name a few one can cite Agriculture, pharmaceuticals, bio-technology etc.

The available structures for venture capital industry if increased and provided with more easy going options will surely enhance the investments. Limited Liability partnership is one such form and is most discussed among the corporate honchos these days. With LLP Act, being enacted after 2008 the chances for this have increased manifold.

As such we have come a long way from the rigid non-flexible phase of restrictive and orthodox economy to a more liberalized investor friendly and global oriented one.

But still as now is the time and the phase which comes only once in the history of any nation which India is going through currently, one needs to accelerate with all possible force to enhance such positive and progressive economic deliberations leading to India being recognized as the most Significant economic Super Power in the Contemporary Times. And development of budding and prospective growth oriented ideas will pave the way for this and provide the required fuel.

More flexibility in the current regulatory setup will certainly prove fruitful and take the Indian Economy to the ultimate stage of glory which we have always dreamt about.

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Specific links are mentioned along with the relevant footnote.