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Fuelling Entrepreneurship

Start-up survey findings and policy recommendations

October 2022

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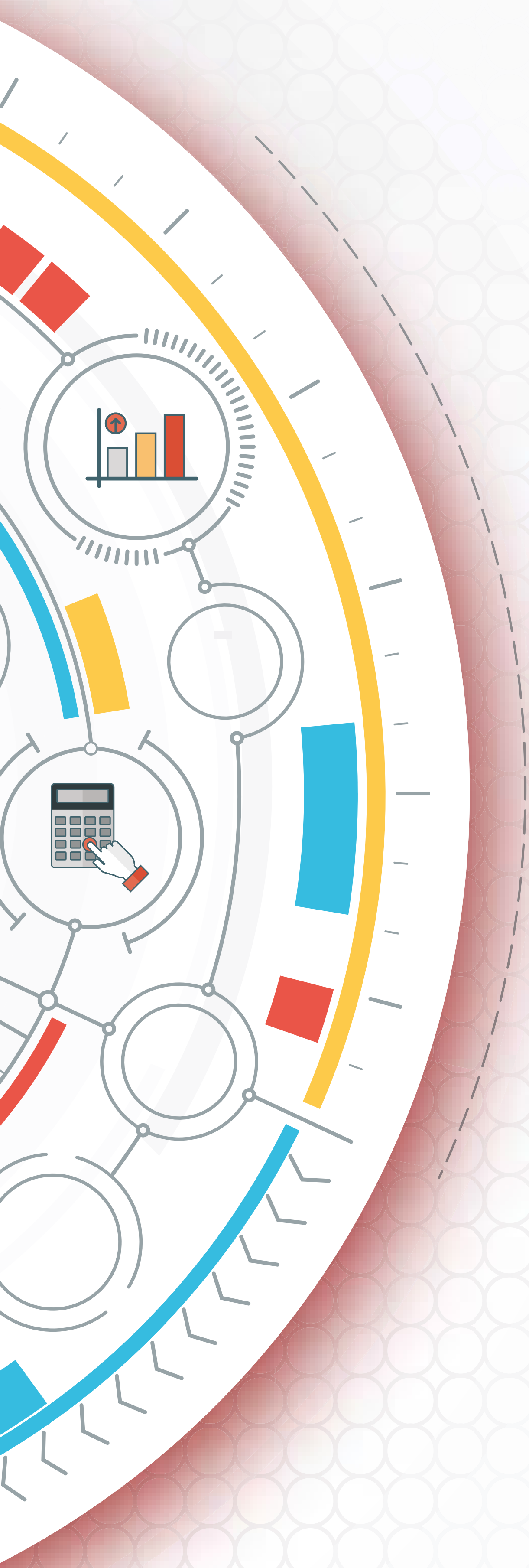

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Preface

Start-ups help drive innovation, come up with new offerings, pioneer new business models and solve problems with agility. The growing success of the start-ups in India is evident from rising confidence and trust of global investors, increasing number of unicorns and the resilience demonstrated by our entrepreneurs.

The momentum is with us to make India the world's biggest start-up hub. Going forward, talent and capital will be the key ingredients that will determine the pace at which the start-up ecosystem expands and succeeds. India is a known tech-talent hub and given the demand, good talent is always in short supply. NASSCOM's programmes, such as Future Skills Prime and Deep-Tech Start-ups Club, focus on enabling the availability of the right talent. Access to capital has significantly improved over the recent years but continues to be a major challenge, irrespective of the stage at which the start-ups are. The report presents updated information regarding access to capital for start-ups, including, trends in equity funding deals, support being extended to start-ups by the government etc.

What can be done to encourage access to capital? How can the existing legal and regulatory framework be tweaked to enable inflow of more domestic and foreign capital into India's thriving start-up ecosystem? How can collaboration between start-ups, industry and academia be encouraged to leverage synergies? This is the theme of our report.

To find answers to the above questions and focus on the discussion on the way forward, NASSCOM, TiE Delhi-NCR and Grant Thornton Bharat conducted a survey of investors and entrepreneurs and interviews with start-up ecosystem leaders. The survey corroborates access to capital as the most important enabler as well as the challenge for a start-up in India today.

We believe that the government can play a vital role by bringing in necessary changes with respect to tax policy, revamping methods of procurement to create more market opportunities, facilitating industry, start-up and academia collaboration and operationalising the norms for overseas listing. This report attempts to clear the pathway on some of the identified issues related to access to capital.

The start-up ecosystem in India is poised for tremendous growth and there is a need for best minds in the ecosystem, be it the founders, investors, industry associations, legal experts, academia, and of course, the government and the regulators, to continuously engage, collaborate and help clear the pathway for the success of the start-ups. We look forward to this exciting journey.

Ashish

Ashish Aggarwal
Vice President and Head of Public Policy
NASSCOM

Srikant Sastri
President
TiE Delhi-NCR

Raja Lahiri
Partner and TMT Leader
Grant Thornton Bharat

Executive summary

India has emerged as the third-largest ecosystem for start-ups globally, with 100+ unicorns and over 79,000 start-ups recognised by the Department for Promotion of Industry and Internal Trade **(DPIIT)** across the country.

2021 witnessed start-up funding from Private Equity **(PE)** and Venture Capital **(VC)** investors of USD 48.2 billion, being the highest in the last decade. This was coupled with 65 companies raising USD 17.7 billion via Initial Public Offering **(IPO)**, an increase of 2.7 times in issue size, as compared with 2020. This demonstrates the confidence and strength of the Indian start-up ecosystem. In 2022, PE and VC start-up funding continues to be strong at USD 5.1 billion for six months ending 30 June 2022, although global downside trends in funding as well as valuations are expected to continue in 2022, which may impact start-up funding in India as well. Irrespective of the trend at any point in time, access to capital is key to the success of any start-up ecosystem.

It is in this context, this report by NASSCOM, in partnership with TiE Delhi-NCR and Grant Thornton Bharat, analyses the state of access to capital to the start-ups in India.

The report covers findings of a detailed survey of the start-up ecosystem in India comprising founders, investors, incubators, etc., and examines the issues and challenges in access to capital, throughout the life cycle of a start-up, i.e., from early stage to listing.

The survey indicates that access to capital and various funding options are the most important enablers as well as the top challenge, particularly for early stage start-ups. For others, access to capital continues to be the most important enabler but other aspects, such as ease of doing business and listing, also attain importance.

Over 40% of the respondents highlighted access to capital as the most important enabler for success of the start-up, followed by access to various funding options (debt, equity, structured debt, public markets etc.,) at 23%, ease of doing business at 20%, access to mentorship at 13% and ease of liquidation and tax incentives at 4%.

Funding: 49% respondents highlighted PE and VC as the most preferred option for raising capital, followed by bootstrapping/ founder-funding (22%), incubators (18%) and listing (11%).

Challenges: 36% respondents highlighted lack of innovative funding instruments, followed by:
- Valuation mismatch between founders and investors (22%)
- Lack of funding platforms such as crowdfunding (23%)
- Lack of funding in place of business and tax incentives (19%)

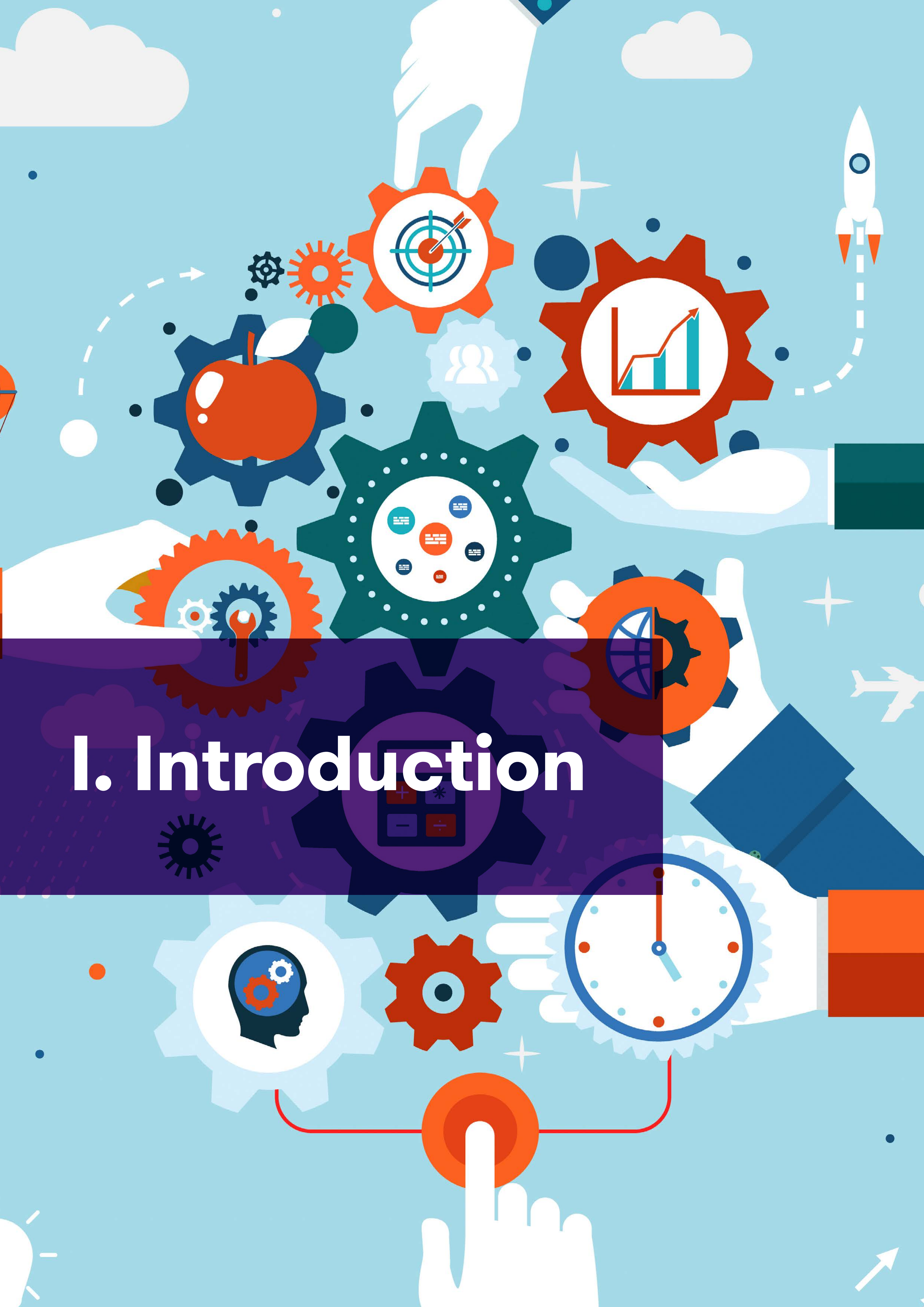
The report covers an in-depth analysis of various sources of funding available to start-ups, both domestic and overseas, as well as listings, both in India and overseas. The report explores ways in which direct overseas listing may be made possible for the advantage of start-ups in India and the regulatory changes required in India to implement them.

The key recommendations, which have been dealt in detail, include:

1. Increased impetus for domestic investors by way of tax reforms, especially by harmonising tax rate on Long Term Capital Gains **(LTCG)** applicable to resident and non-resident investors; harmonising tax rate on LTCG applicable to listed securities and unlisted securities.
2. Creating and enhancing market opportunities for start-ups through government procurement reforms.
3. Supporting creation of industry-led innovation clusters to enhance collaboration between start-ups, industry and academia
4. Regulatory and tax reforms to enable direct overseas listings.

The recommendations are an outcome of the survey findings, interactions with the start-ups, entrepreneurs, mentors and investors.

I. Introduction



A. Start-ups roar in India: The current landscape

In the last two decades, India's booming start-up landscape has grown to become the world's third largest.

Enterprises with the following specifications have been recognised as start-ups by DPIIT:

1. It has been incorporated/registered for not more than 10 years in any of the following forms:
   - A private limited company under the Companies Act, 2013 (including one-person companies).
   - A partnership firm under the Partnership Act, 1932.
   - A Limited Liability Partnership **(LLP)** under the LLP Act, 2008.
2. Its turnover has not exceeded INR 100 crore for any of the Financial Years **(FYs)** since incorporation.
3. It is working toward the innovation, development or improvement of products/processes/services or is a scalable business model with high potential for employment generation and wealth creation.
4. It has not been formed by splitting up or reconstructing an already existing business.

79,306* Start-ups recognised by the government

6,50,000 Jobs created by recognised start-ups

107* Unicorns in India, 44 added in 2021 and 21 added in 2022

Source: Startup India, Invest India *as of September 2022

India's success story in the start-up ecosystem is evidenced by a number of factors:

- India is home to the world's third largest number of unicorns, next to the United States of America **(USA)** and China.[1] As of September 2022, 21 unicorns have been added during the year, bringing the total number of unicorn start-ups in India to 107, with a total valuation of USD 340.79 billion.[2] Unicorns are companies with a valuation of over USD 1 billion.
- The average deal size has increased remarkably, with investment rounds closing at record speed. PE investment values recorded USD 48.2 billion in 2021, marking the highest yearly values witnessed in any given year since 2011. 2021 witnessed 1.5 times growth in the investment volumes, compared with 2020, attracting a considerable portion of funding from overseas investors.[3]
- Since the launch of the Start-up India initiative by the government in 2016, 79,306 start-ups have been registered with the DPIIT.[4] 70 incubators have been recognised for funding under the Startup India Seed Fund Scheme since the launch in April 2021.[5] The development of the Innovators Growth Platform **(IGP)** and the Gujarat International Financial Tec-City **(GIFT)** has created a conducive environment for the growth of start-ups. A detailed discussion on these initiatives is captured in this report.

The success of start-ups is particularly noteworthy as the ecosystem is still nascent. There is a lack of access to capital, particularly at the initial stage. Despite the growth in the support infrastructure, such as incubators, there is a need for more interventions. Awareness about market opportunities continues to be low and challenges around ease of doing business and other regulatory hurdles, continue to be significant.

This report examines the various sources of domestic and foreign funding available to start-ups, and the issue of direct listing of start-ups in foreign jurisdictions. It explores ways in which such overseas listing can be implemented in India.

NASSCOM, TiE Delhi-NCR & Grant Thornton Bharat survey

The report draws from a survey conducted by NASSCOM, in partnership with Grant Thornton Bharat and TiE Delhi-NCR (the survey), with the objective to gather deeper insights about the start-up ecosystem in India. The survey sought inputs from various stakeholders (start-ups, investors, incubators, etc.,) around the current and future state of the start-up ecosystem in India. The respondents covered a variety of investors and start-ups ranging from those that have been operational for less than a year to more than 10 years. In terms of revenue generation, the respondents could be placed in three categories: less than USD 5 million, USD 5-25 million and more than USD 25 million. In terms of business models, majority of the respondents represented tech-enabled start-ups focused on India and other emerging markets, while others represented global start-ups with India back-office presence.

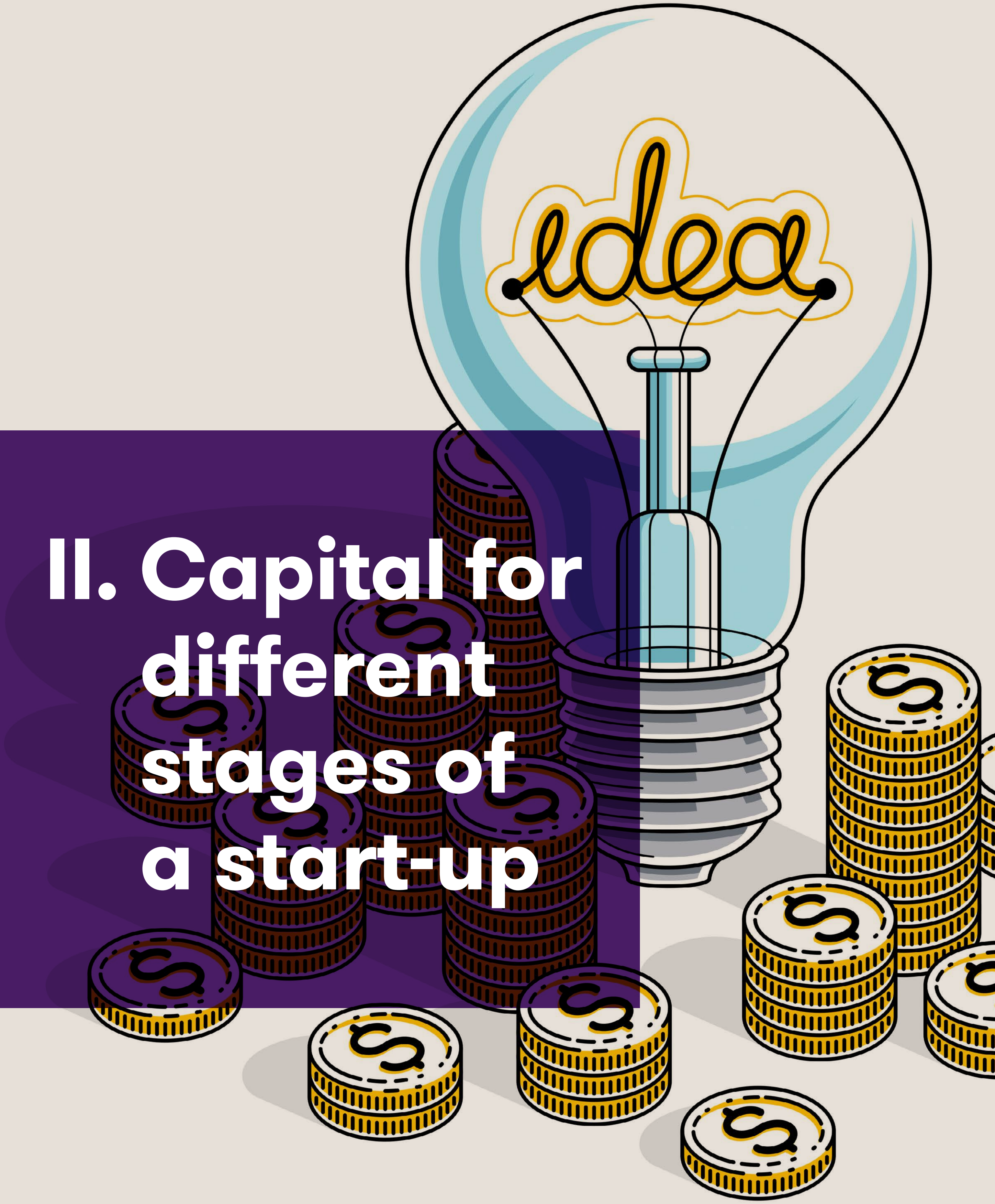
A total of 131 respondents participated in the survey with the set of questions largely focused on:

1. Key enablers, such as access to capital and incubators, for a start-up to be successful.
2. Regulations, compliances and ease of doing business in India.
3. Listing in India and overseas capital markets.

The survey findings have been referred to throughout the report in relevant parts, to add value by giving data-points and insights on what start-ups and investors think. However, given that the findings were based on a sample and cover select focus areas for start-ups, the conclusions are only indicative and not necessarily comprehensive.

1. Hurun India Future Unicorn List 2021, available at: https://www.hurunindia.net/hurun-india-future-unicorn-list-2021
2. The Indian Unicorn Landscape, Invest India, available at: https://www.investindia.gov.in/indian-unicorn-landscape
3. Grant Thornton Dealtracker, Providing M&A and PE Deal Insights, 18th Annual Edition, 2022, available at: https://www.grantthornton.in/globalassets/1.-member-firms/india/assets/pdfs/grant_thornton_dealtracker_annual_abridged_final.pdf
4. DPIIT Recognition, Startup India, available at: https://www.startupindia.gov.in/content/sih/en/startup-scheme.html (as of September 2022)
5. Startup India Seed Fund Scheme, Portfolio, available at: https://seedfund.startupindia.gov.in/portfolio

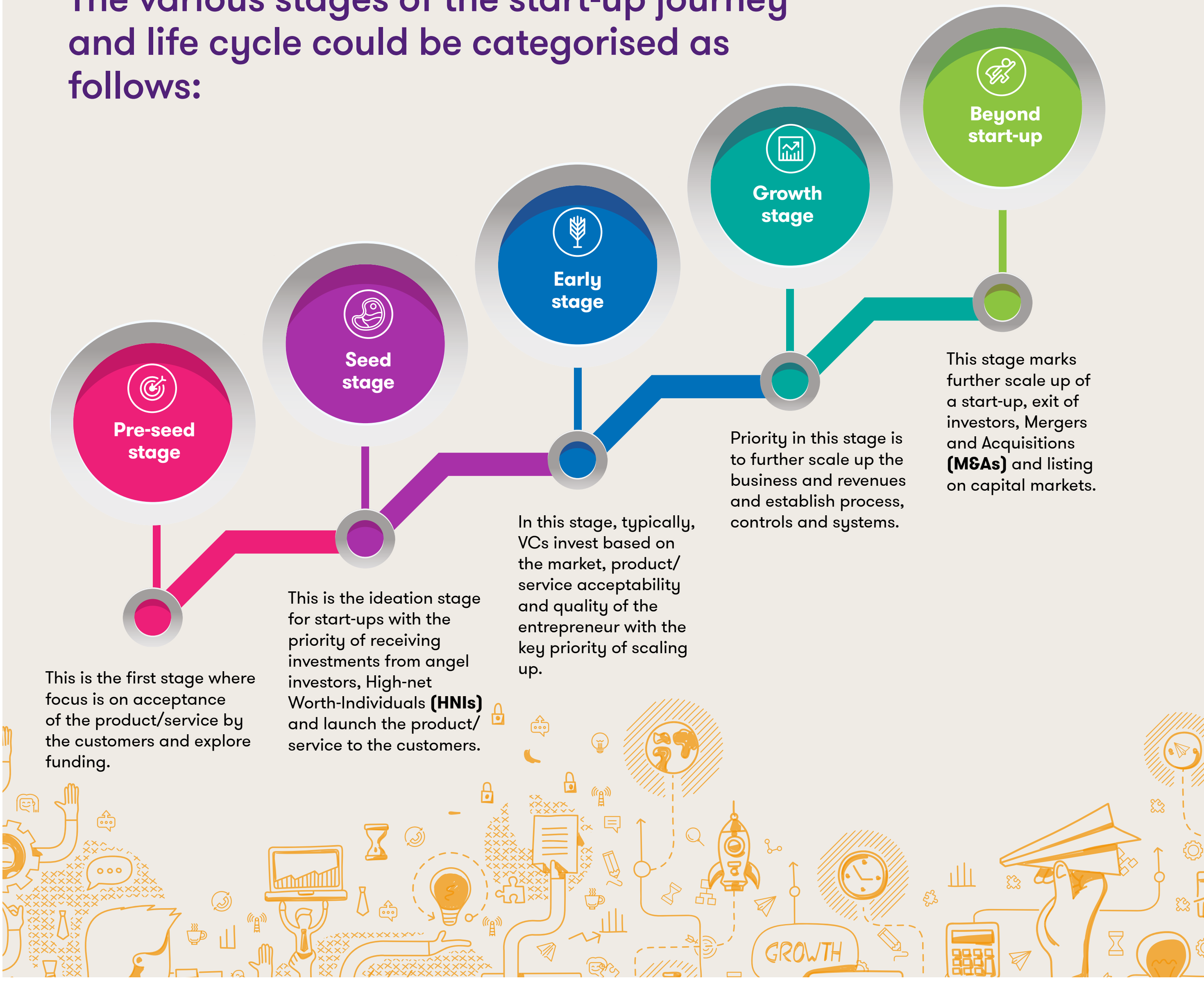
II. Capital for different stages of a start-up



This section dives into the various stages of a start-up and looks at sources of funding, challenges and ways of ameliorating access to capital throughout the various stages of a start-up.

A. Start-up journey and life cycle: Stages and priorities

The various stages of the start-up journey and life cycle could be categorised as follows:

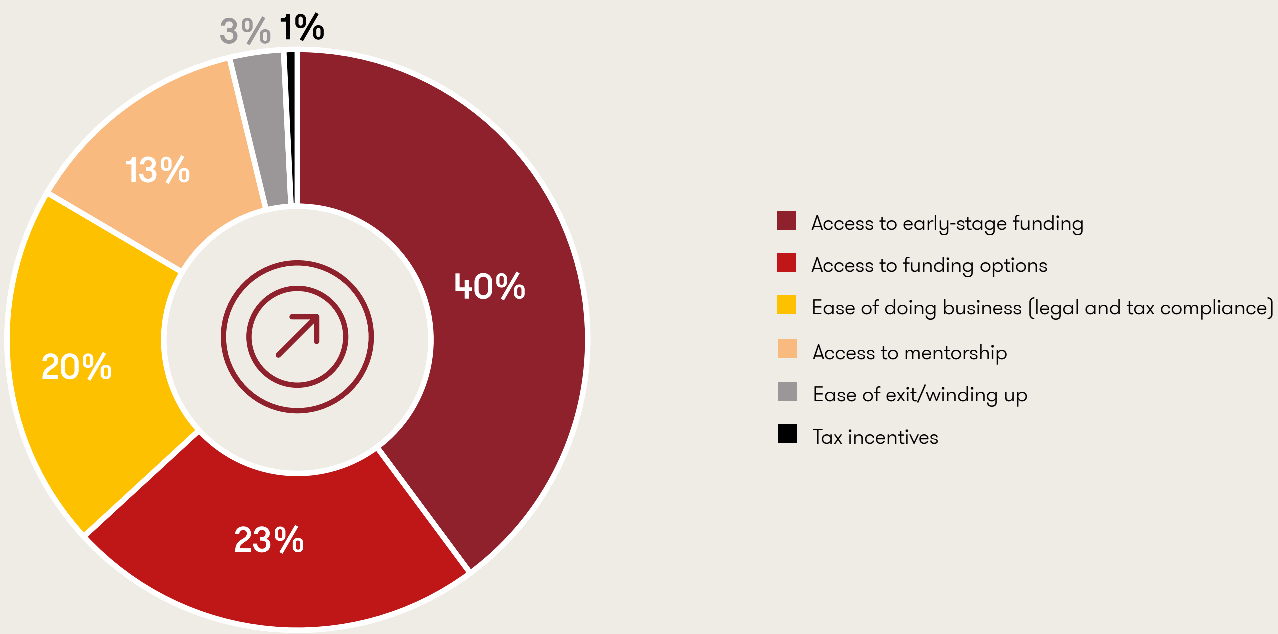


B. Sources of funding for start-ups

Funding objectives evolve with the life stage of a start-up as detailed in the graphic above.

The survey shows that access to early-stage funding and different funding options are the most important enablers for start-ups, particularly for those in the early stages of the start-up life cycle.

Most important enablers for your start-up success journey



- Overall, 40% respondents view access to early-stage funding as the most important enabler for their start-up success, followed by access to funding options cited by 23% respondents.
  - Among start-up respondents that have been operational for less than 10 years, 41% view access to early-stage funding as the most important enabler for their start-up success, followed by access to funding options cited by 23%.
  - Among start-up respondents that have been operational for more than 10 years, 42% view ease of doing business (legal and tax compliance) to be the most important enabler, followed by 25% citing access to funding options.
- While the perspective on the most important enabler for start-up success changes as a start-up matures and strengthens its business model, access to funding remains an overall dominant enabler for start-ups.

Further, the survey asked respondents to provide details on funding options that the start-ups were targeting. Overall, PE and VC funding are the top choices for funding. While, for start-ups with a revenue less than USD 5 million, bootstrapping emerged to be the top source of funding. Overall, 28% of the respondents are targeting to get VC funding for their start-ups, while 22% are considering bootstrapping and 21% are looking to raise PE.

Funding source	Overall	Revenue less than USD 5 m	Revenue more than USD 5 m
Bootstrapping - self, family and friends	22%	25%	9%
Incubator	18%	20%	9%
VC	28%	27%	31%
PE	21%	19%	26%
Domestic listing	6%	5%	11%
Overseas listing	5%	3%	13%

The different types of funding are discussed below:

i. Bootstrapping

It refers to building a company with personal savings and the cash coming in from the first sales. Borrowing from friends and relatives, prompt invoicing, choosing customers who pay quickly and negotiating best terms with suppliers are common bootstrapping methods. This funding option is skewed towards individuals with access to sizeable personal savings or a network willing to make such discretionary investments.

The findings indicate that bootstrapping is an important source of funding for early-stage start-ups. 25% of the early-stage start-ups stated that they are targeting this mode of funding, compared with 9% of the growth-stage start up respondents.

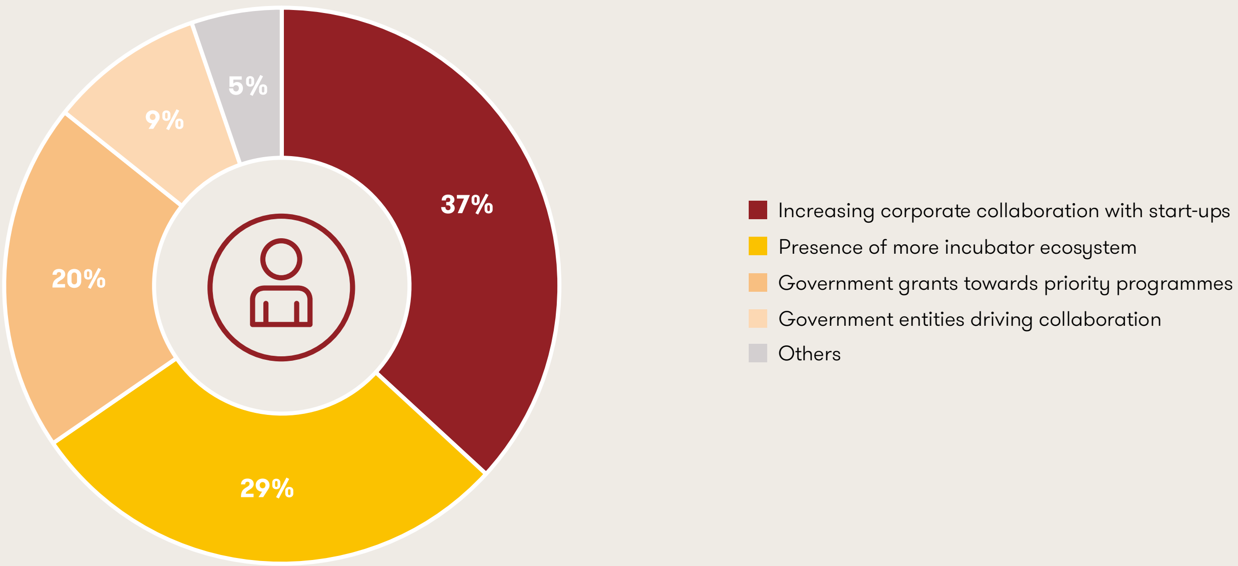
ii. Incubators and accelerators

Incubators are usually responsible for mentoring start-ups, providing ideation and technical support, access to resources, networking events, etc. India is home to over 520 active tech incubators, including both government-supported and private incubators.[6] There are more than 100 cities in India with at least one tech incubator or accelerator programme, with over 63% of the programs being active outside of tier 1 cities.[7] Growth in programmes outside established start-up hubs is primarily due to incubators set-up by academia, industry associations such as NASSCOM and government agencies.

The incubator ecosystem is critical for the development of grassroot entrepreneurship, particularly outside of tier 1 cities. 20% of early-stage start-ups and 9% of growth-stage start-ups surveyed are targeting incubator funding.

6. Start-Up Catalysts – Incubators & Accelerators, NASSCOM, 2020, available at: https://nasscom.in/knowledge-center/publications/start-catalysts-%E2%80%93-incubators-accelerators
7. Ibid

Ecosystem support most critical to encourage grassroot entrepreneurship in tier 2/3/4 cities and towns



The Department of Science and Technology, Ministry of Science and Technology is driving setting-up of new incubator and accelerator programmes. Ministry of Electronics and Information Technology is focused on enhancing capabilities especially in technologies, such as Internet of Things **(IoT)**, Artificial Intelligence **(AI)** and blockchain. The Ministry of Micro, Small & Medium Enterprises **(MSMEs)** supports Technology Business Incubators **(TBIs)** primarily around academic and technical institutions to tap potential technology ideas and innovations.

The programmes supported by multinational companies have increased steadily and consistently over the last decade. Majority of the programmes supported by corporates are focused on early stage and growth stage start-ups and are majorly concentrated in start-up hubs such as Bangalore, Mumbai and Delhi-NCR.[8]

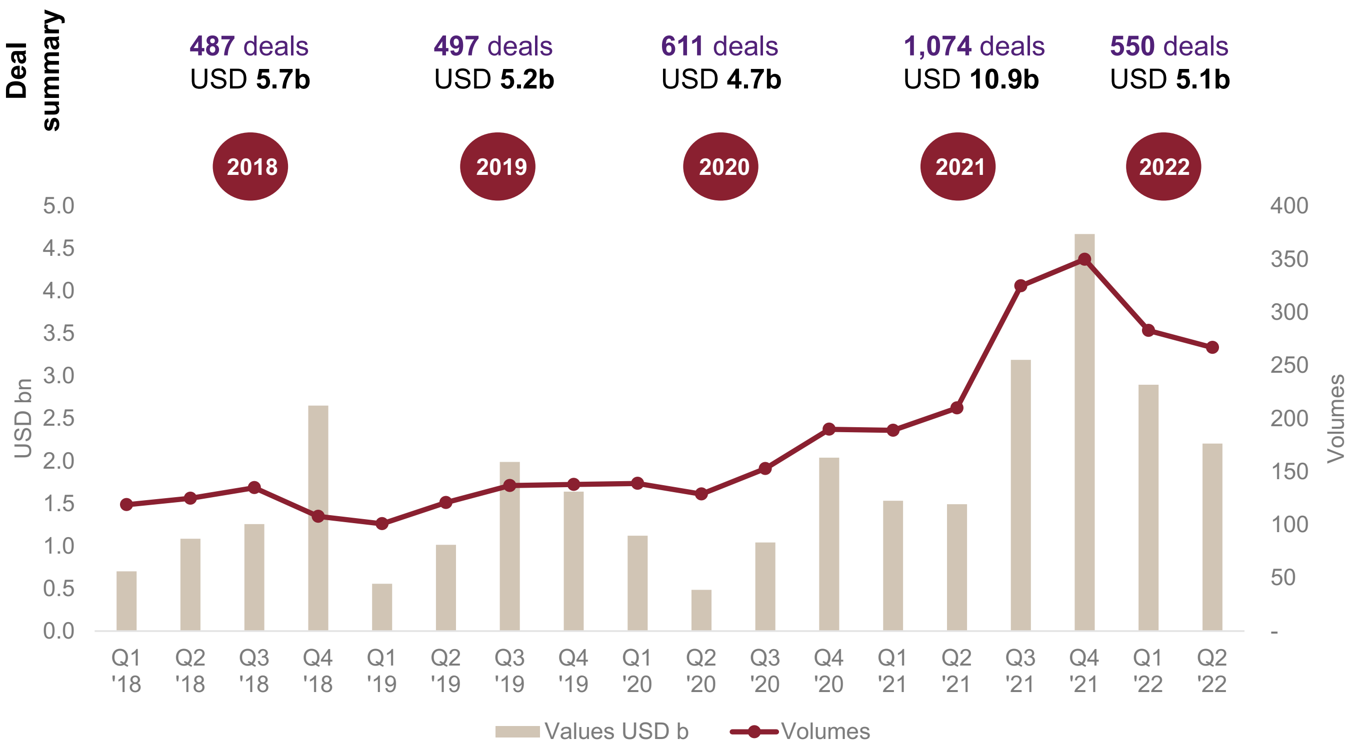
8. Supra note 6

iii. PE and VC

PE entails investment from HNIs and institutional investors. VC can be said to be an arm of PE, where equity investment is made into young ventures or start-ups that are poised to have a high growth potential over long-term. It usually entails investment from specialised VC funds and investment banks.

The following gives an insight into the kind of PE/VC deals that have happened in India recently:

- Start-ups raised USD 5.1 billion during January-June 2022 as against USD 3 billion in the same period in 2021.
- Already during January-June 2022, a greater number of deals that are valued at or above USD 50 million have been witnessed than in the entire year 2019. The investor and start-up community are showing strong signs of recovery from the pandemic.



Source: Grant Thornton Dealtracker (as on June 2022)

The findings indicate that PE and VC are the leading funding options for start-ups across stages of the business lifecycle. 47% of early-stage start-ups and 57% of growth-stage start-ups surveyed are targeting PE or VC funding or both.

iv. Venture debt funding

It is an alternative to commercial bank debt financing that involves an investor lending money to an entrepreneur for a certain period at a given rate of interest. The total venture debt funding in Indian start-ups has almost doubled to approximately USD 538 million in 2021 from from USD 281 million in 2019.[9]

Venture debt funding typically accompanies venture equity financing. It is usually extended to firms that have raised at least a round of VC and are relatively mature. For the same reason, accessing venture debt funding as a standalone funding option is not viable, especially for early-stage start-ups. Venture debt funding is relatively young in India at almost 12 years old, dominated by only a few players and remains under-penetrated. Indian companies raised USD 0.5 billion in venture debt in 2021, as compared to USD 68 billion by US companies during the same period.[10]

v. IPO

The last leg of the start-up journey could entail raising money directly from the public through listing on a public stock exchange, in India or overseas. Once listed, a company graduates from the status of a start-up as per one of the criteria in the definition under the Indian laws.

Domestic listing options in India entail listing on the National Stock Exchange **(NSE)** and the Bombay Stock Exchange **(BSE).**

Overseas listing of Indian start-ups in foreign stock exchanges is currently allowed only in an indirect manner, i.e., via the American Depository Receipts **(ADR)**/Global Repository Receipts **(GDR)** route. Special purpose acquisition companies **(SPAC)** is also an option for start-ups. However, there is no option for direct overseas listing.

5% of the respondents selected overseas listing as a targeted source of funding. Of these, 43% prefer direct overseas listing over indirect overseas listing (detailed in Section III of the report).

There are a few additional sources of funding, including:

- Government support
- Angel investment
- Crowdfunding
- Others

9. India Venture Debt Report, Stride Ventures, 2022, available at: https://s3.ap-south-1.amazonaws.com/www.strideventures.in/Stride+Ventures+India+Debt+Report+2022.pdf

10. Ibid

vi. Government support

Government extends support in the form of grants, tax breaks or other relaxations in taxation to eligible start-ups. These include:

- **Tax exemption under Section 80 IAC of the Income Tax Act:** Start-ups that meet the incorporation (private limited company or LLP), annual turnover (less than INR 100 crores), years of operation (less than 10 years since date of incorporation) and innovation criteria are eligible for recognition by the DPIIT under the Start-up India programme. After getting recognition, start-ups incorporated after 1 April 2016 can apply for a certification to get income tax exemption under Section 80 IAC of the Income Tax Act for three consecutive years out of its first 10 years since incorporation.[11]
- **Relaxation in conditions for setting-off losses:** Normally, change in ownership i.e., voting power of more than 51%, of an unlisted loss-making company would preclude the company from carrying forward its losses. However, in case of eligible start-ups, the restriction on quantum of holding has been relaxed and it shall be sufficient if the shareholders as at the last day of the FY in which loss was incurred and carried forward continue to remain and hold those shares as at the last day of the FY in which such loss is set off.[12]
- **Exemption from angel tax:** Angel tax was introduced in 2012, wherein a 30% tax is levied on start-ups for funds raised through resident investors if the investment exceeded their fair market valuation. In 2019, government issued a notification exempting start-ups registered with DPIIT from paying angel tax, subject to certain conditions.[13]
- **The Start-up India Seed Fund scheme** was launched in 2021 with a target corpus of INR 945 crore, which is to be disbursed over a five-year period to support nearly 3,600 entrepreneurs through 300 incubators. The investment would be made in eligible start-ups to support their proof of concept, prototype development, product trials, market-entry and commercialisation.
- **The Fund of Funds for Start-ups (FFS)**, set-up by the government in 2016, is managed by the Small Industries Development Bank of India **(SIDBI)**. SIDBI has been running FFS operations such as all India funds, regional funds, MSME-risk capital fund, India aspiration funds for start-ups and ASPIRE Fund through which contributions are made to Alternative Investment Funds **(AIFs)** for investment in start-ups through various stages such as seed-stage, Series-A, etc. FFS was formed with an approved corpus of INR 10,000 crore for contribution to Securities and Exchange Board of India **(SEBI)** registered AIFs. As of 31 March 2022, around 72% (7,225.45 crore) of the allocated corpus has been committed by SIDBI for disbursement to AIFs.[14] It has enabled an investment of INR 9,408 crore by AIFs in 582 start-ups.[15]
- The government has initiated a few loan schemes to provide collateral-free debt to aspiring entrepreneurs and help them gain access to low-cost capital. These schemes include Credit Guarantee Fund Trust for Micro and Small Enterprises **(CGTMSE)**,[16] loans by Micro Units Development and Refinance Agency Ltd. **(MUDRA)**[17] and Stand-up India scheme.[18]

> "The government's FFS has had a catalytic effect on the early-stage ecosystem in the country in various ways. It has unlocked much larger pools of monies for start-ups as VC funds need to raise ~80% of the fund size to avail this FFS commitment. Hence, approximately USD 1.5 billion has ensured another USD 7.5 billion. This has also had the effect of creating early-stage investor talent pool. The number of VCs have grown by over five times over the last five to six years."
>
> ***Padmaja Ruparel***
> ***Co-Founder – Indian Angel Network, Founding Partner – Indian Angel Network Fund***

The survey has highlighted concerns regarding the awareness of government schemes and incentives, especially in tier 2/3/4 cities.

11. DPIIT has set up an Inter-Ministerial Board **(IMB)** that validates start-ups or granting tax benefits. The IMB comprises of members from DPIIT, Department of Science & Technology, Department of Bio-technology
12. As per Section 80-IAC of Income Tax Act, 1961, eligible start-up means a company or a LLP engaged in eligible business and fulfilling the following conditions:
(a) incorporated on or after 1 April 1 2016 but before 1 April 2023
(b) total turnover does not exceed INR 100 crore
(c) holds a certificate of eligible business from IMB
13. See GSR Notification No. 34(E) issued by Ministry of Commerce and Industries, available at: https://www.startupindia.gov.in/content/dam/invest-india/Templates/public/notification.pdf
14. SIDBI Fund of Funds, available at: https://www.sidbivcf.in/en/funds/ffs
15. Ibid
16. The committed corpus amount of CGTMSE is INR 7500 crore. 304 Member Lending Institutions have registered for the scheme. Cumulatively as on 31 March 2021, a total of 65,90,413 accounts have been accorded guarantee approvals for an amount of INR 2,60,202 crore. For more information, visit: https://www.cgtmse.in/Home/VS/3
17. Cumulatively as on 31 March 2021, MUDRA scheme has impacted 29.55 crore MSE borrower accounts with credit support of 15.52 lakh crore. Out of this, 68% of the loan accounts belonged to women beneficiaries. For more information, visit: https://www.mudra.org.in/
18. Objective of the Standup India Scheme is to facilitate bank loans between 10 lakh and 1 crore to Scheduled Caste, Scheduled Tribe and women entrepreneurs to set-up a greenfield enterprise. For more information, visit: https://www.standupmitra.in/Home/SUISchemes

vii. Angel investment

- Angel investors typically invest in the initial phase of a start-up, usually in exchange for equity holding in the company. In Q2 2021, approximately 3,528 seed and angel deals were completed, which was over 600 deals less than Q2 2020.[19] In 2020, Indian start-ups secured 341 investment deals with angel investors, a 24% increase from 275 deals in 2019.[20] The average size of angel rounds in India has been around USD 2 million.[21]
- Angel investors are eligible for certain tax incentives on account of investment in start-ups such as, exemption from LTCG on transfer of a residential property (applicable only up to 31 March 2022), if such gains are invested in equity shares of an eligible start-up and the start-up utilises the amount for acquisition of a new asset.

> India has been able to lay the foundation for one of the most innovative start-up ecosystems across the globe with the aim of driving its journey to a high-income nation. Existing capital markets, efficient in capital mobilisation, have provided the required nudge to this competitive growth. Indian start-ups are now ready to take off and are looking forward to the much awaited regulatory space and support."
>
> ***Alok Mittal***
>
> ***Board Member, TiE Delhi-NCR***

viii. Crowdfunding

- It involves raising money from a large number of individuals contributing relatively small amounts. Details about the cause/business plan need to be shared, usually on a platform to attract donors/investors for funding. Crowdfunding can open up opportunities for start-ups, especially those who do not have access to capital through a formal financial institution.
- In India, Section 42 of the Companies Act, 2013 lays down the conditions on private placement of securities by companies. Private placement offers can be made only to such persons whose names are recorded by the company prior to the invitation to subscribe. Companies offering securities through private placement cannot release any public advertisements or utilise any media, marketing or distribution channels or inform the public at large about the offer. A combined reading of the above provisions implies that equity-based crowdfunding is not possible in India. Other forms of crowdfunding such as, donation-based is not regulated by SEBI in India.
- There are other jurisdictions, such as the USA, Singapore and United Kingdom (UK) where equity crowdfunding has been legalised. However, these jurisdictions are also grappling with challenges, such as, the need to secure relevant Intellectual Property (IP) protection to steer away from idea thieves.

ix. Other ways to enable access to capital

There are a few other ways that can indirectly enable greater access to capital for start-ups. Specific recommendations on how these opportunities can be evangelised for the benefit of start-ups are detailed in the recommendations section. These include:

- Incentivising investors through a conducive tax policy
- Creating more market opportunities
- Ensuring that entrepreneurs or start-up founders are adequately aware of the various funding opportunities that are being created by the government in India
- Incentivise investment in Research and Development (R&D) through industry-led innovation clusters

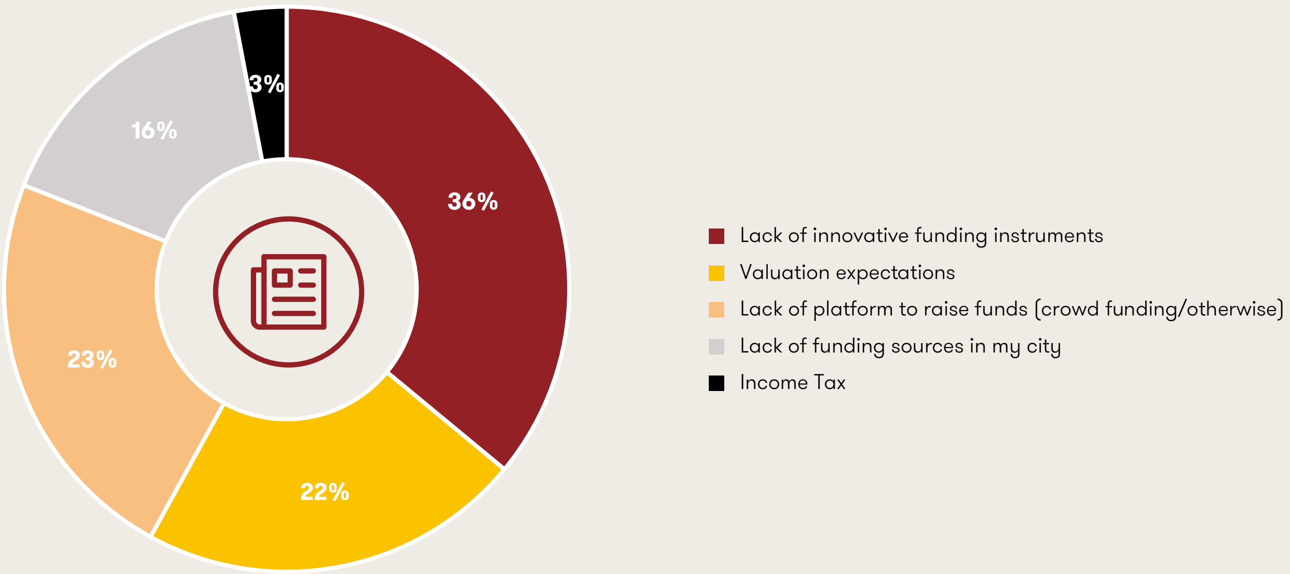
19. Number of seed and angel venture capital deals worldwide from Q4 2016 to Q2 2022, Statista, 2022, available at: https://www.statista.com/statistics/1243973/seed-and-angel-venture-capital-deals-global/.
20. IVCA Private Equity - Venture Capital Report, 2020, available at: https://ivca.in/wp-content/uploads/2021/01/IVCA-PE-VC-Report-2020-Annual.pdf
21. See supra note 3

C. Challenges faced by start-ups and investors in raising funds from domestic markets

Despite a strong and vibrant ecosystem of start-ups in India, the potential for further growth seems to be getting throttled by the challenge faced in raising funds from the domestic market.

As per the survey findings, lack of innovative funding instruments[22] is the biggest hurdle in raising funds for start-ups.

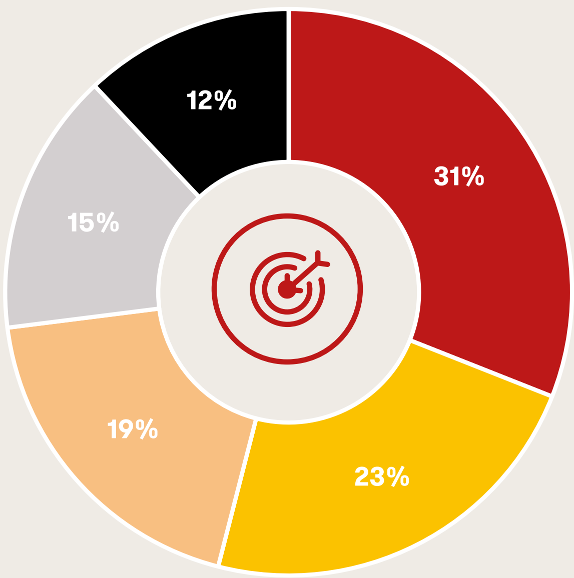
Biggest hurdles for Indian companies in raising funds from domestic markets



It is not just start-ups that struggle to find capital. Investors face their own share of obstacles in adequately supporting start-ups and reaping the benefits from enabling start-ups to achieve their potential. The survey findings show that exchange control limitations on investing in overseas headquartered start-ups is the biggest hurdle for investors in funding Indian origin start-ups. With the recent notification by the Reserve Bank of India (RBI)[23], this limitation of Indian parties investing in overseas headquartered start-ups which have step down subsidiaries or operations in India has been significantly relaxed to permit such structures up to two layers of subsidiaries.

22. We understand 'innovative funding mechanisms' to mean unconventional ways for start-ups to access capital, for example clusters of innovation, acquisition by special purpose acquisition vehicles, listing on international financial services center, etc.
23. Rule 19(3), Foreign Exchange Management (Overseas Investment) Rules, 2022

Biggest hurdles for investors in funding start-ups



- Exchange control limitations on investing in start-ups headquartered overseas
- Capital gains tax exposure on secondary market sale of investments
- Lack of innovative funding instruments
- Restrictions under tax law for claiming write off investments
- Others

"Harmonisation of LTCG tax levied on resident and non-resident investors can be one of the biggest enablers for start-ups in India to access capital. Today, less than 5% of the total capital in India is domestically sourced. This needs to be rectified immediately.

The second biggest enabler can be the formation of multiple Funds of Funds by the government, across sectors and geographies. Given the success of SIDBI's Fund of Funds, more such funds can be a game changer for our start-ups.

The third biggest enabler can be the change in AIF structures to facilitate evergreen funds for long-term capital. This will especially enable investments into deep-tech start-ups that may require a long-term investment."

Sudhir Sethi

Founder & Chairman of Chiratae Ventures India Advisors

Recommendations made by the survey participants focus on enabling more ways of funding support to start-ups, addressing the capital gains tax burden on investments made into start-ups and creating more market opportunities. There are opportunities to be explored beyond the conventional funding options discussed in the previous section. In furtherance of this, we make recommendations for intervention by the government in Chapter IV of this report, to boost the start-up ecosystem in India.

III. The Final milestone for a start-up: Public listing

Listing means the formal admission of securities of a company to the trading platform of a stock exchange. Going public can be a defining moment for a company in its growth journey, strengthening the reputation and offering liquidity to existing shareholders.

Of the respondents that prefer listing, 43% prefer direct overseas listing while the remaining 57% prefer indirect overseas listing. This implies that start-ups are interested in exercising both types of options for overseas listing – direct as well as indirect.

A. Domestic listing

1. Stock exchanges main board

India's two main stock exchanges – the NSE and the BSE, both follow the same trading mechanism, trading hours and settlement process.

2. IGP

The findings on listing show that of 6% respondents who selected domestic listing as a source of funding, 22% of them have considered listing on the IGP.

In 2015, SEBI introduced the Institutional Trading Platform **(ITP)**, a carve-out within the mainboard, with a view to facilitate listing of new age companies in sectors like e-commerce, data analytics, bio-technology and other start-ups and enable access to a wide pool of investors and trading members globally. However, the ITP framework failed to generate interest.

In 2019, SEBI amended the ITP framework and renamed it as the IGP with a more liberal regulatory framework to attract technology-oriented start-ups or companies with early-stage investors, as against listing on the mainboard. However, the market interest in IGP remained tepid.

More recently, in March 2021, SEBI further eased the rules for listing on IGP in order to make the platform more accessible and provide an avenue for start-ups looking to raise series B funding and beyond.

The relaxations include eligible investors having to hold 25% of pre-issue capital for one year (instead of the earlier period of two years), ability to make discretionary allotment up to 60% of the issue size and relaxation in threshold trigger for open offer from 25% to 49%, amongst others.

Who can list on the IGP?

The IGP allows listing of shares pursuant to an IPO as well as for trading on a stock exchange without making a public offer. The IGP is accessible only to institutional investors and certain non-institutional investors.

None of the promoters or directors of the issuer company should have been declared as a fugitive economic offender.

A company is eligible to pursue an IPO on the IGP only if:

- It is extensively engaged in the use of technology, information technology, IP, data analytics, bio-technology or nano-technology to provide products, services or business platforms with substantial value addition.
- At least 25% of the pre-issue capital of the issuer company, for at least a period of two years, should have been held by:
  - Qualified institutional buyers
  - Family trust with net-worth of more than INR 500 crore, as per the last audited financial statements
  - Accredited investors for the purpose of the IGP
  - Certain regulated entities

There are some more specific conditions to be fulfilled with respect to listing via an IPO and without an IPO.

Features	IGP	Main board
Listing	Can be with or without public offering	Needs to be with a public offering
Conditions of listing	No qualitative conditions. However institutional investors must have invested in the past	Qualitative conditions such as net worth, profitability, etc.
Cost and compliance	Not too onerous and reasonable – no minimum subscription requirement, minimum offer size can be as low as INR 10 crore	High costs including annual fee to SEBI, stock exchanges, periodic certifications, audits, immediate disclosures of significant events, corporate governance and related party disclosures, etc.
Who can participate	Only accredited investors	Everyone including retail investors
Delisting	Simpler mechanism	Complex mechanism

The IGP framework has been adopted by the BSE and NSE in the following manner:

a. BSE Small and Medium Enterprise (SME) platform

The BSE had set up the SME platform in 2012 that provides a regulated platform to SMEs to raise funds from the public. Since its inception, the BSE SME has listed 389 companies and helped raise over INR 3,823.96 crore.[24] Out of these, a total of 150 companies have migrated from the BSE SME portal to the main board of the BSE.[25]

b. NSE Emerge

NSE's SME platform, Emerge, constituted in December 2016, offers emerging businesses an option for raising equity capital. Since its inception, 247 companies have listed on the NSE Emerge platform and have raised capital worth INR 3,801.93 crore.[26]

As on August 2022, 239 companies are listed and eligible for trading on the BSE SME platform[27] while 129 companies are listed and eligible for trading on the NSE Emerge platform.[28]

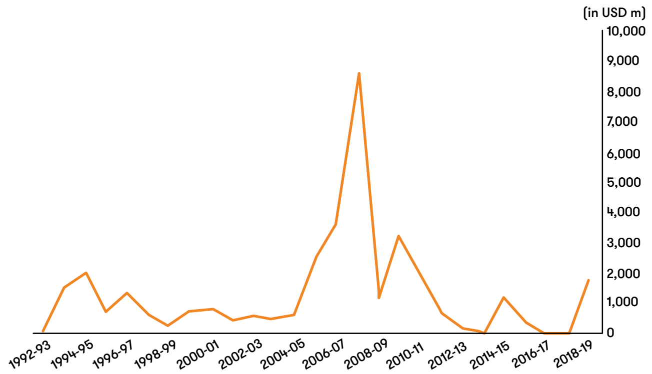
24. Market Statistics, BSE SME Website, available at: https://www.bsesme.com/ (as on August 2022)
25. Ibid
26. Investment Opportunities in Emerging Companies, NSE Emerge, 2022, available at: https://archives.nseindia.com/emerge/sme_brochure.pdf (as on August 2022)
27. Supra note 24
28. Live Market Updates, NSE Emerge, available at: https://www1.nseindia.com/emerge/live_market/dynaContent/live_watch/sme_equities_stock_watch.htm

B. Overseas listing

i. Legal framework for overseas listing

The legal framework in India allows for companies to access the equity capital markets of foreign jurisdictions through the ADR and GDR regime. Companies incorporated in India can list their debt securities on foreign stock exchanges directly through the masala bonds and/or Foreign Currency Convertible Bond **(FCCB)** framework. Companies incorporated outside India can access the Indian capital markets through the Indian Depository Receipts **(IDR)** framework.

Until the early 2000s, many Indian companies, especially those in information technology sector, opted for ADR/GDR routes with an objective to get better valuation for their shares and access to global investors. Thereafter, a steep decline in ADR/ GDR route was observed, due to suspected misuse of GDR instruments for routing black money to India.[29] This is evident from the fact that in 2017, SEBI barred 19 domestic and foreign firms from securities markets in India for manipulation in issuance of GDR and warned several others including Foreign Institutional Investors **(FIIs)**.[30] SEBI also imposed a 10-year ban on some companies whose GDR issuances were manipulated to gain undue advantage.[31] In 2011, only 12 Indian companies raised INR 940 crore through GDRs as compared to 34 companies that raised INR 4,510 crore during the corresponding period in 2010.[32]



Source: The Bank of New York Mellon Corporation – Global Directory of Depositary Receipts

> "India has come a long way in creating a conducive start-up ecosystem and these start-ups have been able to successfully address several domestic as well as global issues. Indian startups, after setting a firm foot in the country, are now poised to expand their brands in the global market leveraging the support from corporates and government organisations."
>
> ***Srikant Sastri***
> ***President***
> ***TiE Delhi NCR***

29. Surajit Ghosal, Repatriation of Black Money — India's Cherished Dream Amidst the Challenges of International Regulations., 3 IJIMS 47, 47-58, 2016, available at: http://ijims.com/uploads/6ba8a20f85f2b579e4ba8.pdf
30. Investigation Report in the Matter of Market Manipulation using GDR Issues, SEBI Report, available at: https://www.sebi.gov.in/sebi_data/commondocs/GDR-Investigation-Annex2_p.pdf
31. Overseas Direct Listing - A Prospective Avenue for Indian Companies, Lex Research Hub Journal, Volume II, Issue II, Apr-Jun 2021, available at: https://journal.lexresearchhub.com/wp-content/uploads/2021/06/vol2-issue-3-008.pdf
32. https://www.indiainfoline.com/article/news/Investors-lost-money-in-85-percent-GDRs-CRISIL-5252679124_1.html

As of June 2022, a total of 64 Indian companies are using the ADR/GDR route to trade their securities overseas – 12 through ADRs, and 52 through the GDR route.

Indian companies listed on global stock exchanges*

Parameters	LSE[33]	LuxSE[34]	NASDAQ[35]	NYSE[36]
Number of Indian companies listed	17	35	4	8
Industry classification	Financial services 17.6%	Financial services 20%	Consumer services 66.66%	Financial services 25%
	Energy 17.6%	Construction and materials 17%	Telecommunication equipment 33.33%	Information technology 25%
	Basic materials 17.6%	Industrial metals and mining 11%		Pharma and biotechnology 12.5%
	Consumer discretionary 11.8%	Consumer goods 6%		Auto manufacturing 12.5%
	Consumer stapes 11.8%	Pharma and biotechnology 6%		Business services 12.5%
	Utilities 11.8%	Others 40%		Business utilities 12.5%
	Technology 5.9%			
	Industrials 5.9%			

*As of June 2022

ii. Direct overseas listing

In June 2018, SEBI constituted a high-level committee comprising members of SEBI, top financial institutions and law firms to analyse the issue of direct listing of equity shares of Indian companies on overseas stock exchanges. The committee analysed the economic considerations for allowing direct listing of Indian companies shares on foreign exchanges and vice versa, while also examining the legal, operational and regulatory implications in facilitating the same. After due deliberations, the committee submitted its report in December 2018 wherein it recommended the government to allow direct listing in permissible jurisdictions outside India.

In March 2020, the Union Cabinet introduced the Companies (Amendment) Bill, 2020 **(the Bill)** to allow direct listing of equity shares of Indian companies on overseas stock exchanges. The Bill received President's assent in September 2020 and proposed amendments to Section 23 of the Companies Act, 2013 to allow direct overseas listing of Indian companies.

Section 23 of Companies Act provides for Public Offer and Private Placement. Sub-sections 3 and 4 were introduced to section 23 of the Companies Act, 2013 as follows:

"(3) Such class of public companies may issue such class of securities for the purposes of listing on permitted stock exchanges in permissible foreign jurisdictions or such other jurisdictions, as may be prescribed.

(4) The Central Government may, by notification, exempt any class or classes of public companies referred to in sub-section (3) from any of the provisions of this Chapter, Chapter IV, section 89, section 90 or section 127 and a copy of every such notification shall, as soon as may be after it is issued, be laid before both Houses of Parliament."

33. London Stock Exchange Issuers List, 31 July 2022, available at: https://www.londonstockexchange.com/reports?tab=issuers
34. Luxembourg Stock Exchange Market Data and Grant Thornton Bharat research
35. Stock Screener, NASDAQ and NYSE, available at: https://www.nasdaq.com/market-activity/stocks/screener
36. Ibid

Advantages of direct overseas listing

Broader investor base

Overseas listing enables a larger pool of international investors, allowing companies to diversify their investor base.

Improved valuations

Indian companies gain access to specialised investor classes who are able to better value securities, thus improving valuations.

Brand visibility

Overseas listing enhances brand awareness in various developed markets such as the USA and Europe.

- **5% of the survey respondents selected overseas listing as a targeted source of funding. Of these, 57% are tier 1 city headquartered start-ups and 86% have been operational for less than 10 years.**
- **Of this 5% pool, 43% of survey respondents prefer direct overseas listing while the remaining 57% prefer indirect overseas listing. This implies that start-ups are interested in exercising both types of options for overseas listing – direct as well as indirect.**
- **The survey respondents that prefer direct overseas listing over indirect overseas listing (i.e., through ADR/GDR) do so for the following reasons: ability and ease to scale business faster, tax advantages, market maturity and better global visibility thus adding to the credibility.**

C. Special Purpose Acquisition Company

- It is a blank cheque company that raises money in an IPO and goes on to acquire an unspecified business through a business combination. Once this business combination is achieved (referred to as de-SPAC transaction), the listed entity functions as a regular listed company.
- SPACs can be a useful vehicle for small companies in India to get access to the capital market. Research shows that in 2021, global IPO SPAC proceeds hit a record high due to low interest rates and abundant liquidity. In 2021, over 59% of the total IPO equity were raised via SPAC route in the US as against 53% in 2020.[37] In 2020 particularly, the number of SPAC IPOs in the US was five times that of 2019, translating into a record of over USD 80 billion funds raised, constituting half of the total IPOs in the US.[38] The US securities market regulator, i.e., Securities Exchange Commission **(SEC)** has in the recent past taken a cautious approach in clearing SPAC listings. This, combined with an overall slowing down of economies worldwide, is leading to a much more cautious approach to SPAC listings with the first half of 2022 witnessing only 70 deals,[39] which is far behind the record run of 613 deals[40] witnessed in 2021.
- SPACs are still an emerging phenomenon for India. In March 2021, SEBI formed a group of experts under its Primary Market Advisory Committee to examine the feasibility of bringing regulations for SPACs in India.[41] Media reports suggest that SEBI plans to build a dedicated framework on SPACs to allow such non-operational entities to raise funds in initial share sales and list in India.[42] At present, SEBI allows listing of only operating companies.

Advantages of a SPAC over a traditional IPO listing

Faster listing process	Can be done in as quickly as in three to four months as against six to nine months for an IPO.
More efficient process	Need to deal with one party as against IPO roadshows to convince multiple investors. There are no or minimal marketing roadshows required for a SPAC listing.
Cost optimisation	SPACs save some cost over a traditional IPO. SPACs underwriting fees and fees at completion (2% and 3.5% respectively) are considerably cheaper than the fees required for an IPO (around 7%).[43] As the SPAC vehicle is already holding onto to funds and is in need to invest the funds raised into an appropriate target, the cost of deploying such funds into the target is lower.
Flexible negotiation	Ability to negotiate stock price and other deal terms as part of the merger agreement and protection from market uncertainty. As the deal is negotiated with one or few parties this flexibility is higher.
SPAC listings are less restrictive	While traditional IPOs have very limited forward-looking guidance, SPACs are generally known for forward looking guidance over a 5-10 year timeline. Therefore, key performance indicators and projected financials are required to give investors the future prospects of the listed business.
Increased valuation	Especially for high growth sectors such as deep tech, renewables and e-commerce

37. A Record Pace for SPACs in 2021, NASDAQ, January 2022, available at: https://www.nasdaq.com/articles/a-record-pace-for-spacs-in-2021

38. Statement on the SPACs Proposal, Commissioner Caroline A. Crenshaw, US Securities and Exchange Commission, March 2022, available at: https://www.sec.gov/news/statement/crenshaw-spac-20220330

39. SPAC Analytics, as of June 2022, available at: https://www.spacanalytics.com/

40. Ibid

41. SEBI Forms Expert Group to Examine Feasibility of SPACs, The Economic Times, 11 March 2021, available at: https://economictimes.indiatimes.com/markets/stocks/news/sebi-forms-expert-group-to-examine-feasibility-of-spacs/articleshow/81449254.cms

42. SEBI plans to build a dedicated framework for SPACs in India, The Economic Times, 15 June 2021, available at: https://economictimes.indiatimes.com/markets/stocks/news/sebi-plans-to-build-a-dedicated-framework-for-spacs-in-india/articleshow/83522696.cms

43. Guide to SPACS, Deal Room Inc, available at: https://dealroom.net/faq/guide-to-spacs

Potential concerns of a regulator for enabling SPAC listings

While regulators of mature capital markets such as the USA would find it less risky to allow SPAC listings and public investment into this high-risk investment, the Indian regulator may have certain reservations around:

Protecting retail investors from the uncertainties of an unknown business and promoter group.	Binding the promoters of the target and the SPAC investment and management teams to key performance indicators and forward-looking statements provided by them while raising funds through SPACs.	Keeping the founders' interest in check: in most SPACs, investors and management teams keep between 10% and 20% of the equity to themselves, diluting the value of the target company. This is a highly one-sided affair that can undermine the retail investors.	SPACs managers and investors are under pressure and incentivised to close acquisitions within an 18-month window. This creates an incentive for them to acquire sub-optimal companies or forces them to acquire target companies at any cost within the time frame.

i. Regulatory hurdles for SPAC transactions in India

SPAC transactions in India are not yet governed by any specialised legislative framework. As a result, a combination of the following laws and regulations makes it challenging to undertake SPAC transactions in India:

- **Companies Act, 2013:** Provisions under the Companies Act, 2013 mandatorily require a company to be formed with a business object. Further, companies are required to file the Memorandum of Association **(MOA)**, which forms the basis of registration of a company. This may not be possible for SPACs since these are shell companies that are yet to identify a target and accomplish a business combination. Further, the Companies Act, 2013 mandates Registrar of Companies **(RoC)** to remove a company's name if it fails to commence business within one year from the date of incorporation. Typically, a SPAC is given 24 months to undertake the business combination which is extendable by a special shareholder resolution. This creates a barrier for SPACs in India.
- **SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018 (ICDR Regulations):** A company is required to fulfil certain eligibility criteria for listing (such as minimum net worth, net tangible assets, average operating profits, etc.).[44] A SPAC is unlikely to meet these criteria at the time of an IPO, due to lack of operating income and net tangible assets.
- **Compliances for cross border mergers:**
  - Companies Act, 2013 requires prior approval from RBI for merger of a foreign entity and Indian entity.
  - Merger with a foreign entity requires compliance with Foreign Exchange Management (Cross Border Merger) Regulations, 2018, which provides that in case of an outbound merger, all properties, assets, liabilities and employees of the Indian company will be transferred to the foreign entity. Shares of the combined entity will be distributed to the shareholders of the Indian target.
  - In accordance with the Liberalised Remittance Scheme **(LRS)**, the fair market value of shares issued to Indian shareholders in the overseas merged entity should not exceed USD 250,000 in every FY.
  - Relevant Foreign Exchange Management Act, 1999 **(FEMA)** regulations need to be complied with in case of a branch or a representative office of the Indian/ foreign amalgamating company becoming the office of a resulting foreign/Indian company.
  - Such outbound merger is not tax neutral (there is no exemption from Indian Income Tax) both at the Indian target shareholder level and at the Indian target level (where its assets are transferred to the SPAC).

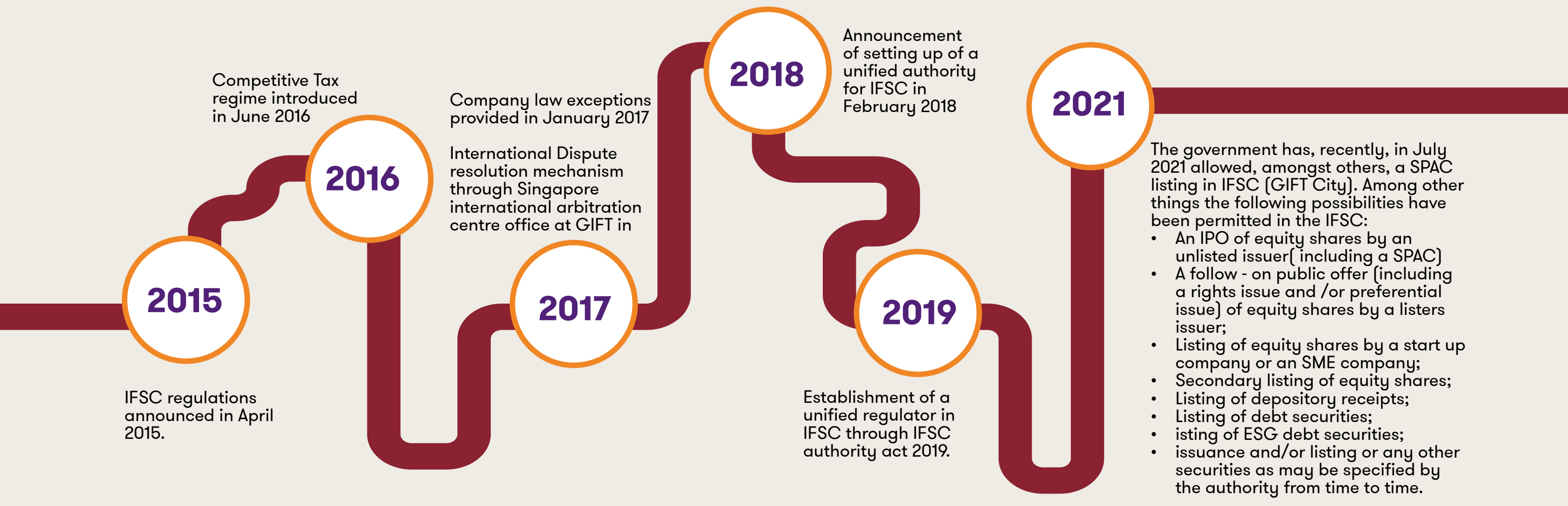
Hence, it will be imperative to examine the above regulations before SPACs can become a reality in India. This would require either introduction of appropriate exceptions to enable SPAC listings or notifying a new framework altogether.

[44] Regulation 6, ICDR Regulations

ii. Emerging SPAC framework in the IFSC

- In April 2015, India's first International Financial Services Centre **(IFSC)** was set-up at GIFT multi-services Special Economic Zone **(SEZ)** in Gujarat. IFSC is a unique financial zone that is treated as an offshore territory under the host country's regulations. IFSC provides financial services (banking, insurance, broking, forex, commodity, etc.) to residents/non-residents, as per the host country regulations.
- The International Financial Services Centres Authority Act, 2019 was enacted in December 2019 to set up a unified regulator, i.e., the International Financial Services Centres Authority **(IFSCA)**.
- The recently notified the IFSCA (Issuance and Listing of Securities) Regulations, 2021 **(IFSC Listing Regulations)** have introduced a listing framework for SPACs on recognised stock exchanges in IFSCs. This allows domestic and international investors to acquire unlisted companies in India and overseas.
- The RBI has clarified that any investment by a resident (corporate or individual) in an IFSC will be treated as overseas direct investment **(ODI)** and all such investment must be made in foreign currency as permitted under the LRS or the ODI windows.[45] This has been reiterated under the recently notified Foreign Exchange Management (Overseas Investment) Rules, 2022 read with the regulations and directions issued by the RBI.[46]
- Restriction on round tripping (ODI-FDI structures) have been significantly relaxed under the recently notified Foreign Exchange Management (Overseas Investment) Rules, 2022 (Rules).[47] These Rules now allow Indian entities and resident individuals to make investments within their respective ODI limits. For resident individuals, a step-down subsidiary outside the IFSC (whether in India or overseas) is also permitted as long as the resident individual does not have control of the IFSC entity, i.e., the SPAC.
- Eligibility criteria for listing of SPACs in IFSC include:
  - Issue size should be more than USD 50 million.
  - Sponsor should hold between 15-20% of the post issue paid up capital of the SPAC.
  - Minimum application size in an IPO of SPAC must be USD 100,000.
  - For the offer to be successful, the minimum subscription should be ≥ 75% of the offer size.
  - SPAC issuer must complete business combination within 36 months from the date of listing.

Key announcements in India related to IFSC



45. Master Circular on Direct Investment by Residents in Joint Venture (JV)/ Wholly Owned Subsidiary (WOS) abroad, 2007, RBI, available at: https://www.rbi.org.in/scripts/BS_ViewMasterCirculars.aspx?Id=3629&Mode=0

46. Foreign Exchange Management (Overseas Investment) Rules, 2022; Foreign Exchange Management (Overseas Investment) Regulations, 2022, available at: https://www.rbi.org.in/scripts/NotificationUser.aspx?Id=12380&Mode=0; Foreign Exchange Management (Overseas Investment) Directions, 2022, available at: https://www.rbi.org.in/scripts/NotificationUser.aspx?Id=12381&Mode=0

47. Foreign Exchange Management (Overseas Investment) Rules, 2022

iii. Listing of start-ups in IFSC

The IFSC Listing Regulations provide the following criteria for start-ups to list on a recognised stock exchange:

- Offer document of the company should be filed within 10 years from the date of incorporation/registration.
- Annual turnover should not have exceeded USD 20 million for any of the FY since incorporation/registration.
- The company should be working towards innovation, development or improvement of products or processes or services, or it is a scalable business model with high potential of employment generation or wealth creation.
- The table below illustrates the permissibility of raising funds through a SPAC in IFSC (GIFT):
  - If the SPAC's sponsor is a resident, then the funds can be raised by the IFSC SPAC from residents/non-residents and these funds can be used to acquire/expand overseas and India. However, it has been clarified under the recent RBI regulations that resident individuals should not control the SPAC.[48]
  - If the sponsor of the IFSC SPAC is a non-resident, then the funds raised can be used to acquire both Indian and overseas entities.

Sponsor	Target	Permissibility
Resident (corporate)	Overseas/Indian entity	Yes
Resident (individual)	Overseas/Indian entity	Yes, subject to condition that such individual is not in control of the SPAC
Non-resident	Indian/Overseas entity	Yes

[48] Para 1(2)(iv), Schedule V, Foreign Exchange Management (Overseas Investment) Rules, 2022

IV. Recommendations

A. Enable access to capital prior to listing stage

i. Harmonising tax rate on LTCG arising from transfer of shares of unlisted companies by resident and non-resident investors

Currently, LTCG arising from sale of unlisted shares is taxed at 20% for resident investors and at 10% for non-resident investors, subject to relief (if any) under the tax treaty. As a result, the tax-policy regime creates an incentive for non-resident investors to invest in start-ups in India. Consequently, more foreign investment is likely to get attracted. While, attracting more foreign investment has its advantages for India, the higher tax rate on investment from resident investors indirectly disincentivises Indian investors from investing into start-ups.

It is important to note that resident investors are more likely to invest in early-stage domestic start-ups because their geographical proximity gives them more confidence to get verifications and background checks done, thereby increasing their confidence to take a higher risk. Without the crucial early-stage investment from resident investors, start-ups will find it more difficult to grow and move to the next stage where they can attract PE/VC funds, foreign investments etc. Therefore, the current tax regime discourages start-ups from seeking domestic investors, as the higher tax incidence for the domestic investor will get factored in the investment deal or the domestic investor may not find the post-tax return on investment attractive enough.

The Union Budget 2022-23 capped a surcharge rate on LTCG arising on transfer of any type of assets to 15% (against the maximum surcharge rate of 37% for individuals, Hindu Undivided Family, association of persons, body of individuals etc. with high income). This will result in a reduction of the Effective Tax Rate **(ETR)** by 4.58% for resident individuals and 2.29% for non-resident individuals. However, this is not enough to bridge the gap and bring harmony in the tax rates applicable to investments by resident versus non-resident investors. The proposed ETR for residents is 23.92% and for non-residents is 11.96%. There is still a difference of approximately 12%.

We recommend that the government should reduce the tax rates on LTCG applicable to resident investors. This will positively impact the Indian start-up ecosystem, by attracting more domestic investments. Ultimately, this will address the impact that the presence of majority foreign investors has on Indian start-ups, i.e., making it conducive from a regulatory perspective for the investee start-up to incorporate in a foreign jurisdiction.

"There is no reason to discriminate between tax charged on capital gains realised by resident and non-resident investors. Given their proximity, resident investors are better placed than non-resident investors to make high-risk investments in early-stage start-ups. A higher rate of taxation discourages them from investing in Indian start-ups. Early-stage investment is crucial for start-ups to grow and be able to attract foreign funds and funds from VC/PEs. Discouraging resident investors by taxing them at a higher rate will disable the start-up right from the beginning and impact the entire lifecycle."

Saurabh Srivastava

Co-founder and Former Chairman NASSCOM

Global best practice

Singapore does not tax capital gains income. The **UK** allows for a 'participation exemption' on capital gains, where if a company holds more than 10% of another group company, then disposal of such shares is not subject to capital gains tax. They also do not distinguish between resident and non-resident investors.

While both countries have corporate income tax rates ranging from 19% (in the UK - being raised to 25% now) and 17% (in Singapore), the incentive of not taxing capital gains (whether resident or non-resident) creates a conducive environment for investments in general. It also creates a level playing field for domestic and foreign investors while giving them confidence that any returns on their investment in the form of capital gains will not be taxed.

ii. Harmonise tax rates on sale of shares of unlisted companies with listed companies

As per Section 112 of the Income Tax Act, 1961, LTCG on sale of equity share of listed companies is chargeable to tax at 10% if the amount of gain exceeds INR 100,000. However, LTCG on sale of shares of unlisted companies is taxed at 20%. Investing in start-ups results in creation of wealth for the country and investors take a significantly higher risk while investing in unlisted companies, such as start-ups with no surety of returns. Imposing a higher tax rate on gains realised by investments in unlisted equity will discourage investments into our start-ups.

Taxation regime applicable to listed securities should be extended to shares issued by DPIIT-recognised start-ups. For this, the government should tax sale of equity shares of unlisted companies and listed companies in the same manner.

Global best practice

Most of the countries that are start-up hubs in the world are following a system harmonious tax rates for transfer of listed and unlisted shares.

S.No	Country	Sale of shares	Harmonious rates
1	USA	There is no distinction between unlisted and listed shares	Taxed as per the ordinary income rate (i.e., corporate tax rate at 21%)
2	UK		Taxed as per the corporate tax rate
3	Japan		Taxed as per the corporate tax rate
4	Australia		Taxed as per the corporate tax rate
5	Greece		Taxed as per the corporate tax rate
6	Argentina	**Sale of unlisted shares** - 15% **Sale of listed shares** - exempt (However, there is no distinction in tax treatment between listed and unlisted shares in case of sale by resident companies)	**Sale of any share:** Corporate tax rate (in case of resident companies) **Sale of unlisted shares:** 15% (in case of foreign companies) **Sale of listed shares:** exempt (in case of foreign companies)

Source: Grant Thornton Research

iii. Creating market opportunities through government procurement reforms

The government can create better market opportunities for Indian start-ups that specifically focus on solving challenges faced by the government and its agencies or departments. There is also tremendous scope for the use of technology in developing and employing solutions for social and governance challenges.

These domestic market opportunities can be created for start-ups by bringing a new approach to the way government procures from start-ups. This can be done by funding innovative start-ups that pass the challenge of addressing the needs of government departments. This will give start-ups an opportunity to innovate through the use of technology to find workable and scalable solutions to government's problems.

Framework and approach for implementation in India

- The model of a grand challenge competition to be used. A minimum number of challenges will be identified per year.
- These challenges will be selected by an expert committee with representatives from government and subject specialists.
- Each year, challenges would be posed to start-ups, where start-ups will compete with the objective of proposing the best solution to the challenges posed.
- Winning solution(s) will be awarded an initial grant, along with follow-on funding and granting of the project by the government for implementation of the solution.
- There can be multiple winning solutions, depending on the scale and nature of the challenge posed.

"Maharashtra start-up week is a one-of-its-kind event designed to provide 24 innovative start-ups with a 15 lakh each paid pilot opportunity with the Government of Maharashtra. In a lot of cases, we have been the first customer to these start-ups. It gives start-ups an entry into relevant government departments and also an opportunity for scale up orders post successful implementation of the pilot projects. The pilots help drive innovation in various government departments and also serve as a strong reference for startups when they pursue business with other state/central government or prospective clients."

Mithun John
Joint CEO
Maharashtra State Innovation Society

Best practice

The Government of Karnataka, the Government of Maharashtra, the Ministry of Defence and the Government of Canada have adopted similar strategies to increase market opportunities for start-ups to solve social challenges through innovation:

- The Government of **Karnataka** implements a Social Innovation Challenge programme to leverage start-ups for finding workable and scalable solutions to the state government's problems. Many challenges have been undertaken and contracts granted to start-ups for deploying the project across four major themes, i.e., water management, healthcare, gender equality and inclusion, and urbanisation. For example, the Karnataka Innovation and Technology Society has implemented Grand Challenge – Karnataka to channelise innovations for social impact.[49] Similarly, the Indian Institute of Science, Bengaluru, conducted competitions to devise sustainable solutions for social problems.[50]
- The Government of **Maharashtra** undertakes the Maharashtra Start-up Week.[51] Start-ups from identified sectors are invited to submit their application, out of which top 100 start-ups are selected to present their solutions to a panel comprising representatives from the government, industry, academia and investors. Thereafter, the top 24 start-ups are selected as winners, who receive work-orders of up to INR 15 lakh from the Maharashtra State Innovation Society to pilot their solutions. The start-ups also receive support in the form of access to government machinery, cloud credits, connect with mentors, investors, etc.
- The Ministry of Defence launched the Innovations for Defence Excellence **(iDEX)** programme in 2018.[52] Under this, the Defence India Start-up Challenge has been launched in partnership with the Atal Innovation Mission, to support start-ups/MSMEs/individual innovators in the area of national defence and security.[53] Under this programme, start-ups/MSMEs/individual innovators are presented with problem statements from relevant government agencies. The received applications are screened by a committee of defence, technology, and innovation deployment experts. Thereafter, winners are granted funds in tranches based on milestones.
- The Government of **Canada** is partnering with Canadian entrepreneurs to develop solutions for challenges posed by the government, through the Innovative Solutions Canada programme.[54] The government sets the problem and parameters for start-ups to solve, outline the desired essential outcomes and funds the development of the innovation by the winning start-up. The funding happens in stages, i.e., if the idea is selected, the innovator receives funding for proof of feasibility; if proof of feasibility is approved, the innovator receives funding for prototype development, etc. Ultimately, if the developed innovation provides effective solution to the problem, the government buys the solution.

"Participating in and winning the iDEX programme has been great for the growth of our company. Since then, we have grown almost 5X and have set-up a factory which is expanding rapidly. The iDEX programme has changed the entire procurement approach of the government in the defence sector. Not only have we benefitted from the grant, but also we have built a strong partnership with the relevant government departments. We are willing and eager to participate in more such government procurement programmes in the form of grand-challenges, to access the market opportunity, as well as leverage our innovation capabilities to develop solutions for the specific needs of the Indian government."

Nikunj Parashar

Founder

Sagar Defence Engineering Private Limited

49 Grand Challenge, Startup Karnataka, available at: https://startup.karnataka.gov.in/grand-challenge-karnataka/

50 Social Innovation Challenge, Centre for Society and Policy, Indian Institute of Science, Bangalore, available at: https://csp.iisc.ac.in/sic2020/

51 About Maharashtra Startup Week, available at: https://msins.in/startup-week

52 Innovations for Defence Excellence (iDEX), available at: https://idex.gov.in/.

53 Defence India Startup Challenges, available at: https://idex.gov.in/challenge-categories.

54 Innovative Solutions Canada, Government of Canada, available at: https://www.ic.gc.ca/eic/site/101.nsf/eng/home.

iv. Ensuring adequate awareness among start-ups on government procurement opportunities being created by the government

The government has attempted to make its public procurement policies start-up friendly by: (a) introducing exemptions for procurement from start-ups from the otherwise stringent selection criteria (such as, prior experience, prior turnover and earnest money deposits); (b) setting an annual target of 25% procurement from MSEs.

While the relaxations in the policy are well received, entrepreneurs do not have adequate visibility on how start-ups have actually benefitted from this, and the extent to which governments are actually procuring from start-ups.

This awareness can be created by regularly publishing procurement data and insights of the government's procurement from start-ups. This would give entrepreneurs the information on how market opportunities are being created by the government in the country for start-ups. This will further give entrepreneurs the confidence to explore and compete for market opportunities in India, thereby attracting more entrepreneurs to incorporate in India.

v. Support creation of industry-specific innovation clusters

Innovation is an important driver for start-ups. Today, cross-industry collaboration is driving innovation. Collaboration between companies from different sectors, think-tanks, academic institutions and start-ups is often necessary to develop innovative products. However, there are no incentives for these entities to come together.

Further, a culture of innovation can be inculcated by making significant investments in R&D, both public and private. However, India's expenditure in R&D is low compared with other competing economies. India spends only 0.6 - 0.7% of Gross Domestic Product **(GDP)** on R&D activities, while countries like the USA, China, Israel and Korea spend between 2.1% and 4.2 %.[55] The government and public sector contribute the lion's share of this, accounting for about 60% of the total R&D expenditure whereas the private sector contributes only around 40%. It is also important to recognise that while industry would invest in R&D projects as required in the market, the high-level of risk involved in funding long-term research, disincentives companies to commit large capital to such R&D initiatives.

To address this, the government should consider adopting a Clusters of Innovation **(CoI)** programme that can encourages companies, think tanks, academic institutions and start-ups to undertake joint R&D projects and co-create innovative technologies. The primary intent of this initiative will be to catalyse innovation in India by enabling collaboration between start-ups, universities, corporates and government agencies that could help building technology leadership. Additionally, this will enhance go-to-market access for start-ups as they would be tied in with large national or multinational corporate giants. Under this programme, the government will incentivise industry-led consortia that intend to undertake joint R&D projects by providing matching grants. A government agency will identify the focus areas and decide on extending funding support.

"Clusters of innovation with their structured approach will significantly increase collaboration between industry, startups, and academia to foster a rich innovation ecosystem. This is a win-win proposition and the key to sustainable innovation. Corporates look to intensify their engagement with start-ups and benefit from their agility and technological focus coupled with their risk-taking ability, which help address portfolio gaps quickly. Start-ups benefit from the potential to direct their technologies into new application areas as well as mentoring from experts in specialised domains, while gaining access to markets with the opportunity to scale, and thereby, access to funding. Academia fuels the ecosystem with their research capabilities and talented young entrepreneurial minds."

Dileep Mangsuli
Executive Director
Siemens Healthineer

55 R&D Expenditure Ecosystem, Economic Advisory Council to the Prime Minister, available at: https://www.psa.gov.in/psa-prod/publication/RD-book-for-WEB.pdf

Framework and approach for implementation in India

1. Identify a nodal agency to implement the CoI programme. The nodal agency will call for applications for development of CoIs in certain predefined areas.
2. Set-up an innovation fund of minimum INR 5,000 crore to make grants to entities with ambitious proposals to develop CoIs and place the fund under the disposal of the nodal agency. The fund size may be increased to INR 20,000 crore in five years.
3. Industry-led consortia, with a minimum of six entities, will be eligible to apply for grants under this programme. Every consortium should mandatorily include at least one private company, MSME, a start-up and an academic/research institution. International organisations would also be permitted to be part of the consortia.
4. Interested consortium to provide a Letter of Intent (LOI) to the nodal agency. The LOI must demonstrate how their proposals will benefit and involve the broader innovation ecosystem to which they belong.
5. The nodal agency, through a committee of external independent experts, will assess the LOIs and invite a detailed plan from the shortlisted consortia.
6. Based on the assessment of the detailed plan, the nodal agency will decide on extending funding support.
7. A final plan is to be agreed between the nodal agency and the consortium. The nodal agency and the consortium can negotiate to arrive at a final plan.
8. Funding provided by the nodal agency is to be matched 1:1 overall by the members of the consortium.
9. Funded entities will use government funding to design, select and carry out projects and initiatives to advance the activities in the final plan.
10. As companies come together to work on projects, they can generate IP assets. The CoI programme would encourage the strategic management of IP through a pre-defined IP strategy in each sector/area. In addition, partners must develop an IP agreement for each collaborative project.
11. Suggested focus areas for India:
    - Mobility, climate and energy: Electric mobility, connected and automated mobility, clean energy and battery and transformation of climate systems
    - Digital healthcare: Transformational digital health systems and personalised medicine
    - Advanced manufacturing: Interoperable digital manufacturing platforms and agile networks and sustainable value networks
    - Communication technology: 5G

Global best practice

The European Union and Canada have adopted similar strategies to promote collaboration between various entities to develop innovative technologies and establish technology leadership.

- **Canada's Innovation Super Cluster Initiative** aims to support business-led innovation superclusters with the greatest potential to energise the economy and become engines of growth[56]. In 2017, it announced a super cluster investment of USD 50 million over five years to accelerate the growth and development of highly innovative industries that would energise the economy and position Canadian firms for global leadership. Through this initiative, Canada aims to create 50,000 jobs and USD 50 billion in GDP. Today, the programme has five verticals: digital technology, protein industries, advanced manufacturing, scale AI and ocean.

- **EU's Horizon Europe programme** aims to promote research and innovation in the EU countries with a budget of €95.5 billion (2021-27)[57]. The programme facilitates collaboration and strengthens the impact of research and innovation in developing, supporting and implementing technologies to boost economic growth and industrial competitiveness.

56. Innovation Superclusters Initiative, Government of Canada, available at: https://www.ic.gc.ca/eic/site/093.nsf/eng/home

57. Horizon Europe, European Commission, available at: https://ec.europa.eu/info/research-and-innovation/funding/funding-opportunities/funding-programmes-and-open-calls/horizon-europe_en

B. Enable access to capital at public listing stage

i. Operationalise direct overseas listing

Although the proposal to allow direct listing of Indian companies' securities in overseas jurisdictions has been approved in September 2020, the implementation framework is yet to be notified. For this, the following regulations need amendments:

a. Foreign Exchange Management Act, 1999, together with regulations, press notes, circulars and notifications thereunder FEMA.

- Listing of an Indian company's equity shares in an overseas stock exchange implies capital account convertibility, i.e.,
  - The instrument will be represented by the currency of the country in which it is listed
  - The stock exchange will permit the instrument to be traded in INR
- For this, Schedule I of the extant Foreign Exchange Management (Non-debt Instruments) Rules, 2019, needs to be amended to allow an Indian company to list shares on an overseas stock exchange and be traded by a non-resident.[58]

b. The Companies Act, 2013, together with the rules, circulars and notifications thereunder:

- The Companies (Amendment) Act, 2020, amended section 23[59] of the Companies Act, 2013, to allow direct overseas listing of Indian companies. The amended section provides that the central government may prescribe the relevant class of public companies, the relevant class of securities, and exempt public companies from any of the provisions of Chapters III[60], IV[61] and sections 89[62], 90[63] or 127[64] of the Companies Act, 2013. However, such notifications have not been published yet.
- It is recommended that the government should notify the relevant class of Indian public companies, the relevant class of securities that may be permitted for direct overseas listing.

c. SEBI regulations

- SEBI should implement the recommendations of the high-level committee[65] for direct overseas listing and notify the overseas stock exchanges over which direct listing of Indian companies would be permitted.

> "One of the primary objectives of setting up the IFSC is to make it an international hub for raising capital from the market. The road is now clear for foreign companies to list on IFSC exchanges. Similarly, domestic companies can also list as soon as the rules are notified by the government, which is expected in the near future."
>
> ***Injeti Srinivas***
> ***Chairman***
> ***International Financial Services Authority (as quoted in Mint on January 12, 2022***

58. Schedule I, Purchase and Sale of Equity Instruments of an Indian company by a Non-Resident, Foreign Exchange Management (Non-debt Instruments) Rules, 2019
59. Section 23, Public Offer and Private Placement, Chapter III, Companies Act, 2013, available at: https://www.mca.gov.in/Ministry/pdf/CompaniesAct2013.pdf
60. Chapter III, Prospectus and Allotment of Securities, Companies Act, 2013, available at: https://www.mca.gov.in/Ministry/pdf/CompaniesAct2013.pdf
61. Chapter IV, Share Capital and Debentures, Companies Act, 2013, available at: https://www.mca.gov.in/Ministry/pdf/CompaniesAct2013.pdf
62. Section 89, Declaration in respect of beneficial interest in any share, Chapter VII, Companies Act, 2013, available at: https://www.mca.gov.in/Ministry/pdf/CompaniesAct2013.pdf
63. Section 90, Investigation of beneficial ownership of shares in certain cases, Chapter VII, Companies Act, 2013, available at: https://www.mca.gov.in/Ministry/pdf/CompaniesAct2013.pdf
64. Section 127, Punishment for failure to distribute dividends, Chapter VIII, Companies Act, 2013, available at: https://www.mca.gov.in/Ministry/pdf/CompaniesAct2013.pdf
65. Report of the Expert Committee for listing of equity shares of companies incorporated in India on Foreign Stock Exchanges and of companies incorporated outside India on Indian Stock Exchange, 4 December 2018, available at: https://www.sebi.gov.in/reports/reports/dec-2018/report-of-the-expert-committee-for-listing-of-equity-shares-of-companies-incorporated-in-india-on-foreign-stock-exchanges-and-of-companies-incorporated-outside-india-on-indian-stock-exchange_41219.html

ii. Permit all Indian companies to issue and list ADR/GDRs in overseas stock exchanges and GIFT – IFSC

a. Currently, the tax and regulatory framework allows only listed Indian companies to use the ADR/GDR route.[66] Both tax and regulatory authorities are clear on the taxation and regulatory implications of ADR/GDR listings, as they are already allowed for listed companies.

b. Between 1993 and 2005, unlisted companies were allowed to list on foreign stock exchanges via ADR/GDR. However, this was changed in 2005, wherein unlisted companies listed on foreign stock exchanges via ADR/GDR were mandated to do a prior or simultaneous listing in India.[67] Thereafter, in 2013, the government once again allowed unlisted companies to list on foreign stock exchanges via ADR/GDR, for a period of two years.[68] However, no clarity was given on what will happen after two years to the Indian unlisted companies who would list on foreign stock exchanges in these two years.

c. We recommend that this amendment should be brought back, allowing Indian unlisted companies to list on foreign stock exchanges without the requirement of a prior or simultaneous listing in India, along with the certainty regarding the requirement to subsequently list on Indian stock exchanges at a later date.

d. We also recommend that necessary safeguards with respect to money laundering, terrorist financing and other related threats to the international financial system should be notified.

iii. Permit issuance of ADR/GDR against a merger of foreign SPAC into Indian target (inbound merger)

a. Currently, the regulatory framework does not allow for issuance of ADR/GDRs as a consideration for cross-border merger.69 This prevents inbound mergers of foreign SPACs with an Indian target.

b. We recommend that the Foreign Exchange Management (Cross Border Merger) Regulations, 2018, be amended to allow issuance of ADR/GDRs as a consideration for cross-border merger. This will open up possibility for Indian companies to use the overseas SPAC listing route for overseas listing. Bilateral recognition of additional jurisdictions that permit such inbound mergers will need to be negotiated by the Ministry of Finance.

66. RBI Circular, RBI/2005-06/156 A.P. (DIR Series), No. 11, 5 September 2005, available at: https://rbidocs.rbi.org.in/rdocs/notification/PDFs/65775.pdf

67. Ibid

68. Amendment to the Issue of Foreign Currency Convertible Bonds and Ordinary shares (Through Depository Receipt Mechanism) Scheme, 1993, RBI/2013-14/363, A.P. (DIR Series), Circular No. 69, 8 November 2013, available at: https://www.rbi.org.in/scripts/NotificationUser.aspx?Id=8558&Mode=0

69. As per Foreign Exchange Management (Cross Border Merger) Regulations, 2018

Annexure

Annexure I: Global best practices for overseas listings

A. USA

The USA has the two largest stock exchanges in the world by market capitalisation, the New York Stock Exchange **(NYSE)** at over USD 20 trillion and the NASDAQ at over USD 10 trillion. The US offers the largest listing platform in the world, with high amounts of monthly trading volumes. US stock exchanges allow companies to list in the following ways:

- **IPOs:** An IPO is the most common way that companies choose to join the public markets in order to raise capital.
- **Direct floor listings:** This type of listing allows companies to list their shares directly and begin trading publicly on the NYSE, without issuing new shares via a traditional IPO.
- **Foreign issuers listing ADRs:** A foreign company that is publicly traded on an international exchange outside the USA can list ADRs on USA stock exchanges without conducting an offering. The stock is tied to the underlying international security and traditionally trades in tandem with that security. Some companies may perceive a higher corporate standing of having its shares listed on two or more exchanges.
- **SPACs:** In 2017, the NYSE tweaked its rules to help attract SPACs, by allowing them to acquire smaller companies, and reduced the initial listing fees it charged them. A SPAC is a company formed for the purpose of raising proceeds through an IPO and using those funds to acquire an operating business.
- SPACS raise money in an IPO, then hunt for a company to merge with or else hand back capital to investors if they fail to find a target within a set period, typically two years. They have accounted for about half the money raised on USA exchanges in 2020, after being just a fraction in previous years.
- **Transfers:** Stocks can be transferred to the NYSE from NASDAQ or vice-versa.

Foreign issuer listing requirements[70]

- In general, foreign issuers that list on the NYSE or NASDAQ follow the same rules and regulations as US companies, but there are certain exceptions for companies that qualify as foreign private issuers.
- There are regulations/compliance procedures which apply specifically to US-based public companies but not foreign issuers.
- Foreign companies are required to abide by the internal control requirements of SOX 404 (internal controls). However, continuous cost reductions with the elimination of excessive testing (materiality) and documentation have decreased the burden on listed companies.
- Regulations surrounding foreign private issuers can be very advantageous, as even some US companies complain about foreign issuers having such loose standards [e.g., using International Financial Reporting Standards **(IFRS)** rather than Generally Accepted Accounting Principles **(GAAP)** or not having to report quarterly]. However, these rules are actively being reviewed to provide a level playing field.

B. UK

- The London Stock Exchange **(LSE)** is one of the most international stock exchanges, with listings from companies from over 60 countries. It serves as Europe's principal source of listed fundraisings and is linked by the way of partnerships to Asia (including a trading link to Shanghai).
- London's significance as a financial market, high trade volumes, access to investor capital and clearing, data and indices capabilities make it an attractive listing destination.
- The LSE enables companies to raise capital and increase their profile. Companies of different sizes can list on the LSE as it runs several markets for listing. It also offers different ways to raise capital.
- For instance, international companies can list several products in London, including shares and debt, offering different and cost-effective ways to raise capital. Additionally, foreign issuers who wish to take advantage of the international market also may choose to pursue listing GDRs, rather than actual shares.[71]

C. Hong Kong

- The Hong Kong Stock Exchange is a leading international stock exchange, which allows full access to foreign investors wishing to trade on its markets and offers a listing venue to foreign companies which can meet its requirements.[72]

70. Initial Listing Guide, 2022, NASDAQ, available at: https://listingcenter.nasdaq.com/assets/initialguide.pdf; International Listings, NYSE, available at: https://www.nyse.com/listings/international-listings
71. A guide to listing on the London Stock Exchange, London Stock Exchange, 2010, available at: https://images.assettype.com/bloombergquint/2019-05/8c394732-baa0-41ba-9730-bb6c193b5be4/guide_to_listing.pdf
72. Listing of Overseas Companies, Hong Kong Stock Exchange, available at: https://www.hkex.com.hk/Listing/Rules-and-Guidance/Listing-of-Overseas-Companies?sc_lang=en

- Key advantages of Hong Kong as a listing destination are its established legal system based on English common law and its regulatory framework on par with other international finance centres, giving investors' confidence in the Hong Kong stock market. It offers many tax advantages, currency convertibility, free transferability of securities and no restrictions on capital flow. The availability of large number of international investment banks, law firms and accountancy firms also facilitate company listings
- Listing of overseas companies in Hong Kong is regulated by the Stock Exchange of Hong Kong Limited **(the HKEX)** and the Securities and Futures Commission **(SFC)**. In September 2013, the HKEX and the SFC issued a Joint Policy Statement **(JPS)** regarding listing of overseas companies.
- The JPS's objective is to assist overseas companies seeking either a primary or secondary listing in Hong Kong. The JPS sets out requirements for overseas companies to be acceptable for listing on the HKEX, including that an overseas company must come from an 'acceptable jurisdiction'.
- The listing rules provide for the listing of companies incorporated in Hong Kong, the People's Republic of China, the Cayman Islands and Bermuda (recognised jurisdictions). The exchange has also accepted companies from 21 other jurisdictions for listing and the list is expected to expand in the future.
- The Hong Kong Exchange has two markets:
  - **The Main Board:** It caters for established companies seeking to raise funds for growth. Applicants need to be able to meet financial thresholds set out in the listing rules which need to satisfy certain requirements.
  - **The Growth Enterprise Market (GEM):** It caters to smaller growth companies and thus has lower entry requirements. Applicants must have positive cashflow generated from operating activities in the ordinary and usual course of business of at least HKD 20 million in aggregate turnover for the two FYs immediately preceding listing and market capitalisation of at least HKD 100 million at listing.
- Hong Kong further attracts companies listed elsewhere and mainly on the NASDAQ by offering secondary listing. HKEX is furthermore extending the use of dual-class stock structures and will allow the listings of a wider array of companies with a dual-class shares structure. The key requirements are that:
  - The standards of shareholder protection in the overseas listing applicant's home jurisdiction must be equivalent to the standards of shareholder protection provided under the Hong Kong law.
  - There must be regulatory co-operation arrangements in place between the statutory securities regulator(s) in the applicant's jurisdiction of incorporation and its place of central management and control and the SFC.
  - The JPS also provides for 'automatic' waivers for applicants seeking a secondary listing on the exchange from many listing rules and corporate governance requirements.

Further, the Hong Kong exchange has recently revised the listing regime for overseas issuers. The new regime came into effect from 1 January 2022. The new regime will result in:

- One common set of core shareholder protection standards will apply to all issuers, providing the same level of protection to all investors
- Greater China Issuers without a Weighted Voting Rights **(WVR)** structure can secondary list: (a) without demonstrating they are an "innovative company" and (b) with a lower minimum market capitalisation at listing than currently required; and
- Grandfathered Greater China Issuers and Non-Greater China Issuers eligible for secondary listing with their existing WVR and/or variable interest entity structures may opt for a dual primary listing.

The Exchange will also publish a guidance letter on change of listing status, to provide guidance for secondary listed issuers, on the Exchange's approach with regards to:

- The migration of the majority of trading in an issuer's securities from an overseas exchange to Hong Kong;
- Voluntary conversion to a dual-primary listing on the Exchange; and
- De-listing from overseas exchanges of primary listing.

Additional key factors to attract overseas listing in HK

- The provision of Stock Connect - an investment channel available to Hong Kong-listed companies that directly links the Shanghai Stock Exchange to the Hong Kong Stock Exchange.

Under this channel, investors in each country can trade on the stock market of the other. This means that eligible investors in mainland China can purchase eligible shares listed on the Hong Kong Stock Exchange via their own local broker, while Hong Kong and international investors will be able to purchase eligible Shanghai-listed shares through their local broker as well.

- The Hong Kong IPO application process is highly transparent, with a full listing guide published on the HKEX website and uniform standards applied to all applicants without exceptions.

- Hong Kong maintains a solid regulatory regime that is consistent with prevailing international practices and allows for the free flow of capital and information.
- Hong Kong has a well-established legal system based on English common law which provides a strong and attractive foundation for companies to raise funds as well as confidence among investors.

Hong Kong's international corporate governance requirements are among the strictest, which results in transparency, accountability, and trust in Hong Kong-listed companies by international investors.

Annexure II: Key features of IFSCs across the globe

A. Dubai

- Founded in 2004, the Dubai International Financial Centre **(DIFC)** has the authority to formulate its own laws for all civil and commercial matters. Its unique legal and regulatory framework is based on the principles of international law and common law.[73]
- DIFC was a part of Dubai's long-term vision to strategically diversify its economic resources and to intensify the capital inclusion in the region. It is a Financial Free Zone **(FEZ)** under the federal law with an independent jurisdiction within the United Arab Emirates **(UAE)**.
- It is tailored to the region's needs by formulating an optimal environment for financial services, related industries, and services to grow.
- The DIFC has established three independent bodies to support the growth and development of businesses at the Centre. These include: the DIFC Authority, the Dubai Financial Services Authority **(DFSA)**, and the DIFC courts and the Dispute Resolution Authority **(DRA)**.
- Entities under the DIFC also receive exemptions from various Dubai laws and regulations, under certain conditions.
- In addition to this, the law of the DIFC on the FEZs in the UAE allowed for the creation of a FEZ as well as in any of the seven emirates of the UAE through a federal decree. It provides exemption to all the FEZs and the financial activities from all federal civil and commercial laws. However, the federal criminal laws are applicable in the FEZs, including the federal laws on anti-money laundering continue to apply.
- During 2019, DIFC introduced series of measures to enhance the regulatory and legal structures that included introduction of new laws related to IP, providing entrepreneurs with full legal protection they need to innovate, new regulations for insolvency, employment, financial collateral, security, and a new framework for prescribed companies.

B. Shanghai

- This Shanghai IFC is aiming to become a first-tier international financial centre. To improve the efficiency of shipping business and promoting foreign investment, the Chinese Central Government announced the approval of China (Shanghai) Pilot Free-Trade Zone **(CSPFTZ)** in September 2013, which aimed to establish Shanghai as a Global Finance Centre.[74]
- CSPFTZ released regulations to foreign investment, finance, and tax. Under its rules:
  - Foreign banks are allowed to directly establish their branches, wholly owned subsidiary, or majority-controlled subsidiary with mainland Chinese business partners in the region within a shorter period timeline.
  - Customs supervision framework was upgraded.
  - Reduced tax rates and incentives were provided besides supporting innovative business models in the CSPFTZ.
- A 'Green Channel' was set up to provide market access in Foreign Trade Zones **(FTZ)** to enhance the administration's efficiency by setting time limits for certain items. The Green Channel is aimed at streamlining the market access for financial institutions by optimising the supervision mechanism, to promote opening and competition among banks and financial institution within the CSPFTZ.

73. Dubai International Financial Centre: The Regions Largest Financial Precinct, available at: https://www.visitdubai.com/en/business-in-dubai/newsroom/news-insights/finance-guide/difc-global-financial-centre; Website of the Dubai International Financial Centre, available at: https://www.difc.ae/

74. Shanghai Free Trade Zone, CzechTrade, available at: https://www.mzv.cz/file/2508780/ShanghaiFreeTradeZone.pdf

C. Singapore

- While Singapore lacks the advantage of Tokyo's large economic base and Hong Kong's proximity to China, it positions itself as a financial centre by providing a world class regulatory environment that responds to the needs of the global markets and institutions, along with most efficient infrastructure for businesses to use as a platform for all of Asia.
- The Monetary Authority of Singapore **(MAS)**, constituted in 1971, has identified four major value propositions that continue to underpin Singapore's success as a financial centre. These include[75] conducive business environment, cost competitiveness, infrastructure and skilled workforce.

Annexure III: Top PE and VC deals in 2021-22

Investor	Investee	Sector	Advisor	% Stake	Investment value in USD m
GIC, the Canada Pension Plan Investment Board, SoftBank Vision Fund 2, Walmart, Qatar Investment Authority, Khazanah Nasional Berhad, DisruptAD, Tencent, Franklin Templeton, Willoughby Capital, Antara Capital, and Tiger Global	Flipkart Online Services Pvt Ltd	e-Commerce	N.A.	N.A.	3,600.00
Three Blackstone affiliate funds	Mphasis Ltd	IT & ITeS	N.A.	55.3%	2,084.49
Bodhi Tree Systems	Viacom18 Media Pvt Ltd	Media and entertainment	N.A.	N.A.	1,776.32
Shell Overseas Investment B.V.	Sprng Energy Private Limited- Solenergi Power Pvt Ltd	Energy and natural resources	N.A.	100.0%	1,550.00
Baring Private Equity Asia	Hinduja Global Solutions (HGS) Ltd- Healthcare business	IT & ITES	N.A.	100.0%	1,200.00
IndInfravit Trust	Brookfield Asset Management- five operational road projects	Infrastructure management	N.A.	100.0%	1,200.00
TPG Rise Climate and ADQ	Tata Passenger Electric Mobility Ltd	Start-up	N.A.	N.A.	1,013.51
Partners Group	Atria Convergence Technologies Ltd	Telecom	N.A.	75.0%	900.00
Falcon Edge, DST Global, D1 Capital, Redbird Capital, Tiger Global, TPG and Footpath Ventures	Dream Sports Inc- Dream11 Fantasy Pvt Ltd	Media and entertainment	N.A.	N.A.	840.00
Canada Pension Plan Investment Board, Ontario Teachers Pension Plan Board, Luxor Capital, Sumeru Ventures, Sofina Group, Baillie Gifford, and others	Ver Se Innovation Pvt Ltd	Media and entertainment	N.A.	N.A.	805.00

Source: Grant Thornton Dealtracker

75. Why Singapore, Monetary Authority of Singapore, available at: https://www.mas.gov.sg/development/why-singapore.

Annexure IV: Top start-up deals in 2021-22

Year	Investor	Investee	Investment value in USD m
2021	TPG Rise Climate and ADQ	Tata Passenger Electric Mobility Ltd	1,013.51
2021	Tiger Global Management, Dragoneer Investment Group, Steadfast Capital, Coatue Management, Insight Partners, Sequoia Growth, Ribbit Capital and Amplo	Resilient Innovations Pvt Ltd - BharatPe	370.00
2021	Octahedron Capital, Moonstone Capital, Lightspeed Venture Partners, DST Global, GGV Capital, Altimeter Capital, and Tencent	Hiveloop Technology Pvt. Ltd - Udaan	280.00
2021	a16z, Coinbase Ventures, Paradigm, Ribbit Capital, Sequoia Capital and Tiger Global	Bitcipher Labs LLP - CoinSwitch Kuber	260.00
2021	General Atlantic, Multiples Private Equity, anada Pension Plan Investment Board, Lightspeed, Intact Ventures and Munich Re Ventures	Acko General Insurance Ltd	255.00
2021	Tiger Global, Falcon Edge, Marshall Wace, Steadfast, DST Global, Insight Partners, Coatue, Sofina, RTP, and Dragoneer	Dreamplug Technologies Pvt Ltd - Cred	251.00
2021	IconiQ Growth, Sequoia Capital, Ribbit Capital, YC Continuity, Tiger Global, Propel Venture Partners, Alkeon, Lone Pine Capital and Steadfast	Billionbrains Garage Ventures Pvt Ltd - Groww	251.00
2021	Falcon Edge Capital, Coatue Management, Insight Venture Partners, DST Global, RTP Global, Tiger Global, Greenoaks Capital, Dragoneer Investment Group, and Sofina	Dreamplug Technologies Pvt Ltd - Cred	215.00
2022	Greenoaks Capital, ICONIQ Strategic Partners, D1 Capital Partners, Steadview Capital Mauritius, Avenir Zetwerk Investors, and Lightspeed Venture Partners, among others	Zetwerk Pvt Ltd	210.00
2021	Faering Capital, Sequoia Capital India, IIFL Alternate Asset Managers and others	Go Digit Infoworks Services Pvt Ltd - Digit Insurance	200.00
2021	Falcon Edge, SoftBank and others	Ola Electric Mobility Pvt Limited	200.00
2022	Tekne Private Ventures, Alpine Opportunity Fund, Edelweiss and others	Ola Electric Mobility Pvt Limited	200.00
2022	Y Combinator Continuity Fund, Kaiser Permanente Ventures, Nexus Venture Partners, Glade Brook Capital Partners and Lachy Groom	KiranaKart Technologies Private Limited - Zepto	200.00

Source: Grant Thornton Dealtracker

About NASSCOM

The National Association of Software and Services Companies (NASSCOM) is the premier trade body and chamber of commerce of the tech industry in India and comprises over 3000-member companies. Our membership spans across the entire spectrum of the industry from start-ups to multinationals and from products to services, Global Capability Centres to Engineering firms. Guided by India's vision to become a leading digital economy globally, NASSCOM focuses on accelerating the pace of transformation of the industry to emerge as the preferred enablers for global digital transformation.

NASSCOM has a vision to scale up the start-up ecosystem in India by 10× and make India a world leader in product start-ups in the next three years. Since 2013, we have impacted over 8500 start-ups and has led over 700 global immersions. We bring together key stakeholders of the ecosystem including start-up incubators, accelerators, angel investors, venture capitalists, start-up support groups, mentors, government, and technology corporations enabling incubation, funding, enterprise connect and support for technology start-ups in India.

For any queries related to this report, kindly reach out to Garima Prakash at **garima@nasscom.in** and Ashish Aggarwal at **asaggarwal@nasscom.in** with a copy to **policy@nasscom.in**.

About TiE Delhi-NCR

TiE is a global not-for-profit organisation dedicated to fostering entrepreneurship through mentoring, networking, education, incubation and funding. Dedicated to the virtuous cycle of wealth creation and giving back to the community, TiE's focus is on generating and nurturing our next generation of entrepreneurs. TiE was founded in 1992 in Silicon Valley by a group of successful entrepreneurs, corporate executives and senior professionals. There are currently 15,000 members, including over 2,500 charter members, spread across a vast network of 58 Chapters in 14 countries.

TiE Delhi-NCR is among the most active chapters across the vast TiE network. In the last 20+ years, it has continuously taken the lead in creating an increasingly positive ecosystem for entrepreneurs and investors. With a strong mentor support base, various events throughout the year covering various aspects of entrepreneurship and multiple opportunities to showcase and network, it has emerged as one of the biggest platforms supporting entrepreneurship. The wide range of programmes include TiEcon, Start-up Expo, India Internet Day, Special Interest Groups across sectors, TiE Institute and TiE Young Entrepreneurs.

About Grant Thornton Bharat

Grant Thornton Bharat is a member of Grant Thornton International Ltd. The firm is at the forefront of helping reshape the values in our profession. We are helping shape various industry ecosystems through our work across Assurance, Tax, Risk, Transactions, Technology and Consulting, and are going beyond to shape a more Vibrant Bharat

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15 offices in 13 locations

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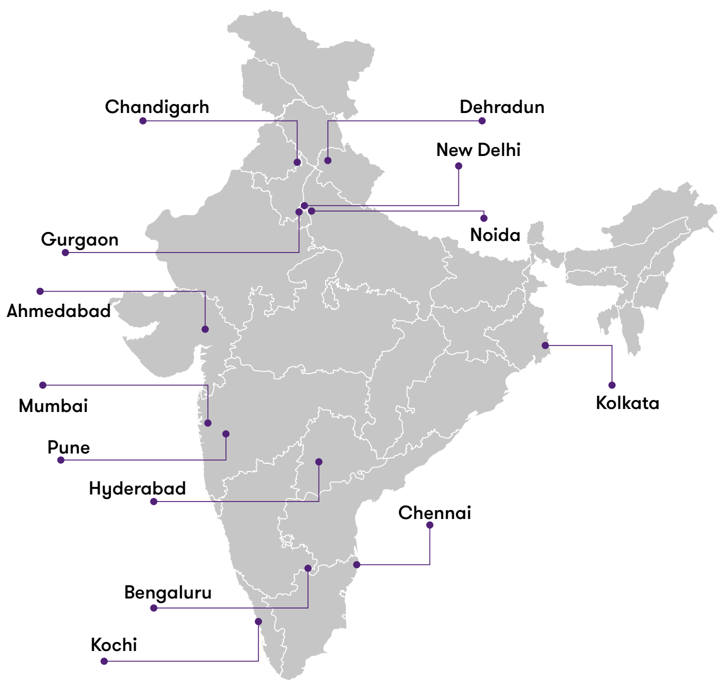

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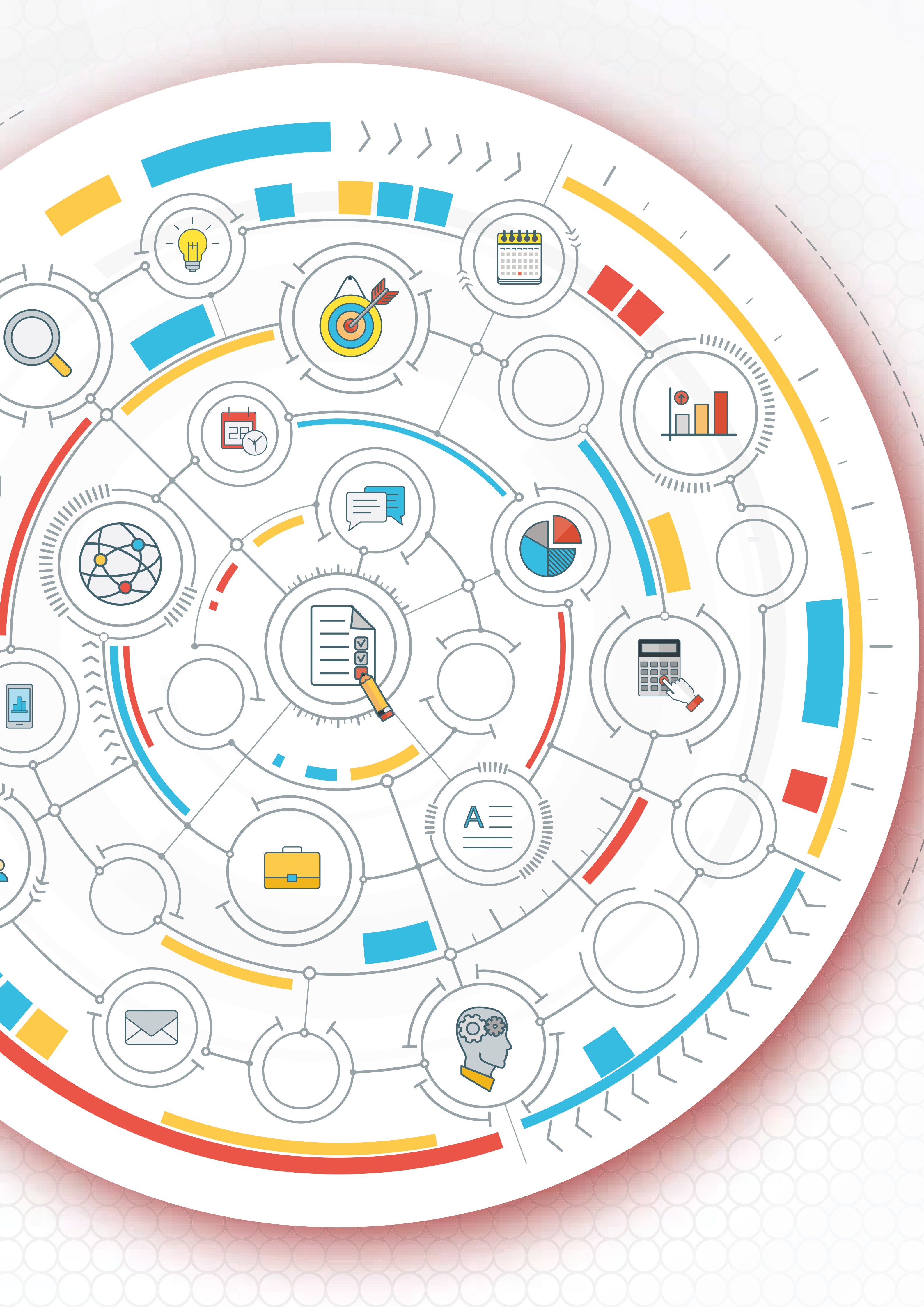

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