

TAX FLASH NEWS

8 August 2019



CBDT clarification with respect to assessment of start-up companies involving application of Section 56(2)(viib)

The Government of India launched the 'Start-up India' initiative on 16 January 2016 to build a strong ecosystem for nurturing innovation and entrepreneurship. Through this measure the government seeks to create large scale job opportunities across the sectors and increase economic growth of the country. As a part of this initiative, the Department of Industrial Policy and Promotion (DIPP)¹ modified the definition of 'startup' and outlined the procedure of application and criteria for a startup to be eligible to apply for tax relief. Further a broad based Inter-Ministerial Board (IMB) was constituted to consider applications of startups for claiming following incentives under the Income-tax Act, 1961 (the Act):

- 100 per cent deduction of the profits and gains from income of start-ups for three out of seven consecutive assessment years under Section 80-IAC of the Act.
- Exemption from levy of income tax on share premium received by eligible start-ups under Section 56 of the Act

On 24 May 2018, the Central Board of Direct Taxes (CBDT) had issued a notification stating that the provisions of Section 56(2)(viib) of the Act shall not apply to consideration received by a company for issue of shares that exceeds the face value of such shares, if the consideration has been received from an investor in accordance with the approval granted by the Inter-Ministerial Board of Certification as per the DIPP notification dated 11 April 2018.

Concerns were raised regarding taxation of angel investments. Accordingly, on 19 February 2019, the

Department for Promotion of Industry and Internal Trade (DPIIT) issued a Notification² stating that provisions of Section 56(2)(viib) of the Income-tax Act, 1961 (the Act) shall not apply to any consideration received by a start-up company, if it fulfills specified conditions under the notification and is recognised by the DPIIT.

Subsequently, CBDT issued a Notification³ stating that the provisions of Section 56(2)(viib) of the Act shall not apply to consideration received by a company for issue of shares that exceeds the face value of such shares, if the said consideration has been received from a person, being a resident, by a company which fulfills the conditions specified under the DPIIT notification, dated 19 February 2019.

However, the AO has been issuing notices under Section 143(2)/147 to start-up companies.

Taking into account the hardship to start-up companies, the Finance Minister in her Budget Speech 2019 mentioned to resolve the 'angel tax' issue. Start-ups and their investors who file requisite declarations and provide information in their income-tax returns will not be subjected to any kind of scrutiny in respect of valuations of share premiums. The issue of establishing identity of the investor and source of his funds will be resolved by putting in place a mechanism of e-verification. With this, funds raised by start-ups will not require any kind of scrutiny from the income tax department. Further special administrative arrangements shall be made by CBDT for pending assessments of start-ups and redressal of their grievances. It will be ensured that no inquiry or verification in such cases can be carried out by the AO without obtaining approval of his supervisory officer.

¹ Notification No. 364(E), dated 11 April 2018

² G.S.R 127 (E) dated 19 February 2019

³ Notification No. 13/2019, dated 5 March 2019

CBDT Circular

Recently, CBDT has issued a Circular⁴ stating that the following procedure for the assessment of start-up companies involving the issue of Section 56(2)(viib) of the Act:

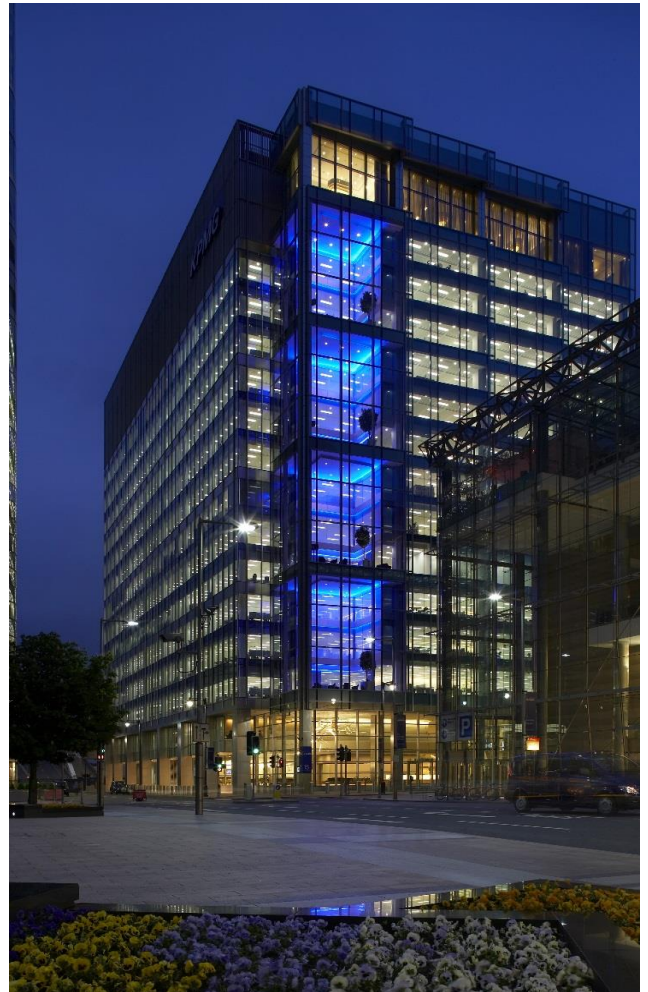
- Where the start-up company has been recognised by the DPIIT but the case is selected under 'limited scrutiny' on the single issue of applicability of Section 56(2)(viib) of the Act, no verification on such issues will be done by the AO during the proceedings under Section 143(3)/147 of the Act. The contention of such recognised start-up companies on this issue will be summarily accepted.
- Where the start-up company has been recognised by the DPIIT but the case is selected under 'limited scrutiny' with multiple issues or under 'complete scrutiny' including the issue under Section 56(2)(viib), the said issue will not be pursued during the assessment proceedings and inquiry or verification with regard to other issues in such cases shall be carried out by the AO, only after obtaining approval of his/her supervisory officer. Due procedure as per the Act shall be followed with regard to other issues for which the case has been selected.
- Where the start-up company has not received DPIIT approval and case is selected for scrutiny, inter alia on the grounds of applicability of Section 56(2)(viib) or any other issue(s), then also inquiry or verification in such cases shall be carried out by the AO, as per the due procedure, only after obtaining approval of his/her supervisory officer.

Our comments

The CBDT circular provides much needed relief to the start-up companies. It states that the prescribed procedure needs to be followed for the assessment of start-up companies involving the issue of Section 56(2)(viib) of the Ac. This clarification would help to boost start-up environment in the country.

The CBDT circular ensures that no inquiry or verification in the cases of start-ups involving issue of Section 56(2)(viib) can be carried out by the AO without obtaining approval of his/her supervisory officer.

The Circular will bring certainty and will help to reduce litigation on angel tax issues which will bring more investment in start-up economy.



⁴ CBDT Circular No. 16/2019, 7 August 2019

home.kpmg/in

Ahmedabad

Commerce House V, 9th Floor,
902, Near Vodafone House,
Corporate Road,
Pralhad Nagar,
Ahmedabad – 380 051.
Tel: +91 79 4040 2200

Bengaluru

Maruthi Info-Tech Centre
11-12/1, Inner Ring Road
Koramangala,
Bengaluru – 560 071.
Tel: +91 80 3980 6000

Chandigarh

SCO 22-23 (1st Floor),
Sector 8C, Madhya Marg,
Chandigarh – 160 009.
Tel: +91 172 664 4000

Chennai

KRM Towers, Ground Floor,
1, 2 & 3 Floor, Harrington Road,
Chetpet, Chennai – 600 031.
Tel: +91 44 3914 5000

Gurugram

Building No.10, 8th Floor,
DLF Cyber City, Phase II,
Gurugram, Haryana – 122 002.
Tel: +91 124 307 4000

Hyderabad

Salarpuria Knowledge City,
6th Floor, Unit 3, Phase III,
Sy No. 83/1, Plot No 2,
Serilingampally Mandal,
Ranga Reddy District,
Hyderabad – 500 081.
Tel: +91 40 6111 6000

Jaipur

Regus Radiant Centre Pvt Ltd.,
Level 6, Jaipur Centre Mall,
B2 By pass Tonk Road,
Jaipur – 302 018.
Tel: +91 141 - 7103224

Kochi

Syama Business Centre,
3rd Floor, NH By Pass Road,
Vytilla, Kochi – 682 019.
Tel: +91 484 302 5600

Kolkata

Unit No. 604,
6th Floor, Tower – 1,
Godrej Waterside,
Sector – V, Salt Lake,
Kolkata – 700 091.
Tel: +91 33 4403 4000

Mumbai

1st Floor, Lodha Excelus,
Apollo Mills,
N. M. Joshi Marg,
Mahalaxmi,
Mumbai – 400 011.
Tel: +91 22 3989 6000

Noida

Unit No. 501, 5th Floor,
Advant Navis Business Park,
Tower-A, Plot# 7, Sector 142,
Expressway Noida,
Gautam Budh Nagar,
Noida – 201 305.
Tel: +91 0120 386 8000

Pune

9th floor, Business Plaza,
Westin Hotel Campus, 36/3-B,
Koregaon Park Annex,
Mundhwa Road, Ghorpadi,
Pune – 411 001.
Tel: +91 20 6747 7000

Vadodara

Ocean Building, 303, 3rd Floor,
Beside Center Square Mall,
Opp. Vadodara Central Mall,
Dr. Vikram Sarabhai Marg,
Vadodara – 390 023.
Tel: +91 265 619 4200

Vijayawada

Door No. 54-15-18E,
Sai Odyssey,
Gurunanak Nagar Road, NH 5,
Opp. Executive Club, Vijayawada,
Krishna District,
Andhra Pradesh – 520 008.
Tel: +91 0866 669 1000

The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavour to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

© 2019 KPMG, an Indian Registered Partnership and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative (“KPMG International”), a Swiss entity. All rights reserved.

The KPMG name and logo are registered trademarks or trademarks of KPMG International.

This document is meant for e-communication only