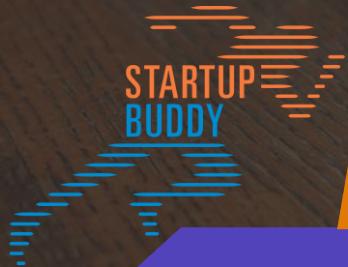




# Innovation Ambassador Training by

## Legal Structures and Ethical Steps in Establishing Startups

23<sup>rd</sup> July, 2021



# How to Start?

Create

Business Plan

Long term as well as short Term

Identify

Key Metrics

For your business

Select  
Correct

Legal  
Structure

For your business



# Various Structure available in India

## Unregistered Structure

Sole Proprietor

Partnership Firm

## Registered Structure

Limited Liability  
Partnership (LLP)

Company  
(Private/ Public Limited)



# Deciding Factors

- ▶ Tax Benefits
- ▶ Team Structure
- ▶ Future Plan
- ▶ Potential Liabilities
- ▶ Residential Status (because of FEMA Rules and Regulations)



# Why to Incorporate?

- ▶ For Branding of Business, incorporation of legal entity is important.
- ▶ To separate out income and expenditure of business from personal
- ▶ For addition of Co-founders
- ▶ Team is key to run business so sharing of Profits with team in the form of ESOP is important aspect
- ▶ For Investment/ Exit, legal entity is must



# When to Incorporate?

- ▶ Purely depending upon business requirements
- ▶ How much funds and which kind of funds will be required
- ▶ Revenue expectation

## ***My Suggestion:***

- ▶ Best is to incorporate just after Proof of Concept

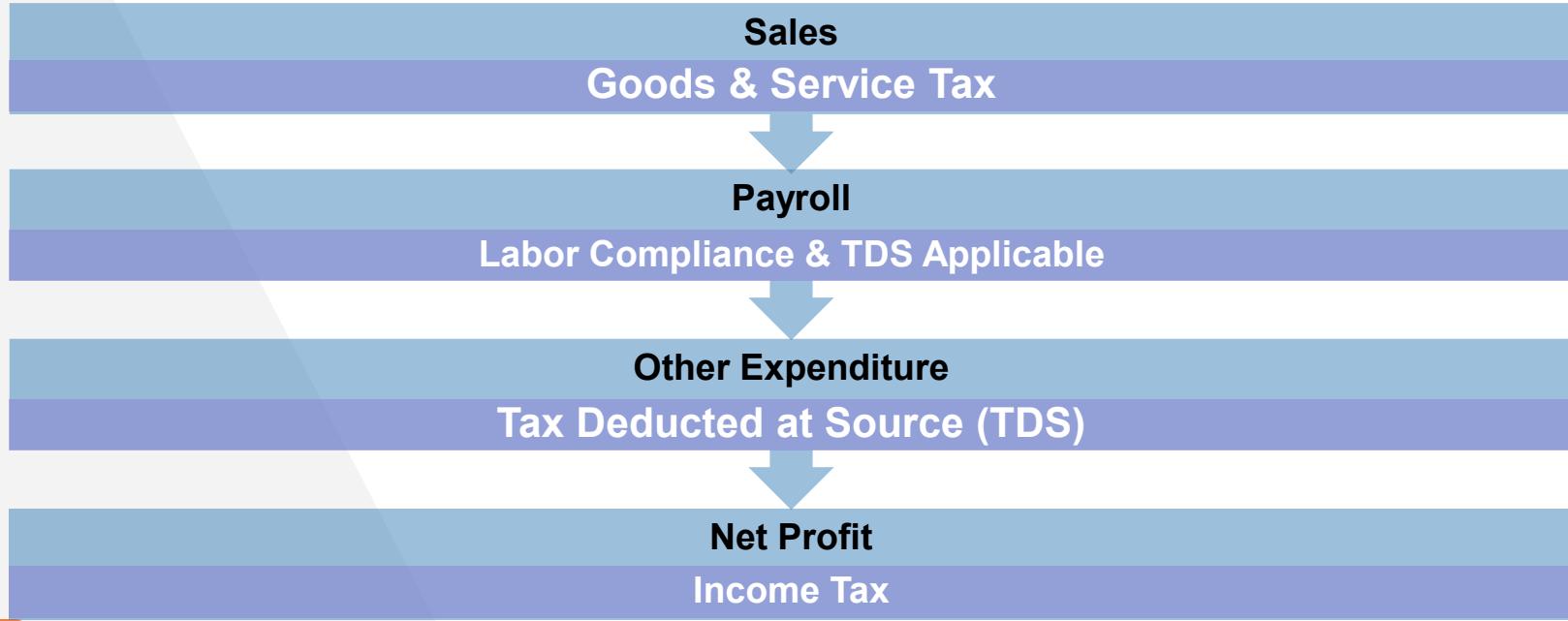


# How to Incorporate?

- ✓ Identify Brand Name & Legal Entity Name
  - This may be same or may be different.
  - Single Entity may have multiple Brands as well
- ✓ Check Trademark for Brand Name and Legal Name
- ✓ Document roles and responsibilities of founding team
- ✓ Select the right Entity according to your business



# Compliances Applicable on Business



# Sole Proprietorship

## Advantage

- Ownership is solely owned by an individual.
- Business owner has a power to control the business operations.
- Owner will receive all the profits and bear all the losses.
- Easy to setup

## Disadvantage

- Owners and business is referred to as one of the same entity (No separation)
  - Unlimited Liability (Not restricted to the capital of the legal entity)
- Can not add another founder in business



# Sole Proprietorship- Compliance

## Compliance Applicable

Separate Income Tax Return	: No
TDS Compliance	: No (Upto Certain Limits)
GST Compliance	: Same rules in all structure (except Reverse Charge)
Payroll Compliance	: Same rules in all structure
Books of Accounts required to Maintain	: No (Presumptive Tax upto Certain limit)
Secretarial Compliance	: No



# Sole Proprietorship- Process

- ▶ Decide the Trade Name
- ▶ Do one Registration like Shop & Establishment, GST, etc.
- ▶ Open a Bank Account
  - ▶ No Separate PAN required
  - ▶ Easiest way to setup & Least compliance



# Partnership Firm

## Advantage

- Two and more individuals share cost and responsibilities
- Terms of partnership recorded in partnership agreement.
- “Silent partner” concept is possible
- Easy to setup

## Disadvantage

- Liable for the action of other partner.
- Unlimited Liability (Not restricted to the capital of the legal entity)
- Benefit of Slab Rate Taxation is not applicable



# Partnership Firm - Compliance

## Compliance Applicable

Separate Income Tax Return	: Yes
TDS Compliance	: No (Upto Certain Limits)
GST Compliance	: Same rules in all structure (except Reverse Charge)
Payroll Compliance	: Same rules in all structure
Books of Accounts required to Maintain	: No (Presumptive Tax upto Certain limit)
Secretarial Compliance	: No

# Partnership Firm- Process

- ▶ Draft a Partnership Deed
- ▶ Print on Stamp Paper to execute by Partners
- ▶ Apply for PAN
- ▶ Open a Bank Account in the name of Partnership Firm



# Limited Liability Partnership (LLP)

## Advantage

- Two and more individuals share cost and responsibilities
- Terms of partnership recorded in partnership agreement.
- Registered with Ministry of Corporate Affairs (MCA)
- Perpetual Succession

## Disadvantage

- Benefit of Slab Rate Taxation is not applicable
  - More legal compliances required than simple partnership Firm
  - Regular and Annual filings with MCA applicable same as body corporate.
- Audit under MCA will be required after some milestone.



# Limited Liability Partnership (LLP) - Compliance

## Compliance Applicable

Separate Income Tax Return	: Yes
TDS Compliance	: Yes
GST Compliance	: Same rules in all structure (except Reverse Charge)
Payroll Compliance	: Same rules in all structure
Books of Accounts required to Maintain	: Yes
Secretarial Compliance	: Yes

# LLP- Process

- ▶ Reserve the name of LLP with Ministry of Corporate Affairs (MCA)
- ▶ Apply for Digital Signatures of Partners
- ▶ Draft a Partnership Deed
- ▶ Print on Stamp Paper to execute by Partners
- ▶ File documents with MCA and wait for Registration Certificate
- ▶ Apply for PAN
- ▶ Open a Bank Account in the name of Partnership Firm



# Private Limited Company

## Advantage

- A Separate legal entity.
- A Company is ruled by its charter documents MOA and AOA.
- Can be as small as one person, or multinational
- Ownership often broken into small units, **SHARES**.
- Those who buy shares – Shareholders
- Since there are many owners, a Board of Directors runs the corporation.
- Shareholders have limited liability, not responsible for debts.
- Get profit as **DIVIDENDS**
- Each share is equivalent to one Vote

## Disadvantage

- Double Taxation on Net Profit if distributed as Dividend.
- Various restriction like taking loan or giving loan from unrelated person is prohibited.
- Regular and Annual filings with MCA applicable
- Audit under MCA will be required from very first day.
- Winding up is not easy.

# Private Limited Company

## Compliance Applicable

Separate Income Tax Return	: Yes
TDS Compliance	: Yes
GST Compliance	: Same rules in all structure (except Reverse Charge)
Payroll Compliance	: Same rules in all structure
Books of Accounts required to Maintain	: Yes
Secretarial Compliance	: Yes



# Type of Shares

## ► Equity Shares

- Called as Common Stocks in some Countries
- Having Voting Power
- No Preference

## ► Preference Shares

- Should be Compulsorily Convertible
- Preference Rights
- Part of Cap Table



# Company Incorporation- Process

- ▶ Check Trade Mark
- ▶ Reserve the name of the Company with Ministry of Corporate Affairs (MCA)
- ▶ Apply for Digital Signatures of all shareholders
- ▶ File the application with MCA including MOA, AOA, ID, Address Proof, etc.
- ▶ MCA will issue the Certification Of Incorporation
- ▶ PAN and TAN will automatically allotted along with Certificate of Incorporation



# Next Few Steps after Incorporation

- ▶ Open Bank Account
- ▶ Transfer Initial Capital as per commitment in Memorandum of Association (MOA)
- ▶ File Business Commencement Certificate with MCA
- ▶ Now the business can be initiated.
- ▶ Directors can bring more funds to the company as Directors Loan

## Next Few Steps (In case of all entity)

- ▶ Apply for Udyam Registration (Also known as MSME Registration)
- ▶ Register the entity with Startup India
- ▶ File Form 2 with startup India for Angel Tax Exemption
  - ▶ Can be filed at the time of fund raise as well
- ▶ In case you expect lots of GST on Vendor's payment, apply GST immediately instead of waiting for threshold limit to claim the input credit.
- ▶ Labour Law Registration, as and when applicable

# Capitalization Table (Example 1)

**Assumption:** Mr. C (Investor) is investing INR 2 Crores for 20% Equity where Mr. A and Mr. B are cofounders:

<b>Name of Shareholder</b>	<b>Current Shareholding</b>		<b>Fresh Issues</b>	<b>Revised Shareholding</b>	
	<b>No. of Shares</b>	<b>%</b>		<b>No. of Shares</b>	<b>%</b>
Mr. A (Founder)	5,000	50.00%		5,000	40.00%
Mr. B (Founder)	5,000	50.00%		5,000	40.00%
Mr. C (Investor)			2,500	2,500	20.00%
<b>Total</b>	<b>10,000</b>	<b>100.00%</b>	<b>2,500</b>	<b>12,500</b>	<b>100.00%</b>

<b>Pre-Money Valuation</b>	<b>Investment Amount</b>	<b>Post Money Valuation</b>
----------------------------	--------------------------	-----------------------------

8,00,00,000	2,00,00,000	10,00,00,000
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Price Per Share

8,000	8,000	8,000
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# Capitalization Table (Example 2)

**Assumption:** Mr. C (Investor) is investing INR 2 Crores for 20% Equity with a condition to keep Provision of 2000 shares for Employees as ESOP

<b>Name of Shareholder</b>	<b>Current Shareholding</b>		<b>Fresh Issues</b>	<b>Revised Shareholding</b>	
	<b>No. of Shares</b>	<b>%</b>		<b>No. of Shares</b>	<b>%</b>
Mr. A (Founder)	5,000	41.67%		5,000	33.33%
Mr. B (Founder)	5,000	41.67%		5,000	33.33%
ESOP Pool	2,000	16.67%		2,000	13.33%
Mr. C (Investor)			3,000	3,000	20.00%
<b>Total</b>	<b>12,000</b>	<b>100.00%</b>	<b>3,000</b>	<b>15,000</b>	<b>100.00%</b>

**Pre-Money Valuation**      **Investment Amount**      **Post Money Valuation**

8,00,00,000

2,00,00,000

10,00,00,000

Price Per Share

6,667

6,667

6,667



# Important Agreements

S. No.	Agreements
1	Founder Agreements
2	Contract with Clients/ Vendors
3	Contract with Employees
4	Non Disclosure Agreements with Employees & Vendors
5	Privacy Policy for website
6	Terms of use for website
7	Software Development Agreement
8	Software Licensing Agreement

# THANKS!

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