

Legal Compliance for Incorporating Startup
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Lecture – 16
How to Capitalize the Business

I welcome you in lecture 16, regarding legal compliance for incorporating startup and I am discussing the module regarding financing and legal compliance. This is our last module in the course and this talk is related to how to capitalize the business.

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Who can access what kind of fund...

Business Form	Accessing to the Founder/Member/Shareholder	Shareholding Share	Private Equity/ Venture Capital fund	Bank & Commercial Financial Institute	Public Financial Institution	Subordinated Debenture/ Bonds/ etc.	Public Investment	Public Market
Proprietorship Firm	✓	✓		✓				
Partnership	✓	✓		✓				
Limited Liability Partnership (LLP)	✓	✓		✓				
Company form	✓	✓		✓				
Society	✓	✓		✓				

Now, I believe you remember the business form which I have discussed with you in the beginning of this particular course. Then I have talked with you how to incorporate it this particular business form. So, some of the business forms are to incorporate and some of them are need to register and we have discussed in detail, while we are talking about these forming of the business form. Now during that particular point of time also, I have also told you that how in generally these particular business forms are finance themselves.

Now, what I did I had put in into a tabular form, that which of the form these particular

business form can access. Now what I will do first, I am going to discuss the upper heading or upper row, where I have mentioned the different name or different form of the fund and then I am going to take you through each of these particular business forms which can access what kind of fund? Now the first column in the first row is talking about the financing by the promoter, members or sponsor; that means, in these circumstances whoever basically either incorporating, registering or promoting these particular business form they themselves bring the fund.

So, in case of the companies you generally talk about the promoter, in case of a society cooperative. So, you generally talk about the members and then in case of the form also we talk about the members. Then when you talk about the sponsor it is basically we indicate trust when the trust has been incorporated for running the business.

Now, please remember when you are talking about that these people can bring the fund they can bring any kind of fund into the business; that means, they can bring the funds which are of a capital in nature or they can even give the credit to this particular business form. Now what are the instruments they are going to use for giving this particular either capital contribution in the capital or they will bring these paid fund or the credit to this particular organization depend on type organization they are basically promoting. So, in case of partnership firm it is basically they bring this kind of money to this particular firm or they can even extend the loan to this particular partnership firm. Similarly in case of the company they can bring the capital fund in form of equity and they can also bring the date fund in form of a bonds and debenture. So, whatever the business form is, they can bring the different kind of instrument for that particular business form.

Now, the second one is the government grants. Now which I have discussed with you other day when I was talking about incorporating the startup, the government basically promotes the different kind of startup because, please do remember startups are generally formed a part of in MSME and government are entrusted to promote this particular MSME for different reason maybe for the local market liquidity or local market supply or even the employment generation or even to promote a particular industry in the form of MSME. So, whatever it mean government generally break gives the grant many of the time and these particular grants are one time grant; that means, you get this particular

grant, but you need not need to pay back to the government.

Like if you are upgrading your machineries, then in that case you might get one time grant. Similarly you might also get the grant in form of equity you might get the grant in form of a credit or you might get a grant in form a credit without interest. So, there are many schemes you will find that runs by the government and these particular funds are available with the different layer of the government. That means, it might be with the local government, it might be with state government or it might be with the central government. So, whatever the government you are basically approaching they have a earmark fund and they also specify that what circumstances they will release this particular fund. So, you might access this particular fund too.

Now, there is a private equity and the venture capital and in my subsequent lecture I am going to deal with it in detail, but let me tell you these people also make an investment in highways and high growth oriented venture. Now in generally these particular ventures are look for more a formal business form because, then in that case it is easy for them to fund as well as there is a kind of regulatory prescriptions are there for these particular organization to whom they can fund and how much they can fund and in what form they can fund. So, that is the reason you will find they generally do not go for the informal sector, but they generally go for a formal business form. So, there is only in case of the company which I am going to talk with you are this particular funds available.

Now, next category is a bank and specialized financial institutions. Now you will find the government is (Refer Time: 07:06) different commercial banks as well as different scheduled banks, different industrial banks which I am going to discuss with you later or even the different specialized financial institutions which are created for a particular sector itself to facilitate the startup or to create a startup fund or create MSME fund, that these particular organization can grow.

Now please remember while they are creating this kind of fund, they are creating it a lot of ease in accessing this particular fund. Previously it was very difficult to get a credit for the purpose of the startup or MSMEs. But nowadays you will find the bank has created a dedicated branch and they have a certain kind of a prescription which you have met those

particular prescriptions you might quickly access this particular fund.

Now, bank also given lot of mandate that in which form they can make an investment in this particular business; either in form of a equity or in form of a debt. So, whatever the prescription is they need to make that particular investment. But at the same time these particular the granting of the loan is not always a standardized, but it can be also customized. So, there can be negotiation done between this particular startup as well as the bank. In some cases if they found that well this particular startup has a potential to go up or grow then in that case there can be some kind of a leniency provided by this particular bank while they are lending the money.

Now, the next one is a public financial institution. Now public financial institution is basically earmarked some of the institution as a public financial institution. It is earmarked because these particular people are been asked to raise the fund for the industry or specific segment of the industry and then to facilitate this particular industry or funds particular industry. Now if you have seen the companies act 1946, then in that case you will find there was a specific provision which was I think 4A which defines the public financial institution, but now under the present act is companies act 2013 this particularly public financial definition has a institution definition has been taken away, nevertheless the public financial institutions are designated where they can make an investment and which are the instrument they can make an investment and which are the organization they can make an investment.

So, this is another source where you wanted to address your growth, but please do remember these particular public financial institutions are generally not financed at the beginning of the startup. So, they basically come maybe where there is growth is already started or somehow there is a prospect or in a you have already build up your balance sheet at that particular point of time this public financial institution come at finance.

Now, there is a institution investors and you have seen that I have put it as a domestic as well as foreign. Now institutional investors which I am going to talk a little later more in detail are those people who are basically manage the different kind of fund. Like it might be the insurance fund, it might be the mutual's, it might be the pension or it might be

some other kind of a of fund which is created for a specific purposes; that means, to put it in other way round these particular institutions are basically borrow the money from the people or they basically issue the different kind of financial instrument or financial product to who the people and then they whatever the money they raise out of that they basically make an investment in a different portfolio. So, one of the portfolio might be portfolio relating to the growth fund of maybe the startup.

But please remember these particular financial institutions again do not make an investment, if you are at the beginning of the startup. They do make an investment once you make you balance sheet and reputation in the market regarding a startup. So, these financial institutions are domestic as well as foreign in nature. If you wanted to access the foreign financial institution relating to your startup there is a lot of regulation you will be subjected to it is prescribed by the RBI as well as the SEBI and you need to follow these particular regulation for accessing this particular type of fund.

Now, the next one is a private placement and I believe I have to refer with you over this particular over private placement before when I was talking with you in the different context. Now private placements are those situations wherein, you can raise the money by issuing the different kind of security from the defined group of people. Now at present you will find the private placement is defined under the companies' act 2013 and therein they said that private placement means it is a closed group of people. Now this closed group of people may be your own client age or maybe your prime clients or maybe your own consumer or the customer whatever it may even it is basically addressing not a public, but a closed group of people. There is some kind of organization only allowed to issue the instrument through this particular private placement. So, at present you will find it can be done by the private limited company as well as the public limited company both listed as well as unlisted.

Now, the last one is the primary market. Primary market means where you can issue the different kind of instrument. Now that particular instrument will be it maybe of capital nature, that instrument might be of a debt nature and I am going to drill this particular thing in detail later on when I am going to talk with you relating to type of instrument you can use for raising this particular fund.

This is quite stringent process because the moment you want to access the primary market, you are subjected to lot of regulations and these particular regulation generally come from the capital market and if you are a capital market regulatory and you need to follow all those particular regulation which has been prescribed by the capital market regulator. Please do remember these accessing the primary market generally happen in much later stage of a startup, like when you have possibly build up your results, you have possibly build up your capital, you have done your business very nicely and you wanted to expand further, at that particular point of time you generally go for the primary market either in form of a initial public offer or in form of a follow a particular offer.

Now, let us look into the table. Now if you look into this left hand side then you will find I have talked about the business form. If you look into the proprietorship, proprietorship basically have a limitation to accessing the fund and they can only access the fund from its own member; that means the promoter or the government grants or maybe the bank and specialized financial institutions. Generally it is only the banks not even the specialized financial institutions.

Now next one is a Partnership. Partnerships also have a similar capacity. It cannot go for any other form of raising the fund. It is the limited liability partnership again they have a similar kind of capacity if you go for the co-operatives you will again find that they have a similar kind of a capacity as well as a society are also the similar kind of capacity; that means, in all this particular five business form you can only either raise the capital from its own member or the promoter or the sponsor or you can go to the government for the different grants which I have explained to you or you can go the public bank or public financial institutions to raise this particular money.

Now, when you are raising the money from the government, these are basically back buttered agreement; that means, you enter into a contract with the government and you promise that in which point of time, if it is not informed of a onetime grant after what time you are going to pay back the particular money? Or is there any clause relating to the rescheduling of those particular loans, or the investment or if the government is investing in your equity or the capital; then in that case how the government will exit after some point of time. So, all this thing has to be included within the bipartite contract

which your all agreement which you are going to enter with the government.

Now, in case of the bank, again it is governed by the bipartite agreement or the loan agreement or investment agreement. Whatever it is and there you detail out what kind of financial returns you required to keep either in form of a dividend or in form of interest. Many of the time you will find that dividend payment is depend on the company's performance. If the company performs then only you make a payment, but if it has come as a credit, then you need to pay a fixed rate of interest or you might have a provision relating to rescheduling of the interest whenever it is required to do that.

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Business Form	Company Equity (Private/Shareholder)	Government Grant	Private Equity/Venture Capital/Fund	Bank & Financial Institution	Public Financial Institution	Investment Institution (Venture Capital/Fund)	Private Placement	Primary Market
One person Company	✓	✓		✓				
Private Limited Company	✓	✓	✓	✓			✓	
Public Limited Company	✓	✓	✓	✓	✓	✓	✓	✓
Public Limited Listed Company	✓	✓	✓	✓	✓	✓	✓	✓
Fund	✓	✓		✓				

Now, in case of the one person company we will find it is almost same as the last business form we have discussed because, if you remember initially I have told that these are basically for a very tiny business setup, business organization and that is the reason they have also restriction relating to accessing the different fund. So, in case of the one person company also they it is corporatized, but it is more like a proprietorship. That is the reason you will find there is a restriction for this particular company to go and raise the fund.

Now if you look into the list of a private limited company and then you will find that

number is increasing now, but which of the fund they can access. In this particular list you will find they can raise the fund from their own promoter or the members they can raise it from the government, they can go to the private equity or a venture capital they can go to the bank or specialized financial institution and they can go for a private placement. So, number of option in case of a private limited company is more than other form of a business organization.

And I have explained to you all those particular thing. Now the public limited company you will find it is even larger than a private limited company. They can even go for accessing the international institutional investment either domestic or the foreign. So, even they can go for issuing a depository receipt which I am going to talk with you little later; that means, they can go to overseas market to raise the fund right? but I think now there is some kind of restriction has been provided possibly you need to have a domestic listing before you go for this ADR in the other country. Otherwise these people even can go to the institutional fund to rise for them.

Now, the most efficient organization for raising the fund is the public listed company. You will find I have ticked all the columns. They can and raise any kind of fund which is suitable for them. Please remember people always think that which fund is a cheaper, which fund is easy to access and which fund can be return quickly. So, this is also one of the considerations which you need to make while you are growing in your startup.

Even if as this particular company has flexibility for accessing the different types of a fund they are also subjected to the high compliance. This particular compliance might come from a multi regulator in the market where they are operating. Either it might it might come from a capital market regulator like SEBI or may be money market regulator or it might come from any other sector regulators. For that matter even these particular people who can go and access even a different government security also government fund also. So, this at these particular public listed companies is a more efficient form of a business to access the fund.

Now, the last one is a trust. In case of the trust you will find that they have also limitation as other form of the organization because, in case of the trust it is a sponsor who create

the corpus and that particular corpus is actually administered for benefit of the beneficiaries. So, in case of a trust is basically again benefiting those people who are becoming the beneficiaries or becoming the member of that particular (Refer Time: 21:52). So, they have also limited capacity, but you will find in some of the sector if you wanted to operate then government prescribe that, you should form it as a trust. So, that it is not a profit making business organization, but it is acting for a benefit of that particular sector or for those people who are going to be in touch with that particular sector itself.

So, these are the all matter relating to who can access what kind of a fund and in the subsequent lectures I am going to discuss with you that in detail relating to the venture capital relating to the public financial institutions and how to access the primary market.

Thank you.