Timely review

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The very idea of an 'angel tax' on start-ups must be reconsidered

- Start-ups troubled by the so-called angel tax may soon receive some concession from the government.
- The Centre set up a five-member working committee to look into revising the norms of the angel tax imposed on start-ups.
- The tax, which was first introduced in 2012 to curb money-laundering through the sale of shares of private unlisted companies at bloated prices, has caused a lot of anguish among start-up investors in the country.
- Start-up owners have complained that income tax officials have asked many start-ups to cough up money when they try to attract capital into their entities by issuing new shares.
- For its part, the IT department fears that start-ups may be used as convenient tools to launder illegally acquired money, so a tax on investments beyond a certain threshold is necessary to deter such shady operations.
- But while the intent of such an angel tax may be justifiable, the arbitrary nature of it means the cost of unintended consequences could be larger than the supposed benefits.
- In trying to curb money-laundering, Section 56(2)(viib) of the Indian Income Tax Act, 1961 gives income tax officials a free hand to harass even genuine start-ups looking to raise investments for their growth.
- The committee set up by the government will, among other things, consider raising the threshold beyond which new investments into start-ups will be taxed.
- This would definitely make life easier to a certain extent for angel investors and start-ups.
- But it will not address the real problem with the angel tax, which has to do with the unbridled power that it vests in the hands of the income tax authorities.
- Otherwise it risks killing the nascent start-up ecosystem in the country.