Treelife

THE START UP GUIDE

“Startups are engines of exponential growth, manifesting the power of innovation. Several big companies today are startups of yesterday. They were born with a spirit of enterprise and adventure kept alive due to the hard work and perseverance and today have become shining beacons of innovation.” - **Startup India.**

Today, India is a thriving consumer-driven market with scope for exponential growth. Entrepreneurs are tapping this opportunity through sustainable and customer-centric business models and redefining the dynamics of business through the use of technology.

India is the third largest startup ecosystem in the world with approx. 83,655 government recognized startups across 656 districts. With 107 unicorns, India minted 23 unicorns in 2022 itself. By 2025, the country is expected to have 250 unicorns

While India makes a mark on the VUCA map, your startup is your personal opportunity to create an impact in the world.

LIFECYCLE OF A STARTUP

1

PRE - INCORPORATION

It all starts with an IDEA!

The first step towards starting up is to validate your idea, through family, friends and most importantly, your target customers. Use smoke tests, conduct a survey, assess yourself.

Once your idea is validated, go to the next step of giving your business a formal identity.

HOW TO CHOOSE THE RIGHT TYPE OF ENTITY

The first question that arises is what type of entity is the best fit for your business.

Your choice of the type of legal structure for your business should be based on your short-term and long-term business goals.

It is one of the most important choices at the start of your business as it determines the personal liability you face, your ability to raise capital, the tax you will pay and the amount of paperwork coming your.

Type of Entity	What Works When?
Sole Proprietorship	Advisable at the **Idea Validation Stage** where the business idea may be tested without incurring a significant expense and with fewer formalities.
Partnership Firm	Advisable when the partners are closely associated (e.g.: Family Members) and the business does not require raising of external capital.
Limited Liability Partnership (LLP)	Advisable when the partners are professionally associated, and the business does not require raising of external capital
Private Limited Company	Advisable for a business that requires raising funds from external sources as it enables the investor to hold a stake in the business.
One Person Company	Advisable when the sole owner wants to manage the Company affairs in an exclusive manner with the enjoyment of the benefits available to the Private Limited Company (but not ideal for fundraising)

“Our only advice to all entrepreneurs is to *START!*”

2

LAUNCH OF BUSINESS

Once incorporated, your business may immediately need contractual relationships, IPR protection and mandatory licenses to launch business operations.

These activities help the founders to focus on core business competencies and eliminate the possibility of regulatory or compliance related hassles.

CONTRACTUAL RELATIONSHIPS

Contractual relationships are very important from a business point of view, to formalize on clear terms and translate the understanding of a business transaction or an arrangement, into an enforceable agreement that sets out and protects the rights of the parties. Startups typically require the following contractual relationships:

1. Co-founders Agreement

A Co-founders Agreement is a formal arrangement inter se the promoters or founders of a company, which sets forth the equity distribution, IPR ownership, initial investments, roles & responsibilities, and/or designation of each promoter/ founder, amongst other things.

2. Term Sheet

A Term Sheet works as an initial offer of investment in a company. It describes the terms on which the Investor will invest in the company, Generally, term sheets are of a non-binding nature (other than a few substantial clauses). However, where the term sheet relates to a settled position, the parties may enter into a binding term sheet.

3. Shareholder's Agreement (SHA)

An agreement amongst shareholders of a company, segregates the ownership and management of the company. It also stipulates the rights and obligations of the shareholders and board of directors including detailed terms.

4. Share Subscription Agreement (SSA)

This sets out the terms of the actual investment, including the amount, the number of shares, the procedure for investment, resolutions to be passed and corporate filings to be made, any post-closing conditions, warranties by the company, promoters/founders, and indemnities.

5. Share Subscription and Shareholder's Agreement (SSHA)

In the case of an early-stage or relatively fewer complex deals, parties may opt to combine the SSA and SHA into a share subscription and shareholders' agreement (SSHA).

6. Share Purchase Agreement (SPA)
In case of a transfer of shares between existing shareholders or to a third party, the parties will enter into a share purchase agreement setting out the amounts and shares to be transferred to the respective buyer and seller

7. Non-Disclosure Agreement (NDA)
Non-Disclosure Agreement safeguards the confidential information of the parties that generally predates the definitive agreements between the parties.

8. Employment Agreement
An agreement to regulate the employer-employee relationship.

9. Vendor Agreement

10. Master Service Agreement
A Service Agreement is a document between the service provider and a customer enumerating the nuances of how the service will be provided and the terms and obligations of the service provider.

11. SAAS Agreement (Subscription Agreement)
SAAS Agreement stands for “Software-As-A-Service” Agreement, it is a type of Subscription Agreement used to determine the terms on which access to the software subscription is provided to a customer, including the term, fees, scope of work, warranties, etc.

12. Terms & Conditions
Terms & Conditions defines the relationship between the service provider (usually, an app or website) and an end user or website visitor and is typically used on online social media sites, e-commerce platforms, and other online business websites.

13. Privacy Policy
A privacy policy is a mandatory requirement under law which outlines how the user data is collected by the business from a user, and how it may be utilized, transferred, processed, and retained by the business as a data collector. It is important to align the privacy policy to the business’ internal policies and applicable laws.

VITAL TERMS IN TERM SHEET

ROFO/ROFR

- ROFO is the offeree's right to first purchase the sale shares at a price point derived from internal negotiations.

- ROFR is the offeree's right to first purchase the sale share at a price point derived from the current market valuation.

Liquidation Preference

- This defines the seniority of the payout order in which the Investors claim their return from the Company on the occurrence of a liquidation event.

Liquidation Preference

- This protects the Investor shareholding % in the event that the Company issues shares at a price below the price per share (Down Round) subscribed by the Investor.

Tag-Along

- Right of minority shareholder to sell shares along with the majority shareholder. Usually on pro-rata basis.

Drag-Along

- Right of the Investor to force the Founders to sell their shares in order to provide the Investor with an exit. Usually triggers on the occurrence of an Event of Default.

INTELLECTUAL - PROPERTY RIGHTS

	Trademark	Copyright	Patent
Nature of right	Protects symbolic expression	Protects creative expression	Protects functional expression
Type of protection	A visual symbol which may be a word, signature, name, device, logo, brand name, tag-line, icon, label, numeral or particular combination of colors used by one undertaking to sell or market its goods or services or other articles of commerce distinguishing a business or brand from another.	Any type of tangible original literary, dramatic, musical and artistic works and cinematograph films and sound recordings from unauthorized uses.	Any type of invention which has industry application and commercial viability.
Ideal time of application for protection	Advisable to apply just before or as soon as business operations under the brand name have started.	Acquisition of copyright is automatic upon development of the work and it does not require any registration or formality. However, registration is recommended to prove valid ownership and prior development in case of infringement.	The application for a patent should be filed before the publication of the invention and till registration is not received, the invention should not be disclosed or published. Application for provisional specification also can be submitted in development stages of invention, and a twelve months window is given to finalize the same.
Duration of Protection	Trademark protection is valid for 10 years from the registration of the mark initially, and can be renewed further after every 10 years.	Tangible original Literary or musical or dramatic or artistic works, cinematograph films and sound recordings are granted copyright protection for a period which extends through the lifetime of the author and up to 60 years after his/her death.	Patent protection is granted for a total period of 20 years from date of application of the patent. A renewal fee is payable for 3rd year onwards. However, after the lapse of 20 years, the subject matter of the patent is not entitled for any further protection.
Examples	Symbols, Logos, Names, creative representation of a word	Source Codes, Music compositions, Books, photographs, software code, films, paintings, etc.	Innovative Technology, New Products

LICENSES/REGISTRATIONS

When you start your business operations, you have to apply for a few licenses/ registrations, depending upon the applicable central/ state laws and the nature/ size of your business.

Few of them are listed below:

1. PAN (Permanent Account Number) For Income Tax purposes

2. TAN (Tax Account Number) For TDS purposes

3. Start-up India Registration
An optional registration that enables the business to enjoy conditional tax benefits and share relaxation to a few tedious secretarial and compliance norms.

4. Shops & Establishment License
A mandatory registration is required irrespective of the place or kind of business carried out.

5. Ministry of Micro, Small, and Medium Enterprises registration (MSME)
An optional registration for the Company that has few operational benefits to the business.

6. Professional Tax

7. Goods and Services Tax ("GST")
Goods and Services Tax envisages bringing together the majority of the indirect taxes in India under one roof. Generally, the GST is levied upon the selling of goods/services.

Registration is mandatory upon satisfaction of the restricted **turnover threshold/conditions laid down by the GST law.**

8. Payroll Registrations

The business has to opt for a few registrations mandatorily in case any employees are engaged/ hired and the business is running payroll;

- Professional tax (EC)
- Provident Fund registration
- Labour welfare fund registration
- Employee State Insurance Corporation registration (ESIC)

9. Miscellaneous Registrations

The business needs to register under a few regulations subject to its operational requirement to obtain the licenses;

- FSSAI License
- TRAI License
- DoT License
- IT/ITes License, etc.

3

RUNNING THE BUSINESS

Running your business hinges on one word - Sustainability.

The strategy you employ to achieve short term goals accumulating into your long-term goals requires a clear visibility of your business plan, important milestones and a systematic tracking of your progress.

When sustainability becomes a part of your organization’s culture, you know your business is here to stay.

Before your business can grow and sustain its momentum, you must take action in support of the following mediums to assure your company builds a strong foundation for long-term success:

Accounting (the core support)

To keep a record of all the transactions of the business. This gives a thorough estimate of the financial standing of the business. The Company needs to ensure that the accounting is well maintained and in real-time to know the standing of the business in the ever-growing market.

Generally, the majority of startups are using Tally and Zoho Books as their primary accounting software platform.

Refer to our blog for tips: 10 Accounting tips to Startups

Secretarial and Regulatory Compliances

The majority of startups fail due to non-handling of the compliances effectively. The primary reason is the non-clarity of the registration/ compliances that any businesses need to operate and there is no quality support to adhere to the requisites.

If compliance feels like an expense, non-compliance will end up in a loss for your business.

Certain compliances ought to be done within specific time limits and are important with regard to keeping the regulators of the government at bay.

Refer to the below link to
Treelife - Compliance Calendar

PAYROLL MANAGEMENT

One of the challenges that every startup face is to effectively manage the payroll for their employees including:

- Drafting the tax-efficient salary structure
- Computation/deduction of the appropriate taxes
- Complying with applicable compliances like PT, PF, etc.

The recommended payroll software tool is RazorX payroll and Zoho payroll,l which most startups use to manage their payroll with ease.

Adequate Budgeting

Budgeting is essential for the allocation of funds for specific activities of your business and benchmarking your performance that can be used with a detailed financial model.

Refer to our blog to access the format - Financial Model for Startups

Management Information System (MIS)

Is a tool for transforming the data collected into the information of the business. This assists the management in charting the road map, taking strategic decisions and enabling the growth of the business.

Refer to our blog to know more - All about MIS Report

Internal Audit and Health check

Along the lines of MIS, an internal audit helps to identify the operational inefficiencies of the business in a detailed manner. Also, the company shall perform a health check run at frequent intervals to evaluate the effectiveness of reporting made by the company under applicable regulatory compliances

This paves the way for effective management and brings stability by

4

RAISING CAPITAL

Startups get on track with bootstrap funding with an initial capital infusion to business. However, to sustain the market and mark its presence, the company seeks external investments to meet the cash burn to go for expansion.

STAGES OF FUNDING

01 Initial Investment

Usually the founder puts their corpus to build an idea into operational phase

02 Angel Investment

When idea converts to a prototype, angal investors extend thier hand to innovate the business

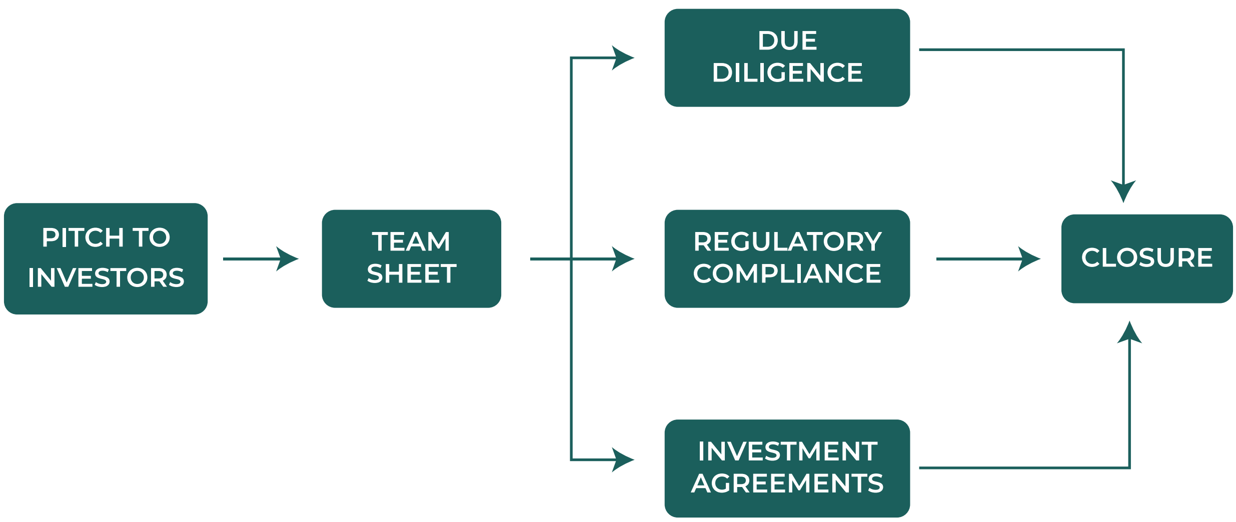
03 Venture Capital

This comes where the business occupy a cut in existing demand and classify for a decent valuation

04 Initial Public Offer

When business earns the public confidence and shout for a public contributors to get a hold in captable

PROCESS FLOW



TYPE OF INSTRUMENTS

The founders incorporate their unicorns with simple equity financing. To go for an external round, Startups typically issue the following instruments:

Type Of Instrument	Meaning	
Equity Shares	It is the common stock of the Company and has all voting rights	Initial investment by promoters/ founder/ friends and family investment
Compulsorily Convertible Preference Shares (CCPS)	Shares issued with specific rights to the investors under the SHA	Preference in liquidation over equity shares and used by angel network
Compulsorily Convertible Debenture (CCD)	Convertible into equity based on a re-determined condition	Preference in liquidation over shareholders and used for angel rounds
Convertible Notes (CN)	Short-term debt that usually converts into shares of the Company	Minimum value for issuance is INR 25 lakhs
Employee Stock Option (ESOP)	Employee benefit drafted to encourage employees to acquire stocks or ownership in the company	It is an option that is granted to employees to purchase a share of the Company at a pre-determined price

Raising capital funds indicates parting away with an equity stake in your business in return for capital. The idea behind raising capital is best explained through an analogy of a “Pie”. At the beginning there are two to three people in the pie with a bigger bite size but less returns.

As you raise more capital, although the bite size of your portion reduces, the size of the overall pie increases.

INTELLECTUAL - PROPERTY RIGHTS

Type of Funding	Stage of Funding	Typical percentage of equity to be diluted and the amount raised
Friends & Family Round Reaching out to people close to you and asking them to put a portion of their savings into your idea	To kickstart the business. Initial stage is after the company is incorporated.	15-20% for Rs. 5 Lakhs to Rs. 10 Lakhs
Seed/Angel Investment Primary effort in raising external capital. Typically, this round is sourced from professionals or semi-professional Angel Investors either individually, or in a consortium.	One of the primary rounds of external capital raising. Often at the time when operational difficulties arise and an immediate requirement of money is an impediment.	Up to 20% for up to Rs. 1 Crore
Series A/Early-Stage Investing Typically, capital is raised through Venture Capital funds	At the time, when the need for a larger amount for growing of the business.	20-30% for Rs. 4 Crores to Rs. 12 Crores
Series B Typically, capital is raised through Venture Capital funds, mostly led by the Series A investors.	At the time of Expansion Stage. A need for Series B is felt and sufficed at the time of expansion of the business.	May vary according to the needs of the business.
ESOPs: Denotes Employee Stock Option Plans.	At the time of Angel Round and/or Series A.	15% pool of the equity.

5

EXTERNALISATION

Externalisation is a strategy designed to flip the ownership structure of a domestic company to an offshore jurisdiction wherein legal and regulatory benefits can be availed.

This process is usually undertaken by startups raising investment from foreign parties or accessing the global clientele/technology.

However, the business needs to evaluate the attached risks including:

- **Transfer pricing**

Due to migration of IP, tech, patents, etc. to the overseas entity which is the holding co., Transfer pricing regulations will be applicable for inter-company transactions.

- **Regulatory conditions**

Conditions under the ODI route need to be evaluated for investment by Indian residents in overseas entities. Additionally, such investments require reporting with the AD Bank

- **Taxation**

Indian entities are liable to pay tax on shares acquired by the overseas entity (holding co.) and consideration value shall be FMV calculated as per Rule 11UA (Income Tax Act).

Given the recently revamped regulations on overseas investment (ODI rules), here are many smaller points in the execution of Externalisation and it is recommended to use expert assistance to build the structure and resolve the other operational challenges.

As you would have realised, starting up is not just about having a revolutionary idea, but also getting the execution right.

It is the execution that is your differentiating factor. And the idea behind a strong execution is a strong business backend. This document gives you a perspective on how to strengthen this part of your business.

At the crux of it, this document is all about
Simplifying Your Business.

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