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Legal Framework for Startups in India

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Introduction

Over the last decade, India has developed one of the world’s most sophisticated legal ecosystems for early-stage companies. The Startup India Action Plan launched in 2016 has evolved into a multi-layered legal regime integrating company law, taxation, intellectual property, foreign exchange management and insolvency law. To a founder, compliance isn’t optional paperwork; it’s the scaffolding on which fundraising, taxation, and the eventual exit are built. This article traces the major statutes and regulatory instruments regulating startups in India, focusing on the reforms introduced in the beginning of 2026.

Choice of Legal Structure

The first thing any founder has to think about is choice of entity. Most startups opt to register as a private limited company under the Companies Act, 2013 or as a limited liability partnership under the Limited Liability Partnership Act, 2008 . This is because only these two forms are eligible for the income-tax exemption discussed below. The Startup India scheme allows recognition for single-person companies, partnership firms and from February 2026, cooperative societies, but the tax holiday under the Income Tax Act, 1961 is still available only for private limited companies and LLPs. This distinction is important in drafting, because it is administratively burdensome to convert an entity after a fundraising or revenue milestone has been passed, and it can upset contractual arrangements with investors.

Startup India Recognition and the 2026 Reforms

Recognition by the Department for Promotion of Industry and Internal Trade ("DPIIT") is the gateway to nearly every statutory benefit available to startups. On 4 February 2026, DPIIT superseded its 2019 framework through a new Gazette Notification[1], introducing the most substantial revision to the scheme since inception. The turnover ceiling for standard recognition was doubled from ₹100 crore to ₹200 crore, and the definition of "Startup" was widened to expressly include Multi-State Cooperative Societies and State or Union Territory-registered Cooperative Societies.

For the first time, the 2026 Notification also created a separate “Deep Tech Startup” category for research-intensive entities. Such entities must show work on new scientific or engineering knowledge, high research expenditure as a percentage of revenue, and ownership of, or progress towards, novel intellectual property . Deep Tech Startups, in contrast, are given a longer recognition window of twenty years and a higher turnover cap of ₹300 crore, taking into account the longer gestation periods for frontier research. The Notification also recalibrated fund-utilisation conditions: restrictions on using startup capital for residential property, luxury assets or speculative investments now apply for the whole recognition period, not just the fixed seven-year window under the 2019 regime. To make the framework administratively scalable with increasing application volumes, the composition of the Inter-Ministerial Board that certifies eligibility for tax benefits can now be changed with the approval of the DPIIT Secretary.

Taxation Benefits under Section 80-IAC

The principal fiscal incentive available to recognised startups is the profit-linked deduction under Section 80-IAC of the Income Tax Act, 1961, which permits a hundred percent deduction of profits for any three consecutive assessment years out of the first ten years following incorporation[2]. Eligibility for claiming this benefit has been extended up to the year 2030, giving founders a longer runway to time the exemption around profitable years rather than loss-making early cycles. A related and long-standing concern for investors—the so-called "angel tax" under Section 56(2)(viib) of the Income Tax Act—has been formally abolished with effect from 1 April 2025, and the 2026 Notification accordingly removed all residual references to that provision. Approval under Section 80-IAC nonetheless remains a separate application,

[1]Dep't for Promotion of Indus. & Internal Trade, Gazette Notification G.S.R. 108(E) (Feb. 4, 2026) (India) [hereinafter 2026 Notification].

[2]Income Tax Act, 1961, § 80-IAC, No. 43, Acts of Parliament, 1961 (India).

distinct from DPIIT recognition itself, and is assessed by the Inter-Ministerial Board on the basis of the innovation, scalability, and employment-generation potential demonstrated by the applicant.

Intellectual Property, Compliance Relief, and Exit

Beyond taxation, DPIIT recognition unlocks concessions under the Patents Act, 1970 and the Trade Marks Act, 1999, including an eighty percent rebate on patent filing fees and a fifty percent rebate on trademark fees, together with fast-tracked examination of applications[3]. Recognised startups may also self-certify compliance under nine labour statutes and three environmental statutes, substantially easing the routine inspection burden typically imposed on new enterprises. Where a startup fails, the Insolvency and Bankruptcy Code, 2016 provides a fast-track corporate insolvency resolution process specifically calibrated for startups, enabling voluntary winding-up in a considerably compressed timeframe compared to ordinary corporate liquidation[4]. This exit mechanism reflects a broader policy recognition that the ability to fail quickly and cheaply is itself an important ingredient of a healthy entrepreneurial ecosystem.

Foreign Investment and Allied Regulatory Considerations

Startups seeking overseas capital must additionally navigate the Foreign Exchange Management Act, 1999 and the rules framed thereunder, which govern the pricing, reporting, and sectoral limits applicable to foreign direct investment[5]. While most sectors permit ordinary equity investment through the automatic route, the treatment of limited liability partnerships under the Non-Debt Instruments Rules remains comparatively restrictive, a gap that has drawn continued commentary despite LLPs being fully recognised as eligible startup entities under the DPIIT framework. Startups must also register under the Central Goods and Services Tax

[3]Patents Act, 1970, No. 39, Acts of Parliament, 1970 (India); Trade Marks Act, 1999, No. 47, Acts of Parliament, 1999 (India).

[4]Insolvency and Bankruptcy Code, 2016, No. 31, Acts of Parliament, 2016 (India).

[5]Foreign Exchange Management Act, 1999, No. 42, Acts of Parliament, 1999 (India); Foreign Exchange Management (Non-Debt Instruments) Rules, 2019 (India).

Act, 2017 once turnover crosses the prescribed threshold[6], and recognised entities are, in addition, entitled to Earnest Money Deposit exemptions on public-procurement tenders and access to the Fund of Funds for Startups administered through the Small Industries Development Bank of India. Each of these regimes operates independently of DPIIT recognition, which means that founders must track company law, tax law, and foreign exchange compliance as parallel, not sequential, obligations.

Conclusion

The Indian startup legal framework has evolved from a single-window recognition scheme into a genuinely interconnected system spanning corporate, tax, intellectual property, and exchange control law. The 2026 reforms—wider entity coverage, the Deep Tech category, and the abolition of angel tax—signal a deliberate shift toward rewarding long-horizon, research-intensive enterprise rather than mere incorporation. For founders and their advisors, the operative lesson is that legal compliance in 2026 is not a one-time formality secured at incorporation but a continuing condition attached to the entire period of recognition, demanding sustained attention through every subsequent stage of the enterprise.

[6] Central Goods and Services Tax Act, 2017, No. 12, Acts of Parliament, 2017 (India).