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STARTUPS' FUNDRAISING, UNICORN GOVERNANCE, AND MERGERS AND ACQUISITIONS CHALLENGES: AN ANALYSIS WITHIN THE VIKSIT BHARAT 2047 FRAMEWORK

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ABSTRACT

The Viksit Bharat vision of India becoming a developed country by 2047 is greatly dependent on the presence of an entrepreneurial ecosystem. Startups are important for stimulating employment, innovation, and foreign investment. However, despite over 125,000 registered startups and more than 110 unicorns, the Indian startup ecosystem is confronted by significant structural, regulatory, and governance issues. This study examines the key concerns: the problem of raising capital at the early and middle stages of startups, the loopholes in corporate governance among unicorns, and the complex regulations governing mergers and acquisitions in the startup space.

This research uses legal analysis, DPIIT and SEBI data, and a comparison with the startup ecosystem in the United States, Singapore, and Israel. This reveals significant gaps, particularly in the Companies Act of 2013, FEMA 1999, and the Competition Act of 2002. These loopholes complicate fundraising for startups, weaken board accountability in high-value startups, and slow down the M&A process. This study also examines how the lack of standard term sheet rules puts weak investor startups at a disadvantage globally. This study proposes a multi-pronged reform agenda, including the establishment of a separate startup regulatory authority, simplified M&A fast-track regimes for qualifying startups, mandatory governance codes of unicorns, and enhanced tax incentives to angel investors. The authors argue that these reforms are not only good policy options but also lawful and institutional necessities to fulfil India's Viksit Bharat 2047vision.

Keywords: Viksit Bharat 2047; Startup Fundraising; Unicorn Governance; Mergers and Acquisitions; DPIIT

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1. Introduction

1.1 Background

Viksit Bharat, which translates to "Developed India," is the national vision aimed at transforming India into a fully developed country by the 100th anniversary of its independence in 2047. It aspires to build a nation that is inclusive in its economic growth, technologically self-reliant, innovative, vibrant, and globally competitive. A core component of this vision is that startups and entrepreneurship are essential for achieving this transformation. The Indian start-up ecosystem has proven to be highly vibrant over the last decade. The country ranks 3rd in the world by the number of recognised startups, with over 125,000registered under the Departments for the Promotion of Industry and Trade as of 2024. The ecosystem includes over 110 unicorns, placing India third globally after the United States and China. Areas such as fintech, edtech, health tech, deep tech, agritech, and software-as-a-service (SaaS) have already raised billions of dollars in venture capital and are driving job creation and technological advancement like never before.

However, behind the façade of dynamism, there are unrelenting and structurally deep-rooted legal, regulatory, and governance issues that threaten to stifle India's entrepreneurial desires. Two interconnected problem clusters require urgent scholarly and policy considerations.

First, the fundraising for startups, especially at the seed, Series A, and growth rounds, is still needlessly complicated by the inconsistent regulations of the Companies Act 2013, and the FEMA.

(1999) and the Securities and Exchange Board of India (SEBI) regulations. The net effect is a slower, more expensive, and more uncertain capital formation environment than that in a similar jurisdiction, which puts Indian startups at a disadvantage in accessing capital in the global market.

Second, corporate governance structures do not keep pace with the scale of Indian start-ups becoming unicorns. These characteristics of the founder-led structure, lack of transparency in independent board control, lack of transparency in related-party transactions, and dual-class share structure have not been under regulatory control and have led to a sequence of high-profile governance failures. The BharatPe, GoMechanic, and Trell cases opened the door to the dark side of the unicorn ecosystem in India and raised acute concerns about fiduciary

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responsibility, protection of investors, and suitability of the current legal frameworks to deal with corporate malpractices in Indian-based technology companies.

Third, startup space is limited by procedural complexity, jurisdictional ambiguity, and valuation issues in M&A activity. The Competition Act 2002 review thresholds, FEMA cross-border investment norms, and NCLT approval timelines have a multilayered approval architecture, which is unequal in burdening startups relative to the age of the corporation. The regulatory framework is tailored to an alternative age of corporate dealings, and has not been adapted to the unique attributes of start-up enterprises. of technology-based start-up companies.

1.2 Statement of the Problem

This study focuses on key legal issues in the Indian startup ecosystem using the aspirational Viksit Bharat 2047 framework. It investigates the normative aspects and empirical consequences of such issues with reference to fundraising, corporate governance, and mergers and acquisitions, and suggests specific legal changes to address these issues.

1.3 Research Objectives

1. To test the legal and regulatory restrictions on raising startup funds in India under the Companies Act 2013, FEMA 1999, and the Income Tax Act 1961 across various funding phases.
2. Determine the effectiveness of the corporate governance framework in unicorn-stage startups by revealing the structural vulnerabilities and accountability loopholes in the pre-IPO stage.
3. To assess the fit of the current state of the start-up's regulatory environment in India and the long-term expectations of Viksit Bharat 2047 according to global standards.
4. To examine regulatory intricacies and procedural difficulties in inbound and outbound M&A deals in Indian startups.
5. To make evidence-based legal and policy changes to fill regulatory gaps and improve a consistent, globally competitive environment for Indian start-ups.

1.4 Significance of the study

This study is important because it determines that there are critical legal and regulatory loopholes that impede the growth of startups in India. This highlights the role of fundraising barriers and poor governance worldwide in determining India's competitiveness**.** This study

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offers a comparative view of global practices to determine India's competitiveness. It also proposes specific legal changes to enhance reforms, strengthen the startup ecosystem, and contribute to the vision of Viksit Bharat 2047.

2. Systematic Literature Review

The academic literature on India's startup ecosystem, corporate governance, and M&A regulations has increased significantly over the past decade. Nevertheless, there are still large gaps, especially in areas where startup law meets corporate governance theory and the Viksit Bharat 2047 policy framework. This review surveyed the most pertinent contributions concerning the three thematic clusters.

1. Startup Fundraising and the Regulatory Environment.

Lerner and Nanda (2020) confirmed that regulatory friction is a disproportionately low resource; early-stage firms with inadequate legal and financial resources are the most impacted by regulatory friction in capital markets. Agrawal, Catalina, and Goldfarb (2022) also confirmed this in the Indian context, reporting that founders of startups devote a disproportionate amount of time to dealing with regulatory issues. The World Bank Doing Business Report (2019, 2020) has continuously placed India lower than the global averages on the measures of setting up business and minority investor protection, implying structural constraints at the systemic level, as opposed to the failure to enforce regulations.

Dossani and Kenny (2007) provide preliminary research on venture capital in India. They observed that the legal infrastructure, especially in the areas of repatriation of profits and exit, was far behind the zeal for entrepreneurs in the foundation. A later analysis by Mitra (2020) found that the pricing guidelines of FEMA and the approval requirement of RBI created what he called a regulatory discount on the valuation of Indian startups in cross-border deals. The expert committee on the startup ecosystem 2022 of the finance ministry found the provision in Section 56(2)(viib) of the Income Tax Act, which introduced the so-called "angel tax," to be a major disincentive to domestic early-stage investments, a problem that was partially but not entirely solved by later amendments to the law.

2. Unicorn Governance and Corporate Law

Gilson and Milhaupt (2021) had argued that the technology companies, which are increasingly expanding in the world, have a structural conflict between the control of the founder and the responsibility of the investors, and this is usually solved through the dual-class structure of the

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shares that should be rigidly controlled by the regulatory authorities to prevent entrenchment. The Companies Act 2013 of Indian private companies was designed to match traditional businesses, as argued by Varottill (2019) and Bhandari (2021).

Chakrabarti (2023) identified such governance failures in BharatPe to be indicative of a structural regulatory incompetence: the absence of necessary independent audit committees with investigative materiality in pre-IPO startups. The consultation paper, on the basis of differentiating voting rights by SEBI (2019), identified the need to have a governance structure that would intervene in the incentivization of founders and safeguard the interests of investors but had only partial legislative responses in the following years, never eliminating the underlying tension.

3. M&A, Competition Law, and Startup Transactions

A study of the variation between the Competition Commission of India's jurisdictional thresholds and the deal value transactional environment in the reality of startups, Bagchi (2020), discovered that a 2023 introduction of a transaction-based value threshold was still an imperfect proxy of deal value in startups. Desai (2022) reported systematic valuation mismatches between Indian regulatory standards and international valuation frameworks, such as disconnected cash flow and other similar company analyses by FEMA pricing rules, which had real cost implications for the transaction parties and created uncertainty in cross-border deals.

When comparing the approval procedure through the BRICS countries in relation to M&A, Singh and Khanna (2023) determined that the average time of Indian NCLT procedures of merger was 14-18 months, in comparison with 3-4 months in the Singapore High Court.

4. Viksit Bharat 2047 and the Innovation Policy Framework

Paperwork, including the NITI Aayog India Innovation Index (2023) and the DPIIT Startup India Action Plan review, has the vision of the government to turn India into a global hub of innovation by 2047. In their commentaries, Krishan (2023) and Raghunath (2024) indicated that such a desire requires not only fiscal policies but also an overhaul of the legal structure of entrepreneurship. The importance of legal design in the creation of sustainable innovation economics has been critically grounded in the comparative analysis of the legal-institutional ecosystem of Silicon Valley presented by Saxenian (2006), and the cause-and-effect analysis of the role of law in the development of the venture capital market presented by Gilson (2003).

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3. RESEARCH METHODOLOGY

This study followed a mixed-method approach that involved doctrinal legal analysis, a review of empirical data, comparative legal analysis, a case study approach, and normative analysis. It analytically considers primary legislation (including the Companies Act, FEMA, and SEBI regulations) and secondary legal sources, as well as empirical data from sources such as DPIIT, SEBI, and RBI (2018–2024). It further compares the regulatory framework of India to other jurisdictions, such as the US, Singapore, Israel, and the UK, as well as provides real-world case studies of governance failures and M&A transactions, and reviews any proposed reforms in relation to constitutional principles and international standards to ensure legal soundness and relevance in practice.

4. DISCUSSION

4.1 Research Analysis

1. Startup fundraising: Navigating the Regulatory Labyrinth

i. The capital formation framework and its structural discontents

The start-up fundraising process in India is multi-layered, and its regulation is complex, which has evolved, rather than been designed, over the years. On a simple level, the Companies Act 2013 governs securities like equity shares, compulsorily convertible debentures (CCDs), and compulsorily convertible preference shares (CCPS), the most used instruments in venture capital transactions. Above this foundation are FEMA 1999 and the Foreign Direct Investment policy, which regulates the inflow of foreign capital with the requirement of approval. Section 56(2)(viib) was one the most important of the many provisions given by the alternative investment vehicles and the income tax act of 1961 in terms of the economics referred to as regulatory stacking, a situation where in theory it is possible to meet all layers of regulation but the cumulative cost of both regulatory tires is prohibitive to start-ups with limited resources.

ii. The Angel Tax: A Penalty on Entrepreneurial Success

Income Tax section 56(2)(viib), commonly referred to as the "angel tax", is an income tax levied as income under other sources on any premium paid on the issue of shares in a closely held company that is not at a fair market value calculated according to prescribed methodologies. This provision was enacted in 2012 to reduce money laundering by means of inflated share premiums, but has had profoundly counterproductive implications for legitimate startup fundraising in the ten years since

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its enactment.

According to the pricing guidelines of the Foreign Exchange Management (Non-Debt Instruments) Rules 2019, Indian companies shall not issue shares to foreign investors at a price below the fair market value as calculated under the SEBI or income-tax-prescribed methodologies, and transfers should not be made by foreign investors to Indian residents at a price higher than this value. This imposes a regulatory limit, especially for materials with a secondary transaction. The shares of a startup sold and bought between investors at market-determined prices may not be within the allowable range, which exposes both parties to compliance risks.

2. Unicorn Governance: Power Lacking Commensurate Accountability

FEMA's pricing guidelines under the Foreign Exchange Management (Non-Debt Instruments) Rules 2019 mandate that Indian companies may not issue shares to foreign investors below the 'fair market value' as determined under SEBI or income-tax-prescribed methodologies and that transfers from foreign investors to Indian residents may not occur above this benchmark. This creates a regulatory constraint that proves particularly consequential in secondary transactions: startup shares traded between investors at market-determined prices may fall outside the permitted range, creating compliance exposures for both buyers and sellers.

3. Unicorn Governance: Power Without Commensurate Accountability

Corporate governance among Indian unicorns has a structural paradox: firms controlling thousands of crores of investor capital and tens of thousands of employees tend to have corporate governance structures that are more characteristic of partnership firms than publicly traded firms with similar stakeholder footprints. The Companies Act 2013 contains strong governance standards, including mandatory audit committees, nomination committees, remuneration committees, and independent directors, for companies listed and large companies with paid-up capital exceeding set limits. However, the legal form of practically all pre-IPO startups, irrespective of valuation, has a broad exemption from such requirements by Section 462 of the Act covering a private company. The practical implication of this is that the protection of investors in unicorn-stage startups relies more on negotiated contractual terms in shareholders' agreements, including information rights, board representation rights, anti-dilution rights, drag-along, and tag-along rights, than on statutory protections available by resort to a publicly available regulatory mechanism.

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4.2 Case Study: Governance Failures and Their Legal Dimensions

One case in point is the BharatPe governance crisis of 2022. The board of directors alleged. One case in point is the BharatPe governance crisis of 2022. The board of directors alleged that the co-founder and managing director of the company engaged in financial misconduct, such as making fraudulent payments to vendors, non-disclosure of conflicts of interest in making procurement decisions, and falsifying academic qualifications in their official disclosures. The ensuing investigation and legal case revealed that the company lacked the following in its governance structure: an independent audit committee with investigative powers that are independent of the executive team; a strong whistle-blower policy with legal protection of those who blow the whistle; well-defined and board-approved procedures in the related party transactions; and enforceable fiduciary duty standards applicable to the executive management of non-public companies similar to those applied to directors of the listed company.

The legal remedies that investors and the board have used to combat these failures, the civil litigation on breach of contract and breach of fiduciary duty, complaints to the Serious Fraud Investigation Office (SFIO), and the NCLT petition for oppression and mismanagement, were slow, costly, and untested in their effectiveness. There was no customised mechanism of private enforcement of governance failures in high-value private firms, which exposed investors and other stakeholders to enormous loss in comparison to the solutions that shareholders of listed firms under the SEBI umbrella could enjoy under the enforcement umbrella.

4.3 Mergers and Acquisitions: Structural Complexity and Strategy Impediment

1. Competition Law and the M&A Startup Challenge

The Competition (Amendment) Act 2023 established a deal value requirement of INR 2,000 crore for mandatory notification to the Competition Commission of India (CCI) on transactions whose target is significant business operations in India. The amendment resolved a real jurisdictional issue; the previous threshold, based on asset and turnover values, often did not reflect the large-value transactions of data-rich and capital-light technology startups. Nevertheless, this practice is problematic.

The term "substantial business operations in India" does not have a clear statutory or regulatory meaning at the time of writing, which introduces pre-notification uncertainty as a mandatory condition for dealing parties. The timing risk presented by the possible length of the Phase II investigation (up to 150 working days) can fundamentally change the economics of startup acquisitions, where the value of the target can be highly contingent on the ability to keep key

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employees, maintain competitive momentum, or complete a product development cycle that cannot be stopped during the regulatory examination. Lack of a specific startup M&A track in the review architecture of CCI implies that comparatively simple acquisitions can be handled at the same time as complex deals with real competition issues.

2. Cross-border M&A: FEMA, Pricing, and Structural Complexity

Mergers and acquisitions across borders with Indian startups: Indian startups, be they inbound acquisitions by foreign companies or outbound acquisitions by Indian startups of foreign companies, must navigate both the FEMA Overseas Direct Investment (ODI) and the Overseas FDI under the FEMA Overseas Investment Rule 2022. The interplay of these rules with the India tax treaty network, transfer pricing regulations, and indirect transfer tax provisions in the Income Tax Act provides a multidimensional compliance environment that creates high transaction costs.

5. CONCLUSION AND SUGGESTIONS

5.1 Summary of Key Findings

The report concludes that regulatory and structural inefficiencies are major limiting factors for India's start-up ecosystem. It finds that duplication in the disposition of major laws discourages capital formation, posing delays, excessive compliance costs, and unpredictability in fundraising. It also demonstrates that there are serious lapses in corporate governance in unicorns, especially in the inadequacy of board accountability and regulatory oversight in the pre-IPO phase. Moreover, the study points out that complicated and time-intensive M&A processes lower deal efficiency and deter investments.

5.2 Conclusion

The Viksit Bharat 2047 vision is the most ambitious formulation of national development aspirations ever made in India. The decision to put India's demographic strength, entrepreneurial drive, and technological potential into a fully developed, globally competitive economy within a generation. Startups do not happen to be incidental to such a vision; they, in the very words of the government itself, are the main drivers of innovation and job creation. However, the legal and regulatory frameworks in which Indian startups exist are still designed in a disjointed manner, heavily handed in their implementation, and not adequately adjusted to the governance complexity and global ambitions of high-valuation technology startups.

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The paper has revealed, through a combination of a doctrinal analysis, review of empirical data, comparative legal literature, and a case study analysis, that three mutually reinforcing issues– fundraising friction, deficiencies in unicorn governance, and procedural complexity in M&A– are a structural limitation of India's entrepreneurial potential that cannot be solved by incremental tinkering. All these factors together comprise an angel tax scandal, FEMA pricing inflexibility, and the legal ambiguity of innovative financing vehicles, producing an environment of capital formation that is probably less competitive than those of peer jurisdictions in India. The lack of compulsory governance principles of pre-IPO unicorns opens loopholes of accountability that burst into big scandals with regularity, hurting investors and the global image of the Indian startup ecosystem. The multi-layered M&A approval system between CCI, NCLT, FEMA, and tax rules sets the timing and costs of disincentivizing startup consolidation and cross-border acquisition, limiting the ecosystem's production of the large-scale technology companies Viksit Bharat needs.

The reform agenda suggested by this study, a unified startup regulatory authority, a rationalised angel tax, FEMA instrument clarity, a unicorn governance code, single-point ESOP taxation, M&A fast-track procedures, and a regulated secondary market, is neither radical nor untested. All of these elements consider the existing international precedent, have been supported in one way or another by academic and policy literature, and have filled a particular identified legal gap with a structurally consistent answer. All of them make up a consistent legal reform agenda that can make a material contribution to the startup ecosystem in India in a timeframe pertinent to the 2047 horizon.

One more dimension should be highlighted. These reforms have more constitutional overtones than economic policies. Part IV of the Constitution of India, the Directive Principles of State Policy, requires the state to work towards the achievement of economic arrangements that will avoid the concentration of wealth and promote equitable distribution of opportunities. A regulatory framework that systematically puts domestic investors at a disadvantage over foreign investors, punishes successful fundraising by imposing arbitrary taxation demands, and does not hold powerful founders to any meaningful governance demands conflicts with these founding commitments. The reform of law in this field is not economically desirable, but in some sense, it is constitutionally imperative. The question before lawmakers, regulators, and legal scholars in India is to develop the legal infrastructure that Viksit Bharat is worthy of: allowing but not being permissive, protecting but not restricting, and being sophisticated yet

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not inaccessible.

5.3 Suggestions

1. **Form a Unified Startup Regulatory Authority**

The initial reform proposed by this paper is the institution of a statutory Unified Startup Regulatory Authority (USRA) with a composite mandate such as the single-window regulatory clearance of fundraising transactions, the power to coordinate regulatory conflicts between agencies in startup matters, the special adjudicatory forum with fast-track authority, and the power to rule through the issuance of startup-specific regulatory standards of binding legal effect. The USRA is to be established based on a specific Startup Enterprises Act, and a governing board should include representatives of DPIIT, SEBI, RBI, MCA, and the income-tax authority, as well as independent members of the private sector with experience in venture capital and start-up operations.

2. **Rationalise the framework, Viksit Bharat, the Angel Tax, and Develop Early-Stage Investment Incentives**

The present study proposes that the full exemption of startups listed under the DPIIT list under Section 56(2)(viib) in the Income Tax Act should be amended, and a full statutory carve-out of arm-length investment based on investor eligibility declarations should be introduced instead of the existing partial carve-out. In non-arm's-length transactions, a specific anti-abuse provision can be used; however, the fact that the transaction is with non-arm's-length parties should be proven by the tax authority and not by the startup regarding whether the fair market value has been met.

Complementarily, DPIIT-recognised startups should have a minimum three-year tax holiday under Section 80-IAC, changed to seven years, and the incorporation date eligibility sunset clause should be eliminated. The exemptions of the capital gains of angel investors in Section 54GB should be extended to include investments made through Category I and II AIFs, and this will eliminate the direct investment requirement, which is unfavourable to institutional aggregation of angel capital.

3. **Regulatory Clarity over Innovative Financing Instruments**

The Foreign Exchange Management (Non-Debt Instruments) Rules should be revised to provide legal recognition, classification, and pricing guidelines for SAFEs, convertible notes, and revenue-based instruments of financing. An effective regulatory framework must clarify

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the maximum allowable period for conversion, the pricing mechanism that can be used in conversion events, such as valuation caps and discount rates, the reporting requirements that must be made to the Reserve Bank of India, and the specific implications of FDI for each category of instruments. Such regulatory consistency would allow Indian startups to use globally standardised fundraising instruments and would directly deal with offshore incorporation arbitrage that now directs the potential India-registered investment to Singapore and Delaware.

4. Create a Startup M&A Fast-Track Regime

The Companies Act 2013, section 233, needs to be significantly expanded to establish a so-called Startup M&A Fast-Track Regime, which would cover mergers involving at least one DPIIT-recognised startup that meets certain criteria. Under this regime, the maximum NCLT approval timeframe must be limited to 90 days, either through special startup benches or an electronic fast-track system; regional directors must be empowered to grant deemed approval if no creditor or regulatory objection is received within 60 days; and the small-company thresholds for NCLT approval are a paid-up capital of INR 50 crore and a turnover of INR 500.

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