

# Exploration of Corporate Law for Startup business organizations: A study based on Startup Business Organizations in Sri Lanka

**Ratnayake. S.B.D.C**

Business School, Asia Pacific Institute of Information Technology (APIIT) Sri Lanka  
[dasunr@apiit.lk](mailto:dasunr@apiit.lk)

## ABSTRACT

*This study examines how corporate law and startup business organizations interact in Sri Lanka, with particular emphasis on the legal frameworks and challenges these emerging enterprises encounter during their early stages of growth. With an increasing number of startups across various industries, Sri Lanka has seen a boom in entrepreneurial activity in recent years. However, many startup businesses still find it difficult to navigate the complexities of corporate law, including issues with contract law, intellectual property law, governance, business formation, and local regulatory compliance. The study identifies the key legal issues faced by Sri Lankan startups by analyzing primary and secondary data and conducting interviews with entrepreneurs. It also evaluates the role of the Sri Lankan government in fostering the startup ecosystem, with a focus on recent policy reforms designed to facilitate business transactions and encourage innovation. This research aims to provide insights for policymakers and entrepreneurs seeking to navigate the evolving corporate law landscape in Sri Lanka, identifying gaps in the current legal framework and making recommendations for improvement. Ultimately, the study underscores the importance of a supportive legal environment in creating a thriving startup ecosystem and advancing the nation's economic development.*

**Keywords:** Corporate Law, Regulatory framework, Startup Business Organizations

## 1. Introduction

The development of startups in developing countries has been widely recognized as crucial for growing the private sector (Davis, 2022). Modern startups not only seize opportunities but also create them (Rompho, 2018). The recent formation of startup businesses has become an important aspect for developing countries, as they are often burdened by unemployment and poverty. In this context, Sri Lanka, as a developing country, could gain significant economic benefits by fostering the growth of startup businesses. While corporate law is crucial for all businesses, startups are particularly impacted because they often have fewer resources and may lack the expertise to navigate complex legal matters. There is a growing need to understand how Sri Lankan startups manage the legal requirements related to company formation, governance, intellectual property protection, and other regulatory compliance. This study investigates the role of corporate law in Sri Lankan startups and its effects on their performance. Furthermore,

political, economic, social, technological, environmental, and legal (PESTEL) factors significantly affect the operations of these companies.

Business law plays a vital role in maintaining order in today's fast-paced business environment, serving as the guidebook for business transactions, agreements, and interactions, ensuring fairness and impartiality. In the Sri Lankan context, corporate law was introduced by the British during the colonial period. A major challenge for these companies is that they often lack awareness of the business laws that affect their operations. The main concern of Korreck, (2019) is regulatory framework for the startup businesses and therefore it is stated that better to remove too many rigid bureaucracies associated in the regulatory framework. Naturally, there are challenges in starting and growing a business, including legal issues, with the rapid growth of startups (Laksmana & Permana, 2023). The argument here is that startup businesses must carefully study Sri Lankan laws and regulations relevant to their operations before launching. Additionally, startups should research the potential obstacles they may face during the launch and operation of their business, as doing so can reduce the risk of failure. In this study, the researchers examine the legal challenges that must be anticipated when building a startup business organization.

Economic growth, innovation, competitiveness and poverty alleviation have all benefited significantly from entrepreneurship (*New\_Venture\_Creation Self.Pdf*, 2023.). Entrepreneurship policy makers are seeking to increase new enterprises and subsequent wealth creation options. As indicated by André Van Stel et al., (2007) central choice in USA to follow a low regulation route or follow a high support route. Entrepreneurial endeavors and new businesses focused on scalable and repeatable business model are known as startup business (Jain, 2018). Startups are in a phase of development and market research. They attract investors who are interested in the potential for high returns on high-risk investments. Competition law is a crucial tool for promoting economic efficiency and creating an environment where all business actors have equal access to resources. Startup businesses in Sri Lanka often face unique challenges with corporate law that can impact their formation, growth, and long-term sustainability. Managing complex regulatory requirements, ensuring corporate governance standards are met, and understanding the legal implications of doing business in a rapidly changing market are some of these challenges. Although Sri Lanka's entrepreneurial landscape is expanding, there is limited research on how corporate law specifically impacts startup businesses.

The research will investigate the legal framework governing startup businesses in Sri Lanka, focusing on existing laws, regulations and policies that impact the expansion of startups in the country. This study aims to provide valuable insights into how corporate law can better address the needs of startup businesses in Sri Lanka by examining the legal obstacles they face. The ultimate goal is to educate entrepreneurs, inform policymakers about the reforms needed to improve the startup ecosystem and establish a more supportive legal environment for entrepreneurship and innovation.

## 2. Reviewing the literature

A startup business is a venture that is still in its infancy stage with an expanding clientele base (Rompho, 2018). In particular, it is important to note that startups do not operate like legacy corporations. Large-scale organizations have the resources, power, and proven business models that enable their success. In contrast, startup businesses often lack these resources but typically possess innovative ideas, organizational agility, and goals of rapid expansion. Furthermore, startup organizations are fledgling enterprises new businesses that are just beginning to operate. Therefore, startup businesses are usually small, initially financed and run by one person or a small group of founders (Lim, 2021). Small and medium enterprises (SMEs) play a crucial role in Sri Lanka's economy, contributing to trade, services, and manufacturing sectors, which generate a significant portion of revenue and employment. According to statistical sources, SMEs account for 52% of the GDP and 45% of national employment. Findings of the Andre van Stel et al., (2006) disclosed that many necessity entrepreneurs in developing countries avoid business regulations by starting and operating a business in the informal sector. Furthermore, this study focuses on the impact of business regulations on entrepreneurship rates and finds that there is a strong conversion effect from nascent to actual entrepreneurship. Preliminary indications suggest that burdensome labor market regulations may reduce entrepreneurship rates. The findings from Kopera et al., (2018) showed legal challenges is also one of reasons to startup failure.

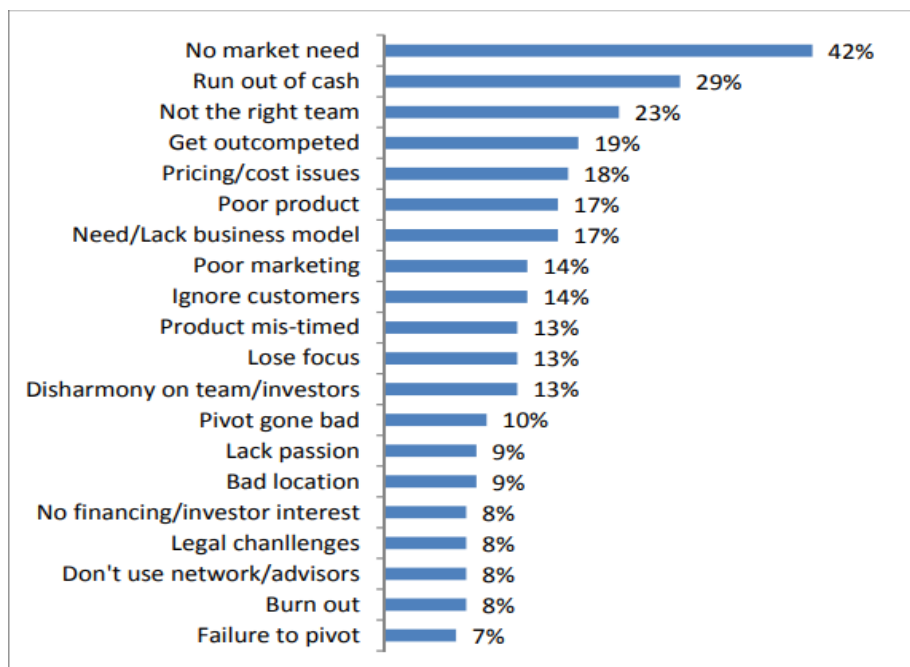


Figure 1- The main reasons of startups failure

The study observed Fryer Jr & Levitt, (2004) by founded that there is a variation of regulations within a country, across industries, across firm sizes. The study also found that startup formation procedures are slower in the provinces compared to the capital city. Additionally, there is a complex process for foreign ownership-based startups, as they require additional verifications. In this study, Fryer and Levitt selected 85 countries and

categorized the procedures into five key themes: screening procedures, tax-related requirements, labor-related requirements, safety and health requirements and environmental-related requirements. Giraudo et al., (2019) how the startup act simplified the bureaucratic procedures associated with starting and operating a new business in Italy. The study found that the introduction of faster and more transparent process for registering startup businesses, lower administrative cost and the ability for entrepreneurs to concentrate more on innovation rather than complex regulatory compliance were the main advantages.

### **2.1 Partnership Ordinance**

Partnership is a relationship which subsists between persons to carry on a business in common with a view of profit. In a partnership agreement among the partners may be made in writing, orally, conduct. The minimum number that can be in the partnership business is two and maximum is twenty (HMSO, 1890). The legislative foundation for partnerships in Sri Lanka is established by frauds prevention ordinance. Section 18 outlines the responsibilities and rights of partners which can be useful in spotting and preventing fraud (Ordinance, 1947). Hence partners should keep up to date financial records.

According to the Partnership Ordinance, partners have certain obligations they must follow:

- i. Provide accurate reports and full information on all matters that impact the partnership, including details of the material's discounted price.
- ii. Provide full disclosure of all benefits received from partnership-related transactions.

The court may order the dissolution of the partnership in the following instances:

- If a partner is found to be insane.
- If a partner is permanently unable to fulfill their obligations under the partnership contract.
- If a partner engages in behavior that is prejudicial to the partnership agreement.

In order to avoid fraud, the Business Names Ordinance governs the registration of business names. This process ensures that no two businesses can use the same name. Thus, through the Partnership Ordinance, a partnership can formalize its relationship and register a business name under the Business Names Ordinance (Asiva Noor Rachmayani, 2015). On the other hand civil procedure code section 64, 202, 249, 252 describes the guidelines for civil litigation including cases involving disagreements between partners and other parties. Partners may use the processes outlined in the civil procedure code to defend against third party claims or to file lawsuits against one another (Nos, 2002).

The startup ecosystem in Sri Lanka is evolving rapidly, with both private sector and government initiatives increasingly supporting young companies. However, for startup businesses aiming for rapid growth and scalability, the Partnership Ordinance may not always be the ideal framework. As a result, private companies are often preferred by many startups in Sri Lanka for a variety of reasons.

## ***2.2 Company Act No 7 of 2007***

As Sri Lankan startups expand, they often require more sophisticated business structures that facilitate the issuance of shares, enable them to attract external funding, and provide governance mechanisms that can grow with the company. This is easier to achieve with a private limited company structure, where liabilities are limited to the company's assets. A company is a body incorporated under Sri Lanka's Companies Act No. 7 of 2007, which replaced the Companies Act of 1982, effective May 3, 2007. This Act outlines the guidelines, protocols, and reporting requirements for registered companies. The Registrar of Companies is responsible for managing annual returns, financial statements, and company registrations. The Act also specifies the requirements for preparing financial statements for businesses and groups. According to the Act, the financial statements of public companies are available for public inspection, while those of private companies are not. However, a private company is required to submit copies of its financial statements and auditors' report to the Registrar of Companies (Sri Lankan Government, 2010). The Act requires that an auditor must be a member of the CASL to carry out audits of specific business enterprises.

Types of companies to be registered under the Companies Act No. 07 of 2007 are listed as follows.

- i. Limited companies
- ii. Unlimited companies
- iii. Company limited by guarantee

### ***2.2.1 Articles of the Association***

This document outlines the objectives of the company, as well as the rights and obligations of its members. Section 2 states that a company should undertake any business or activity, perform any act, or enter into any transaction in accordance with its Articles of Association. Furthermore, Section 13 indicates that if a company includes objectives in its Articles of Association, it must operate accordingly. Directors are the key individuals who control and manage the company and are required to act in compliance with the Articles of Association. The minimum number of directors required for a private limited company is one, and great care should be taken when selecting directors. Additionally, the Companies Act specifies provisions regarding the appointment of directors.

The following individuals are not permitted to be appointed as directors.

- i. A person who is under 18 years of age.
- ii A person who is an undischarged insolvent.
- iii. Any person who does not comply with any qualifications for directors contained in articles of association of the company
- iv. A person who is prohibited from being a director under section 213 or 214 of Companies Act No. 07 of 2007.
- v. According to Section 213 of the Act, any person during the five years after the conviction or adjudication of the following actions shall be prohibited from managing the company.

Where a person,

- Has been convicted of any offence under this act which is punishable by imprisonment.
- Has been convicted of an offence involving dishonest or fraudulent acts.

The duties of the directors below are found.

1. Duty of directors to act in good faith and in the interests of company (Section 187)
2. Duty of directors to comply with Act and Articles of Association of the company. (Section 188)
3. Duty to exercise the degree of skill and care that may reasonably be expected of a person of his knowledge and experience and shall not act in a manner which is reckless or grossly negligent. (Section 189)
4. Director of a company may rely use correct information on reports, statements, and financial data and other sources. (Section 190)
5. Approval of remunerations and other benefits of directors (section 216 of the Act).

### ***2.2.2 Legal personality***

A company is a legal entity. Once incorporated, a company becomes an artificial legal person, distinct from its shareholders, directors, and other officers. As such, a company can sue and be sued in its own name. Additionally, the company's assets and bank accounts are recognized under its name. Similar to a human being, a company can also enter into contracts.

## ***2.3 Intellectual Property Act. No. 36 of 2003***

In the dynamic business world, new trends are constantly emerging that impact both stakeholders and businesses. Therefore, the creation of a legal framework is essential to regulate these emerging trends and the elements that support them. The lawful rights resulting from intellectual activity in fields such as industry, art, science, and literature are known as intellectual property (Yang, 2013). Hence, intellectual property is an intangible creation of the human intellect. It plays a significant role in the economic, social, and technological development of any country. Intellectual property rights provide incentives for new inventors. As outlined by Gaikwad et al., (2023) new products, technologies and business models are frequently created by startup businesses and are essential to their success. Intellectual property laws provide businesses the legal tools to safeguard these innovations allowing startup businesses to maintain the competitive advantage.

### ***2.3.1 Copy right***

The rights granted by law to creators for their artistic and literary works are described in Chapter One, Preliminary Provisions. The owner of the copyright enjoys economic rights, such as the reproduction, sale or lease, distribution, public communication, and translation of the work. On the other hand, moral rights refer to protection against any distortion, mutilation, or other modifications, as well as derogatory actions related to the work, that would be prejudicial to the creator's honor or reputation (Property et al., 2003).

### **2.3.2 Trade mark**

A trademark is any visible sign, including a word, slogan, name, group of letters, symbol, design, picture, or any combination of these, that serves to distinguish the goods or services of one enterprise from those of another. The owner of a trademark can obtain exclusive rights to the mark by registering it under the Intellectual Property Act No. 36 of 2003. The trademark is initially valid for 10 years from the date of registration. Section 108 outlines what constitutes an infringement of intellectual property rights, including specific actions that would violate the rights of the trademark owner.

### **2.3.3 Geographical indications**

A geographical indication is granted when the specialty of a good is linked to its origin in a specific geographic location—such as a country, area, or zone. The quality, reputation, or other characteristics of the good must be essentially attributable to its geographical origin. Geographical indications prevent misleading claims that goods originated in a place other than their true place of origin. This is an important step toward safeguarding regional identities and promoting local products in Sri Lanka, as outlined in the 2022 amendments to the Intellectual Property Act. The study by Gutierrez, (2005) emphasizes the cultural and economic significance of geographical indicators and how they assist safeguard the reputation of goods associated with particular geographic area. The possibility of abuse and the requirement for stronger enforcement measures are two of the issues that Gutierrez discusses with regard to the geographical indicator system.

Eg.: Ceylon tea, Sri Lankan Gems, Udarata Tea, Ceylon Cinnamon, Columbia- coffee  
India -Basmati (rice), Portugal-Port (wine),Greece-Feta (cheese), France-Champagne (sparkling wine) Mexico-Tequila (spirit)

### **2.3.4 Patents**

Patents are granted for inventions, as described in Chapter Two. Once the inventor receives registration, the patent is valid for 20 years from the original filing date. The monopoly granted to the inventor by the state, which prevents others from making, using, or selling the invention, is known as the patent right. Additionally, the duties of the registrar include examining applications to ensure legal compliance (Section 63 of the Intellectual Property Act).

### **2.3.5 Industrial Designs**

Industrial designs are the decorative and aesthetic features of goods. The protection for an industrial design can be taken only if it is new.

## **2.4 Ethics**

Business ethics include set of moral principles and values (Velentzas & Broni, 2010). It is also stated that if a company does not adhere to business ethics and breaks the law, it typically ends up being fined. In order to prevent rivals from duplicating its success, Google protects its algorithm as a proprietary formula. In order to safeguard this information, Google employs non-disclosure agreements along with other legal measures. Assuring Google's continued dominance as the top search engine is largely dependent on

the efficiency of its search algorithm. Furthermore, this align with the findings of Crittenden et al., (2015), by limiting employee access to the formula, coca cola uses trade secret laws to protect its recipe. Therefore, the organization uses strict security protocols to preserve privacy. Coca-Cola stands out from its rivals because of its secret recipe, which helps it maintain its distinct flavor. In the beverage industry, this differentiation is crucial for maintaining market dominance and fostering brand loyalty.

### ***2.5 Employee Provident fund***

The Employee Provident Fund (EPF) was established under the EPF Act No. 15 of 1958 to secure the future of employees. Employees contribute 8% of their monthly gross earnings to the EPF, while employers contribute 12%. The total contribution is 20%, and the employer also contributes 3% to the Employee Trust Fund (ETF) for each employee. These contributions must be paid into the respective accounts, and the Central Bank monitors them. EPF provides opportunities for employees to take loans, and employees can withdraw up to 30% of their EPF balance for specific reasons legally accepted under labor law, such as purchasing land or building a house. Permanent employees who have worked for more than 5 years are entitled to receive gratuity. Overtime pay is required for employees working more than 8 hours per day or 45 hours per week. Additionally, there is a minimum salary for employees covered under labor law.

Following employees are not covered under Employee Provident Fund Act.

- 1 Government Employees
- 2 Family Members (contributions should be made for persons living separately from the family)
- 3 Non performing Directors
- 4 Partners of a Partnership
- 5 Contributors to an approved Provident fund(Ex: University Provident Fund)

In the following instances an employee is entitled to claim his/her EPF.

- a. Reaching the age of retirement (Male – 55 years; Female – 50 years).
- b. A female employee resigns from employment in consequence of marriage. (Should get married within 3 months of resignation or resign within 5 years of marriage.)
- c. Certified medically unfit to work due to a permanent and total disability. (It has to be certified by a registered medical practitioner who is registered under the medical ordinance)
- d. Migrating from Sri Lanka with no intention of returning.

The Employees Trust Fund (ETF) Act No. 46 of 1980 also covers university academic staff members. Upon cessation of employment, employees can claim the fund balance when they cease employment for the first time. This includes instances such as changing employment, retirement at the appropriate age, dismissal, resignation, or vacation of post. Generally, a second claim can be made after five years have passed since the first claim.



## **2.6 Shop and Office Act**

Types of leaves that can be identified under the Shop and Office Employees Act No 19 of 1954.

1. Poya Holidays
2. Casual leave
3. Annual Holidays
4. Maternity Leave

## **3. Methodology**

The framework indicates that business registration laws, labor laws, contracts, and ethics have both direct and indirect effects on startup business formation. The research methodology serves as the blueprint for conducting the research, outlining the overall data collection process. It further focuses on how the researcher will collect data, the approach and philosophy followed, as well as the methods and strategies employed. Saunders et al., (2019) showed that there are different layers of research methodology which explaining each element for the researcher to make the decisions based on the research aims and objectives.

### **3.1 Research Philosophy**

This layer forms the foundation of the research methodology. It generally elaborates on how data collection will be carried out and includes the researcher's beliefs about data collection (Ranney et al., 2015). Hence, there are three types of research philosophies: interpretivism, positivism, and pragmatism. For this study on business law application and awareness, the interpretivist philosophy has been chosen. An interpretivist philosophy focuses on understanding how individuals perceives the world. In this study, it is particularly valuable to understand how startup entrepreneurs view and interpret corporate law. In order to explore the barriers and opportunities from the entrepreneur's perspective, it is essential to investigate the subjective meanings and experiences of startup owners when navigating the legal environment, which this philosophy facilitates. It also emphasizes the importance of exploring the institutional and economic aspects of the local context that influence how startup businesses perceive and engage with corporate law.

### **3.2. Research choice**

Data collecting requires qualitative and quantitative research approaches. Qualitative research approach aims at the development of theories (Oshagbemi, 2017). Hence, a qualitative approach will help better understand the individual experiences and challenges faced by startup businesses. Interviews would be a useful tool for gathering detailed information about how startup businesses navigate legal issues, how well they understand corporate law, and how it impacts their operations.

### 3.3 Data collection technique

Data triangulation involves using multiple methods in qualitative research to develop a comprehensive understanding of a phenomenon. The author Carter et al., (2014) stated triangulation involves more than two participants in the same study to provide more conclusions. Interviews were used to collect primary data for this study. The interview participants were selected via snow ball sampling method (Kitchenham & Pfleeger, 2002). An overview of the respondents was given in the table that follows.

Table 1: Overview of Interview

| <b>Respondent</b> | <b>Position</b>   | <b>Organization</b>  |
|-------------------|-------------------|----------------------|
| 1                 | Managing Director | Sriposha Foods       |
| 2                 | Managing Director | Toffline apparels    |
| 3                 | Legal Director    | Earthbound creations |
| 4                 | Legal officer     | Circle Books         |
| 5                 | Managing Director | Asgiriya Tyre House  |

The interviews were guided by a set of pre-determined questions regarding business and corporate law applications. The purpose of these interviews was to identify the benefits of business-related legislation on operations and to assess the startup owners' attitudes toward business law. The data collected through the interviews provided a thorough understanding of the current level of business law adoption from different perspectives, allowing for a more comprehensive assessment. Additionally, startup businesses from a variety of industries, including software, food manufacturing, automobile, apparel, and craft design, were selected for this study. This diversity in selection reflects the varying legal requirements that apply to different business operations, particularly since the respondents hold diverse roles, including managing directors and legal officers.

### 4. Data Analysis

Thematic analysis is a qualitative research method used to systematically analyze and interpret data. It involves identifying, examining, and reporting patterns (themes) in the data, providing a thorough exploration of the research objectives. As suggested by the Braun & Clarke, (2008) thematic analysis strategy was used to analyze the data. Thematic analysis involves six steps: familiarizing with the data, creating initial codes, collating codes with supporting data, grouping codes into themes, revising themes, and writing a narrative. The results of the thematic analysis on the legal issues and perceptions of startup businesses in Sri Lanka are presented. The primary aim of this analysis is to explore how entrepreneurs engage with corporate law, including their understanding of legal frameworks, the obstacles they encounter, and how these challenges impact the operations and growth of their businesses. The qualitative data gathered from semi-structured interviews with startup founders and legal officers were subjected to thematic analysis. The results are organized according to several key themes that emerged from the data, highlighting the main legal issues and experiences shared by the participants.

#### **4.1 Doctrinal approach**

Judicial interpretations, statutes, and case law are the main subjects of a doctrinal approach to legal research. Scholars who employ this approach often analyze the legal doctrines that inform court decisions and interpret the law based on legal precedents (Hutchinson, 2016). Although this approach focuses on identifying rules and applying them to a particular situation, it does so without considering the wider social and political implications.

##### **4.1.2 Salomon Vs Salomon Case**

According to the decision in this case, a business has a separate legal existence from its shareholders, a fundamental principle in company law. Therefore, shareholders are not personally liable for the company's debts beyond their investment (Jombo, 2018).

##### **4.1.3 Lee Vs. Lee's Air Farming Ltd**

Even if a company is controlled by a single person, the case reaffirms that it remains a distinct legal entity. The judgment also upheld the right of an employee to receive compensation and benefits, regardless of whether they were solely acting as a director (Director-employee, 1897).

##### **4.1.4 Distilleries Company of Sri Lanka V. Deputy Commissioner of Labour**

The case in question concerns whether the employee is eligible for gratuity for the duration of their employment, including the time spent working for the corporation before its conversion. The magistrate court ruled that the petitioner company was required to pay the gratuity (Court, 2009).

##### **4.1.5 Kumara Fernando and others Vs Commissioner of Labour**

This case analyzes the disagreement over Sri Lankan labor law, involving labor rights, duties and matters pertaining to the Industrial Disputes Act.

#### **4.2 Findings**

The findings of this study are presented based on the research questions addressed, including the applicability of legal concepts of corporate law for startup organizations. Codes were established for each category into which the content was divided. After analyzing the interview data, five main themes emerged regarding the legal challenges faced by startup businesses.

Table 2: Themes

| <b>Sub theme</b>                      | <b>Main theme</b>                            |
|---------------------------------------|--|
| Bureaucratic Red Tape                 | Legal Registration and Compliance Challenges |
| Lack of Clarity on Legal Requirements |  |
| Legal Documentation and Paperwork     |  |
| Unclear Tax Obligations               | Taxation and Financial Compliance            |
| Financial Record-Keeping Challenges   |  |
| Risk of Penalties for Non-compliance  |  |

|  |   |
|--|---|
| Lack of Knowledge about Intellectual Property          | <b>Intellectual Property Awareness and Protection</b> |
| Fear of Idea Theft                                     |   |
| Difficulty in Registering IP                           |   |
| High Cost of Legal Services                            | Access to Legal Resources and Support                 |
| Limited Legal Awareness and Resources                  |   |
| Need for Government and NGO Support                    | Legal Impacts on Business Growth and Sustainability   |
| Business Growth Stagnation Due to Legal Challenges     |   |
| Fear of Legal Penalties Preventing Business Innovation |   |

Source – Developed by the researcher, 2024

### Theme 1: Legal Registration and Compliance Challenges

Startup businesses were particularly concerned with navigating the complex and often time-consuming process of registering their companies and complying with local laws. Many entrepreneurs expressed challenges in understanding the legal requirements for business formation and the administrative hurdles they had to overcome to formally establish their businesses.

#### Sub themes

##### i. Bureaucratic Red Tape

A number of business owners pointed out that ineffective government systems were the cause of registration process delays.

*“I spent months just trying to get my business registered. Every time I submitted something, they told me something else was missing. It was exhausting and frustrating.”*

-Toffline Apparels, Pallekele-

##### ii. Lack of Clarity on Legal Requirements

Many business owners expressed that they were unclear about the various business structure types (Sole proprietorship, limited liability companies) and the related legal obligations.

*“I didn’t even know there were different types of companies I could register as. I just picked the one that seemed easiest, but now I’m realizing there are many legal responsibilities I didn’t know about.”* – Managing Director, Earthbound creations.

##### iii. Legal Documentation and Paperwork

The amount of paperwork needed for business registration and compliance was frequently mentioned by entrepreneurs as problem.

*“The paperwork is so overwhelming. We need a lot of legal documents that I had no idea about when I first started. Even simple things like opening a business bank account are complicated without the right documents.”* – Legal officer, Circle books.

## **Theme 2: Taxation and Financial Compliance**

### **Sub themes**

#### **i. Unclear Tax Obligations**

Startup businesses frequently find it difficult to understand the tax structure and requirements for proper filing.

*“I had no idea what taxes I should pay and how to file them. The tax laws seem so complicated, and I don’t have an accountant, so it’s hard to keep track of everything.”*

– Sripasha Lanka Foods, Kundasale

#### **ii. Financial Record-Keeping Challenges**

The significance of accurate book keeping and financial records for compliance purposes is not well understood.

*“In the beginning, I didn’t think much about keeping proper records, but I’ve learned that without them, it’s impossible to keep track of taxes and expenses.”*

– Circle books, Pallekele

#### **iii. Risk of Penalties**

Entrepreneurs voiced concerns about the risk of fines due to failure of understanding of tax laws.

*“I’m always afraid of getting into trouble with the tax authorities because I’m not sure if I’m doing everything correctly.”*

– Asgiriya Tyre house.

## **Theme 3: Intellectual Property Awareness and Protection**

### **Sub themes**

#### **i. Lack of Knowledge about IP**

Entrepreneurs frequently lacked knowledge about what intellectual property is and how to legally protect it.

*“I didn’t even know what intellectual property was when I started my business. I thought I owned everything I created, but now I realize that’s not the case.”*

– Circle books, Pallekele

#### **ii. Fear of idea Theft**

Business owners feared that their concepts would be stolen, but they were unsure how to prevent it legally.

*“We had a unique product, but I didn’t know how to protect it. Now, I’m worried someone will copy our idea and sell it cheaper.”*

– Earthbound creations, Peradeniya.

#### **iii. Difficulty in Registering IP**

Entrepreneurs stated that registering patents, copyrights, trademarks can be difficult and expensive

*“The process to register a trademark seemed too complicated and expensive, so I just gave up on it.”*

– Circle Books, Pallekele.

## **Theme 4: Access to Legal Resources and Support**

### **Sub themes**

#### **i. High Cost of Legal Services**

Due to the perception that legal fees were too expensive for small startup businesses many entrepreneurs had to handle corporate law alone.

*“Legal help is so expensive. I couldn’t afford to hire a lawyer, so I ended up trying to figure things out on my own.”* – Sriposha Foods Lanka.

#### **ii. Limited Legal Awareness**

Entrepreneurs often didn’t know where to find trustworthy legal consultants

*“I had no idea where to go for legal advice. It took me a long time to find someone who could explain things to me in simple terms.”* – Circle books.

#### **iii. Role of Government and NGOs**

Some entrepreneurs expressed the need for government to provide more easily accessible legal support.

*“It would be great if there were more workshops or programs to educate small business owners about legal requirements. I’ve had to learn everything the hard way.”* – Asgiriya Tyre house

## **Theme 5: Legal Impacts on Business Growth and Sustainability**

### **Sub themes**

#### **i. Business Growth Stagnation**

Legal issues frequently prevented entrepreneurs from expanding their businesses.

*“I couldn’t expand my business because I was always dealing with legal issues, like filing taxes late or figuring out intellectual property protections.”* – Sriposha Foods.

#### **ii. Fear of Legal Penalties**

Some entrepreneurs were discouraged from pursuing new business opportunities due to the fear of penalties for non compliance.

*“I’m always worried about getting sued or facing penalties, so I avoid taking risks that could potentially lead to legal trouble.”* – Circle books.

## **5. Discussion**

The results of the study are consistent with the findings of Moussetis & Cavenagh, (2021) who argue that legal environment is crucial to long term viability for businesses. The cumulative effect of legal challenges can seriously hinder a business's capacity to grow, attract investment, and establish long-term partnerships. Therefore, businesses that pay insufficient attention to legal matters expose themselves to the risk of losing their competitiveness and credibility. This study’s findings align with research by Rambhia et al., (2021) which claims that entrepreneurs specially in emerging economies frequently undervalue intellectual property protection. Startup businesses risk losing the competitive advantages essential to their survival and growth if they do not have adequate protection.

As a result, many startups in Sri Lanka are vulnerable to intellectual property theft due to a lack of awareness about the procedures involved in patenting, trademark registration, and copyright protection.

## **6. Implications**

There are significant implications arising from the slow and bureaucratic nature of the registration process. To make it easier for entrepreneurs to start their businesses, the Sri Lankan government must expedite the registration process, reduce delays, and develop a more effective, user-friendly system. Moreover, there is a lack of legal knowledge and education among entrepreneurs, as evidenced by their uncertainty about business formation and the excessive paperwork required for registration. Additionally, in terms of support for business growth and sustainability, entrepreneurs are often distracted by compliance issues and hesitant to pursue growth opportunities due to frequent legal challenges and fear of penalties. As a result, the potential for business growth is restricted and innovation is limited by the fear of legal consequences.

## **7. Recommendations**

For any startup to succeed, a variety of skills are required. Some researchers suggest that startup failure is inevitable if the necessary skills and knowledge are lacking, forcing the business to outsource key aspects of its operations. Therefore, if a startup lacks full awareness of relevant legislation, outsourcing the legal function may be the best option. In this regard, the academic sector holds significant potential, though it remains underutilized. Despite new laws being passed in Sri Lanka, it appears that many startup firms have not effectively applied much of the legislation to their operations. Thus, enhancing legal education and awareness for startup businesses is strongly recommended.

The legal requirements that affect startups, such as corporate governance compliance, tax obligations, and intellectual property protection, are often unclear to entrepreneurs. Startup founders could make more informed legal decisions if they had easy access to workshops and legal consultation services that help them understand their legal rights and responsibilities. To provide educational initiatives tailored to the needs of startups, collaboration between government agencies, academic institutions, and legal bodies would be highly beneficial.

In terms of digitalization and automation, authorities should work to reduce processing times and facilitate remote business incorporation. Additionally, establishing a one-stop shop for business registration—where entrepreneurs can manage all legal requirements (such as business registration, licenses, and tax registration) on a single platform—would be a valuable recommendation. Furthermore, to improve trade secret protection, relevant authorities should consider enacting specialized legislation to safeguard proprietary formulas, algorithms, and customer information.

## 8. Conclusion

The study highlights how Sri Lankan corporate law provides foundational support for startup businesses by recognizing various business structures, such as sole proprietorships, partnerships, and limited liability companies, which help reduce risks for those structuring their operations. The Partnership Ordinance of 1890 and the Companies Act offer significant legal frameworks for business registration and management, ensuring that the rights and obligations of owners are clearly defined. To better understand corporate law, including legal personality, employee rights, and corporate liabilities, the study references landmark cases such as *Salomon v. Salomon* and *Lee v. Lee's Air Farming Ltd.*

In conclusion, while Sri Lankan corporate law offers essential legal frameworks for new startup businesses to launch and operate, there are still several key gaps and real-world challenges. These obstacles including bureaucratic inefficiencies, weak intellectual property enforcement, and governance issues can stifle innovation and limit the ability of startups to grow. Sri Lanka needs to focus on streamlining and reforming legal procedures, strengthening intellectual property protection, and enhancing governance frameworks for new companies in order to create a more favorable environment for startup success. By addressing these issues, Sri Lanka can cultivate a more vibrant startup ecosystem that drives innovation, economic growth, and job creation.

## References

- Asiva Noor Rachmayani. (2015). *Application of Partnership ordinance in the businesses Title. 6.*
- Braun, V., & Clarke, V. (2008). Using thematic analysis in psychology, Qualitative Research in Psychology. *Journal of Chemical Information and Modeling*, 3(2), 77–101. <http://dx.doi.org/10.1191/1478088706qp063oa>
- Carter, N., Bryant-Lukosius, D., Dicenso, A., Blythe, J., & Neville, A. J. (2014). The use of triangulation in qualitative research. *Oncology Nursing Forum*, 41(5), 545–547. <https://doi.org/10.1188/14.onf.545-547>
- Court, S. (2009). *Sri Lanka Law Reports.*
- Crittenden, W. F., Crittenden, V. L., & Pierpont, A. (2015). Trade secrets: Managerial guidance for competitive advantage. *Business Horizons*, 58(6), 607–613. <https://doi.org/10.1016/j.bushor.2015.06.004>
- Davis, P. (2022). The Start . William James, June, 1-C1.P67. <https://doi.org/10.1093/oso/9780192847324.003.0001>
- Director-employee, T. H. E. (1897). *.the dual status.* 251–260.
- Fryer Jr, R. G., & Levitt, S. D. (2004). The causes and consequences of distinctively black names. *The Quarterly Journal of Economics*, 119(3), 767-805.
- Gaikwad, A. H., Prasarak, S., & Nagarpalika, S. (2023). a Study on Intellectual Property Rights and Its Significance for Business. *Amity Journal of Management, September*, 43–50. <https://doi.org/10.31620/ajm.1125>
- Giraud, E., Giudici, G., & Grilli, L. (2019). Entrepreneurship policy and the financing of young innovative companies: Evidence from the Italian Startup Act. *Research Policy*, 48(9), 103801. <https://doi.org/10.1016/j.respol.2019.05.010>



- Gutierrez, E. (2005). Geographic Indicators: A Unique European Perspective on Intellectual Property. *Hastings International and Comparative Law Review*, 29(1), 1–24.
- HMSO. (1890). *The Partnership Act 1890*. 1–18. <https://www.legislation.gov.uk/ukpga/Vict/53-54/39/contents>
- Hutchinson, T. (2016). The Doctrinal Method: Incorporating Interdisciplinary Methods in Reforming the Law. *Erasmus Law Review*, 38(3). <https://doi.org/10.5553/elr.000055>
- Jain, S. (2018). 'Growth of startup ecosystems in India'. *International Journal of Applied Research and Studies*, 2(12), 152-154.
- Jombo, F. (2018). *Current approaches to separate legal personality of a company in Ireland, the State of Delaware in the United States of America, and Nigeria*, 1–167 Available: <https://hdl.handle.net/10344/7012>
- Kitchenham, B., & Pfleeger, S. L. (2002). Principles of Survey Research Part 5: Populations and Samples. *ACM SIGSOFT Software Engineering Notes*, 27(5), 17. <http://portal.acm.org/citation.cfm?doid=571681.571686>
- Kopera, S., Wszendybył-Skulska, E., Cebulak, J., & Grabowski, S. (2018). Interdisciplinarity in Tech Startups Development - Case Study of “Unistartapp” Project. *Foundations of Management*, 10(1), 23–32. <https://doi.org/10.2478/fman-2018-0003>
- Korreck, S. (2019). *The Indian startup ecosystem: Drivers, challenges and pillars of support* (Observer Research Foundation Occasional Paper No. 210). Observer Research Foundation
- Laksmiana, I. N. H., & Permana, I. P. H. (2023). *Legal Challenges for Digital Startup Development in Indonesia*. 2(2).
- Lim, D. (2021). *How can startup leaders strategically disclose vulnerabilities during periods of crisis?* 1–44.
- Moussetis, R., & Cavenagh, T. (2021). Strategic, Legal, and Accounting Challenges for Social Enterprises. *J. of Business and Management*, 27(1), 23–52. <https://doi.org/10.1504/jbm.2021.141286>
- Ordinance, P. (1947). *CH: Prevention of frauds*. 121–123.
- Oshagbemi, T. (2017). Chapter 4. Research Design and Methodology. *Leadership and Management in Universities*, 67–95. <https://doi.org/10.1515/9783110853681-006>
- Property, I., No, A., Act, A. N., Provide, T. O., The, F. O. R., Relating, L. A. W., Intellectual, T. O., An, P., Procedure, E., The, F. O. R., Amend, T. O., Customs, T. H. E., High, T. H. E., Of, C., Provinces, T. H. E., Act, P., Provide, T. O., Matters, F. O. R., Therewithincidental, C., ... Directors, D. (2003). *09\_Sri Lanka Int Prop Act*. 36.
- Rambhia, V., Mehta, V., Mehta, R., Shah, R., & Patel, D. (2021). Intellectual Property Rights Management Using Blockchain. *Lecture Notes in Networks and Systems*, 190(June), 545–552. [https://doi.org/10.1007/978-981-16-0882-7\\_47](https://doi.org/10.1007/978-981-16-0882-7_47)

- Ranney, M. L., Meisel, Z. F., Choo, E. K., Garro, A. C., Sasson, C., & Morrow Guthrie, K. (2015). Interview-based Qualitative Research in Emergency Care Part II: Data Collection, Analysis and Results Reporting. *Academic Emergency Medicine*, 22(9), 1103–1112. <https://doi.org/10.1111/acem.12735>
- Rompho, N. (2018). Operational performance measures for startups. *Measuring Business Excellence*, 22(1), 31–41. <https://doi.org/10.1108/MBE-06-2017-0028>
- Saunders, M., Lewis, P., & Thornhill, A. (2019). *Research methods for business students* (8th ed.). Pearson Education Limited.
- Sri Lankan Government. (2010). *Companies Act, No. 07 of 2007*. 07, 13–15.
- Stel, A. van, Storey, D., & Thurik, R. (2006). The effect of business regulations on nascent and actual entrepreneurship. Papers on Entrepreneurship, Growth and Public Policy, edited by Group Entrepreneurship, Growth, and Public Policy, Max Planck Institute of Economics, Jena, Germany.
- Van Stel, A., Storey, D. J., & Thurik, A. R. (2007). The effect of business regulations on nascent and young business entrepreneurship. *Small Business Economics*, 28(2–3), 171–186. <https://doi.org/10.1007/s11187-006-9014-1>
- Velentzas, J., & Broni, -Georgia. (2010). Ethical Dimensions in the Conduct of Business: Business Ethics, Corporate Social Responsibility and the Law. the “Ethics in Business” As a Sense of Business Ethics. *International Conference On Applied Economics – ICOAE*, 795–817.
- Yang, D. (2013). Valuing Intellectual Property. *Understanding and Profiting from Intellectual Property*, October, 1–14. <https://doi.org/10.1057/9781137094667.0017>