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## Navigating Legal Challenges as a New Startup in Pakistan: An Analysis of the Regulatory Framework

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### **Abstract:**

*Starting a new business in Pakistan can be a challenging endeavor, especially when it comes to navigating the legal and regulatory framework. This research article examines the legal challenges faced by new startups in Pakistan and provides an analysis of the regulatory framework for startups in the country. Through a literature review, case studies, and interviews with industry experts, the article identifies the common legal challenges faced by startups in Pakistan, including obtaining necessary licenses and permits, complying with tax laws, and navigating labor regulations. Additionally, the article identifies best practices for navigating legal challenges in Pakistan, including working with legal experts, conducting thorough research, and building strong relationships with government agencies. The findings of this research provide valuable insights for startups seeking to establish themselves in Pakistan's competitive business environment, as well as policymakers seeking to improve the regulatory framework for startups in the country.*

**Key Words:** SECP, IPO, Company, Entrepreneurship, Startup, Legal Framework

### **1. Introduction:**

Starting a new business in Pakistan can be a challenging and complex process, especially when it comes to navigating the country's legal and regulatory framework. The World Bank's "Doing

Business 2020" report ranks Pakistan 108th out of 190 economies in terms of ease of doing business, indicating that entrepreneurs in the country face significant regulatory barriers. This research article examines the legal challenges faced by new startups in Pakistan and provides an analysis of the regulatory framework for startups in the country.

Previous studies have highlighted the legal and regulatory challenges faced by startups in Pakistan. For example, in their book *"The Pakistani Entrepreneur: A Comprehensive Guidebook for Starting and Running a Successful Business in Pakistan,"* authors Rizwan Hussain and M. Sadiq Soofi identify legal and regulatory compliance as a major challenge for entrepreneurs in the country. They note that obtaining the necessary licenses and permits, complying with tax laws, and navigating labor regulations can be time-consuming and costly for new startups.<sup>1</sup>

Similarly, in their article *"Entrepreneurial Ecosystem in Pakistan: Opportunities and Challenges,"* authors Khalil Ahmed and Muhammed Akbar note that while the Pakistani government has taken steps to improve the regulatory environment for startups, significant challenges remain. They identify intellectual property rights and protections as a particular area of concern, noting that the lack of strong legal protections can discourage innovation and investment in the country.

### **Objectives and Research Questions:**

The objective of this research article is to identify the legal challenges faced by new startups in Pakistan and to provide an analysis of the regulatory framework for startups in the country. Specifically, the research seeks to answer the following questions:

1. What are the common legal and regulatory challenges faced by startups in Pakistan?

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<sup>1</sup> M. Sadiq Soofi and Rizwan Hussain, "The Pakistani Entrepreneur: A Comprehensive Guidebook for Starting and Running a Successful Business in Pakistan," Startup Guide Pakistan, July 28, 2019, <https://startupguide.com.pk/>.

2. What is the regulatory framework for startups in Pakistan?
3. What are the best practices for navigating legal challenges in Pakistan, and how have successful startups in the country addressed these challenges?

**Significance of the study:**

The findings of this research will be valuable to entrepreneurs and policymakers in Pakistan, as well as to scholars and researchers interested in the regulation of startups and small businesses. By identifying the legal challenges faced by new startups in Pakistan and analyzing the regulatory framework for startups in the country, this research can inform efforts to improve the business environment and encourage entrepreneurship in Pakistan.

**2. Entrepreneurship:**

Entrepreneurship is a complex and multifaceted concept, with many definitions and interpretations. According to Schumpeter (1934), entrepreneurship is the process of "*creative destruction*," in which entrepreneurs introduce new products, services, and processes that disrupt and replace existing ones. This view emphasizes the importance of innovation and risk-taking in entrepreneurship.<sup>2</sup>

Another definition of entrepreneurship comes from Shane and Venkataraman (2000), who define it as "*the scholarly examination of how, by whom, and with what effects opportunities to create future goods and services are discovered, evaluated, and exploited*". This definition highlights the

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<sup>2</sup> Joseph A. Schumpeter, *Theory Economic Development* (Cambridge, Mass: Harvard University Press, 1934).

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importance of opportunity recognition and exploitation in entrepreneurship, as well as the role of individuals in the process.<sup>3</sup>

In his book "The Art of Possibility," Rosamund Stone Zander defines entrepreneurship as "the art of bringing new possibilities to life." This definition emphasizes the creative and visionary aspects of entrepreneurship, as well as the importance of perseverance and resilience in pursuing new ventures.<sup>4</sup>

### **3. Legal and Regulatory Challenges for the startups:**

According to previous research, startups in Pakistan face a range of legal and regulatory challenges that can make it difficult to establish and grow their businesses. Some common challenges include:

1. Obtaining licenses and permits: Starting a business in Pakistan requires obtaining a variety of licenses and permits, which can be time-consuming and expensive. This can include registering with the Securities and Exchange Commission of Pakistan, obtaining a national tax number, and registering with local authorities.<sup>5</sup>
2. Complying with tax laws: Pakistan's tax laws are complex and can be difficult for new entrepreneurs to navigate. Startups are required to register for sales tax and income tax, and failure to comply with these regulations can result in fines and penalties.<sup>6</sup>

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<sup>3</sup> Scott Shane and S. Venkataraman, "The Promise of Entrepreneurship as a Field of Research," *The Academy of Management Review* 25, no. 1 (2000): pp. 217-226, <https://doi.org/10.2307/259271>.

<sup>4</sup> Rosamund Stone Zander and Benjamin Zander, *The Art of Possibility: Transforming Professional and Personal Life* (Camberwell, Vic.: Penguin, 2002).

<sup>5</sup> See note 1

<sup>6</sup> Muhammad Akbar et al., "Entrepreneurial Ecosystem in Pakistan: Opportunities and Challenges.," in *Handbook of Research on Entrepreneurial Success and Its Impact on Regional Development*, ed. S.S. Ahmad (IGI Global, 2017), pp. 286-302.

3. Navigating labor regulations: Labor laws in Pakistan can be challenging for startups, particularly when it comes to hiring and firing employees. Employers are required to provide a range of benefits to employees, including social security, health insurance, and retirement benefits.<sup>7</sup>
4. Protecting intellectual property: Intellectual property protection is weak in Pakistan, which can make it difficult for startups to protect their ideas and innovations. This can discourage innovation and investment in the country.<sup>8</sup>

#### 4. Regulatory Framework for Startups in Pakistan:

The regulatory framework for startups in Pakistan includes several laws and regulations that govern various aspects of starting and operating a business. The key laws and regulations include:

- a. **Companies Act, 2017:** This law governs the formation, operation, and dissolution of companies in Pakistan. It outlines the requirements for registering a company, the duties and liabilities of directors and officers, and the procedures for shareholder meetings and voting.
- b. **Securities and Exchange Commission of Pakistan (SECP) Act, 1997:** This law establishes the SECP as the regulatory body responsible for regulating and supervising companies, securities, and other financial institutions in Pakistan. The SECP is responsible for enforcing laws related to securities and investments, as well as providing guidance to businesses on compliance.
- c. **Intellectual Property Organization of Pakistan (IPO-Pakistan) Act, 2012:** This law establishes the IPO-Pakistan as the regulatory body responsible for protecting intellectual

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<sup>7</sup> See note 1

<sup>8</sup> See note 6

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property rights in Pakistan. It outlines the procedures for registering patents, trademarks, and copyrights, as well as the penalties for infringement.

- d. **Income Tax Ordinance, 2001:** This law governs the taxation of businesses in Pakistan, including startups. It outlines the procedures for registering for tax, filing tax returns, and paying taxes. It also outlines the penalties for non-compliance.

#### **4.1.Companies Act, 2017:**

The Companies Act, 2017 is a law that governs the formation, operation, and dissolution of companies in Pakistan. The act was passed in 2017 and replaces the previous Companies Ordinance, 1984. The act provides a modern legal framework for companies, which is aligned with international best practices and aims to promote corporate governance and accountability.<sup>9</sup>

Under the Companies Act, 2017, companies are required to register with the Securities and Exchange Commission of Pakistan (SECP) and comply with various reporting and disclosure requirements. The act also outlines the duties and liabilities of directors and officers, and the procedures for shareholder meetings and voting.

One of the key features of the Companies Act, 2017 is the introduction of a new concept called a "single member company", which allows a company to be formed with only one shareholder. This is intended to make it easier for entrepreneurs to start and operate a business in Pakistan.<sup>10</sup>

Another important provision of the act is the requirement for companies to establish a code of conduct for their directors and officers, and to disclose this code on their website. This is intended to promote transparency and accountability in corporate governance.

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<sup>9</sup> See section 509, The company Act, 2017

<sup>10</sup> See section 2(65), *ibid* act.

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**4.2. SECP Act, 1997:**

The Securities and Exchange Commission of Pakistan (SECP) Act, 1997 is a law that establishes the SECP as the regulatory body responsible for regulating and supervising companies, securities, and other financial institutions in Pakistan. The SECP is responsible for enforcing laws related to securities and investments, as well as providing guidance to businesses on compliance.<sup>11</sup>

For startups, the SECP plays an important role in ensuring compliance with securities laws and regulations. This includes regulating the issuance and trading of securities, as well as ensuring that companies provide accurate and timely disclosures to investors.

Under the SECP Act, 1997, the SECP has the power to investigate and take enforcement action against companies that violate securities laws or engage in fraudulent activities. This is important for maintaining investor confidence in the startup ecosystem and protecting investors from fraud and misconduct.

The SECP also provides guidance and support to startups on compliance with securities laws and regulations. This includes publishing guidelines and regulations, as well as conducting training and awareness programs for businesses.

**4.3. IPO Act, 2012:**

The IPO Act, 2012 is a law that governs the process of initial public offerings (IPOs) in Pakistan. The act provides a regulatory framework for companies to raise capital through the sale of securities to the public, and sets out requirements for disclosure, approval, and registration of securities.

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<sup>11</sup> "Securities & Exchange Commission of Pakistan (SECP)," accessed March 11, 2021, <https://www.secp.gov.pk/>.

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For startups, the IPO Act provides a potential avenue for raising capital and accessing the public markets. However, the requirements for an IPO can be complex and time-consuming, and may not be suitable for all startups.

Under the IPO Act, companies must meet certain eligibility criteria and provide extensive disclosures to the Securities and Exchange Commission of Pakistan (SECP) and the public. This includes financial statements, business plans, and other information that investors need to make informed investment decisions.

The IPO Act also requires companies to obtain approval from the SECP and other regulatory bodies before they can proceed with an IPO. This includes approval from the relevant stock exchange, as well as compliance with securities laws and regulations.

Overall, the IPO Act provides a potential avenue for startups to raise capital and access the public markets. However, the process can be complex and may not be suitable for all startups.

## **5. Recommendations:**

Based on the research findings presented in this article, some key recommendations for startups in Pakistan facing legal challenges are:

- a. Seek legal advice and guidance early on: Startups should consult with legal experts early on in their development to ensure that they are aware of the legal and regulatory requirements they need to comply with, and to avoid potential legal issues down the road.



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- b. Establish good corporate governance practices: Establishing good corporate governance practices, such as a code of conduct for directors and officers, can help startups promote transparency and accountability, and build trust with investors and customers.
  - c. Stay up-to-date on changes in the legal and regulatory landscape: The legal and regulatory landscape in Pakistan is constantly evolving, and startups need to stay up-to-date on changes in laws and regulations that may impact their operations.
  - d. Consider alternative sources of funding: While an IPO may be a viable option for some startups, there are other sources of funding, such as venture capital, angel investors, and crowdfunding, that may be more suitable for startups at different stages of development.
  - e. Engage with regulators and policymakers: Startups should engage with regulators and policymakers to provide feedback on existing laws and regulations, and to advocate for changes that will promote a more supportive and enabling environment for startups in Pakistan.

These recommendations can help startups in Pakistan navigate the legal challenges they face and build sustainable and successful businesses.

## **6. The Conclusion.**

In conclusion, startups in Pakistan face a range of legal and regulatory challenges that can impact their ability to grow and thrive. This article has explored some of the key legal challenges faced by startups in Pakistan, including issues related to corporate governance, intellectual property, and securities laws.

Despite these challenges, there are opportunities for startups to succeed in Pakistan's rapidly growing economy. The government has taken steps to create a more supportive environment for

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startups, including through the introduction of the Companies Act, 2017, and the establishment of the SECP as a regulatory body.

To succeed in this environment, startups need to be proactive in seeking legal advice and guidance, and in establishing good corporate governance practices. They also need to stay up-to-date on changes in the legal and regulatory landscape and consider alternative sources of funding beyond traditional IPOs.

By taking these steps, startups in Pakistan can navigate the legal challenges they face and build sustainable and successful businesses that contribute to the growth and development of the country's economy.

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