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WHITE BLACK LEGAL is an open access, peer-reviewed and refereed journal provided dedicated to express views on topical legal issues, thereby generating a cross current of ideas on emerging matters. This platform shall also ignite the initiative and desire of young law students to contribute in the field of law. The erudite response of legal luminaries shall be solicited to enable readers to explore challenges that lie before law makers, lawyers and the society at large, in the event of the ever changing social, economic and technological scenario.

With this thought, we hereby present to you

# **TECH STARTUPS AND REGULATORY ARBITRAGE** **IN INDIA: A SOCIO-LEGAL STUDY OF** **COMPLIANCE AVOIDANCE AND SOCIAL COSTS**

AUTHORED BY - RAKSHIT SHARMA

## **Abstract**

India's booming tech startup ecosystem has redefined business and consumer landscapes through disruptive innovation, rapid digitisation, and scalable solutions. However, this growth has also exposed serious socio-legal concerns, primarily the practice of regulatory arbitrage. Regulatory arbitrage involves strategically exploiting loopholes, grey areas, or jurisdictional gaps in legal frameworks to bypass compliance obligations. While often portrayed as entrepreneurial agility, this paper argues that such practices create significant legal and social externalities.

Focusing on sectors like fintech, edtech, gig economy, and digital lending, this study explores how startups circumvent regulations relating to labour laws, consumer protection, data privacy, and financial accountability. By examining India's current regulatory ecosystem, including the Companies Act, SEBI norms, RBI directives, IT Act, and the Digital Personal Data Protection Act, 2023, the paper highlights the gaps that enable this phenomenon. It also examines the disproportionate impact on gig workers, low-income consumers, and public trust in law enforcement.

Using a socio-legal approach, the research underscores the need for adaptive regulatory frameworks, legal sandboxes, and strengthened compliance mechanisms. The paper concludes that sustainable innovation must align with democratic legal norms and social responsibility, especially in an increasingly digital economy.

## **Introduction**

India has emerged as one of the most dynamic startup ecosystems globally, with over 100,000 startups registered across various sectors, including fintech, edtech, health tech, logistics, and

mobility.<sup>1</sup> This explosive growth has been fuelled by technological innovation, policy incentives such as “Startup India,”<sup>2</sup> access to global venture capital, and an increasingly digital consumer base. The Indian startup economy contributes significantly to employment generation, financial inclusion, and digital transformation, making it a vital engine of the nation’s economic and technological future. However, the meteoric rise of tech startups has also revealed a critical challenge, regulatory arbitrage, where companies exploit loopholes or underdeveloped legal frameworks to avoid compliance obligations.<sup>3</sup>

Regulatory arbitrage, in essence, refers to the practice of capitalizing on regulatory differences or legal grey areas across sectors, jurisdictions, or business models.<sup>4</sup> While often justified in the name of innovation or competitive advantage, this practice raises serious socio-legal questions about corporate accountability, consumer safety, labour rights, and the effectiveness of the legal system in adapting to disruptive technologies. In the Indian context, where laws often lag behind innovation, startups have frequently operated in regulatory vacuums, circumventing essential safeguards related to financial regulation, data protection, labour laws, and consumer rights.<sup>5</sup>

The case of the gig economy illustrates this concern vividly. Platforms like Ola, Uber, Zomato, and Swiggy have redefined transportation and food delivery but have done so by classifying workers as “independent contractors,” thereby evading obligations such as minimum wage, provident fund, health insurance, or protection under the Industrial Disputes Act.<sup>6</sup> Similarly, fintech startups offering “Buy Now Pay Later” (BNPL) or microcredit services have often operated without falling under the purview of traditional non-banking financial company (NBFC) regulations, leading to unregulated debt accumulation and data exploitation.<sup>7</sup> In the

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<sup>1</sup> Startup India, Department for Promotion of Industry and Internal Trade, available at: <https://www.startupindia.gov.in/> (last visited June 24, 2025).

<sup>2</sup> Pratik Dattani, “India’s Start-Up Boom: The Big Picture,” *Financial Express*, April 10, 2023, available at: <https://www.financialexpress.com/business/indias-startup-boom-the-big-picture/> (last visited June 24, 2025).

<sup>3</sup> Chris Brummer, “Why Soft Law Dominates International Finance—and Not Trade,” 13 *Journal of International Economic Law* 623 (2010).

<sup>4</sup> Genschel Philipp and Thomas Plümpfer, “Regulatory Competition and International Cooperation,” 39 *Journal of European Public Policy* 569 (1997).

<sup>5</sup> Usha Ramanathan, “Aadhaar: A Biometric History of India’s 12-Digit Revolution,” 50(5) *Economic and Political Weekly* 33 (2015).

<sup>6</sup> V. Venkatesan, “Legal Hurdles in Gig Economy Regulation,” *Frontline*, March 25, 2022, available at: <https://frontline.thehindu.com/cover-story/legal-hurdles-in-gig-economy-regulation/article65249044.ece> (last visited June 24, 2025).

<sup>7</sup> Reserve Bank of India, Guidelines on Digital Lending, 2022, available at: <https://rbi.org.in/Scripts/NotificationUser.aspx?Id=12341> (last visited June 24, 2025).

edtech sector, platforms such as Byju's and Unacademy have faced criticism for aggressive sales practices, lack of content regulation, and misleading advertising.<sup>8</sup> These examples demonstrate how innovation is frequently accompanied by legal circumvention.

The social costs of such regulatory arbitrage are far-reaching. Consumers may be misled, overcharged, or left without adequate grievance redressal mechanisms. Workers may be denied labour protections and income security. Data privacy may be compromised in the absence of clear norms. Moreover, the unchecked power of startups operating outside the regulatory fold can lead to monopolistic behaviour, predatory pricing, and erosion of public trust in both markets and legal institutions. While the **Companies Act, 2013**,<sup>9</sup> the **Information Technology Act, 2000**,<sup>10</sup> the **Consumer Protection Act, 2019**,<sup>11</sup> and the **Digital Personal Data Protection Act, 2023**<sup>12</sup> aim to regulate various aspects of corporate and digital behaviour, their enforcement mechanisms are often fragmented, delayed, or reactive.

This research seeks to analyse the phenomenon of regulatory arbitrage within Indian tech startups from a socio-legal perspective. It explores how certain business models are deliberately designed to circumvent regulations and what implications this has for law, policy, and society at large. By examining key sectors such as fintech, edtech, and the gig economy, the paper will map patterns of compliance avoidance and evaluate their broader social consequences. The analysis will be grounded in relevant legal frameworks, including corporate law, financial regulations, labour codes, and data protection law.

Moreover, the study will assess the role of India's regulatory institutions, such as the **Reserve Bank of India (RBI)**, the **Securities and Exchange Board of India (SEBI)**,<sup>13</sup> the **Ministry of Corporate Affairs (MCA)**, and the Competition Commission of India (CCI)<sup>14</sup>, in addressing these challenges. It will also consider policy initiatives such as regulatory sandboxes, self-regulation, and ESG reporting as potential tools to bring disruptive innovation within the ambit of responsible governance. Comparative perspectives will be drawn from countries like

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<sup>8</sup> Shilpa Phadke, "EdTech and the Myth of Equal Access," *The India Forum*, February 3, 2023, available at: <https://www.theindiaforum.in/article/edtech-and-myth-equal-access> (last visited June 24, 2025).

<sup>9</sup> Companies Act, 2013, No. 18, Acts of Parliament, 2013 (India).

<sup>10</sup> Information Technology Act, 2000, No. 21, Acts of Parliament, 2000 (India).

<sup>11</sup> Consumer Protection Act, 2019, No. 35, Acts of Parliament, 2019 (India).

<sup>12</sup> Digital Personal Data Protection Act, 2023, No. 22, Acts of Parliament, 2023 (India).

<sup>13</sup> Securities and Exchange Board of India (SEBI), Ministry of Finance, Government of India, available at: <https://www.sebi.gov.in/> (last visited June 24, 2025).

<sup>14</sup> Competition Commission of India (CCI), available at: <https://www.cci.gov.in/> (last visited June 24, 2025).

Singapore, the United Kingdom, and the European Union, which have experimented with adaptive regulatory models and proactive enforcement.<sup>15</sup>

Importantly, this paper does not aim to vilify startups or stifle innovation. Rather, it emphasizes the need to balance innovation with legal accountability and social responsibility. The fundamental premise is that the law must not only catch up with innovation but also anticipate and shape it in a way that serves the public interest. In a rapidly digitizing economy, where the impact of corporate actions extends beyond profit margins to include user wellbeing, privacy, labour dignity, and market fairness, regulatory frameworks must evolve to be both flexible and firm.

Ultimately, this research contributes to the broader discourse on law and technology by highlighting the risks of unregulated innovation and proposing ways to harmonize legal frameworks with dynamic business models. The socio-legal approach employed here will evaluate not only what the law is but also what it ought to be in the context of a just and inclusive digital economy. Through this inquiry, the paper hopes to offer insights that are relevant to policymakers, legal scholars, regulatory authorities, entrepreneurs, and the general public.

## **Literature Review and Theoretical Framework**

### **Literature Review**

The rise of tech startups in India has brought regulatory arbitrage into sharp focus, particularly as new-age business models continue to challenge traditional legal frameworks. Regulatory arbitrage refers to the practice of exploiting gaps or inconsistencies in laws and regulations to gain a competitive edge without outright violating the law. While such practices may be legally permissible, they often raise ethical concerns and result in significant social costs.

International scholarship, especially in financial and tech sectors, has closely studied regulatory arbitrage. It has been described as a form of legal engineering used to reduce compliance burdens while maintaining operations within formal legality.<sup>16</sup> In the Indian startup context,

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<sup>15</sup> Douglas W. Arner, Janos Barberis, and Ross P. Buckley, "FinTech and RegTech: Impact on Regulators and Banks," 41 *Journal of Banking Regulation* 1 (2017).

<sup>16</sup> Chris Brummer, "Why Soft Law Dominates International Finance—and Not Trade," 13 *Journal of International Economic Law* 623 (2010).

arbitrage is primarily “voice-based” rather than “exit-based,” as startups often lobby for favourable interpretations or exploit legal uncertainty without shifting jurisdictions.<sup>17</sup>

Digital platforms have enabled newer forms of arbitrage. Scholars have emphasized how internet-based companies transcend borders, allowing them to avoid both national regulations and global governance frameworks.<sup>18</sup> In India, fintech platforms that offer credit without registering as NBFCs and edtech firms that provide unregulated online courses illustrate this trend. Some critiques of the digital infrastructure underpinning Aadhaar and financial technologies argue that techno-legal designs often enable compliance avoidance under the guise of innovation.<sup>19</sup>

Within Indian academic and policy literature, direct analysis of regulatory arbitrage is limited, though related themes have been studied. Some studies focus on how gig economy platforms like Ola and Swiggy classify workers as independent contractors to avoid compliance with labour laws.<sup>20</sup> Others highlight how startups strategically avoid statutory CSR obligations under the Companies Act, 2013 by staying below financial thresholds or exploiting definitional ambiguity.<sup>21</sup> These studies point to a broader trend of structured legal avoidance that calls for a unified regulatory response.

Policy documents have also acknowledged the issue. The NITI Aayog’s report on gig workers flags the use of corporate layering and informal work models to avoid long-term liability.<sup>22</sup> Similarly, the RBI’s digital lending guidelines recognize the dangers of unregulated credit disbursement via mobile apps.<sup>23</sup> Yet, despite these acknowledgments, the law lacks a unified framework to address regulatory arbitrage systematically across sectors.

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<sup>17</sup> Genschel Philipp and Thomas Plümper, “Regulatory Competition and International Cooperation,” 39 *Journal of European Public Policy* 569 (1997).

<sup>18</sup> Anupam Chander and Uyên P. Lê, “Data Nationalism,” 64 *Emory Law Journal* 677 (2015).

<sup>19</sup> Reetika Khera, “Aadhaar and the Infrastructural Power of the Indian State,” 19(2) *Contemporary South Asia* 123 (2020).

<sup>20</sup> Supriya Routh, “Worker (In)security in the Platform Economy: The Case of Ola and Uber Drivers in Kolkata,” 12(1) *Indian Journal of Labour Economics* 47 (2016).

<sup>21</sup> Shruti Bhushan, “Startup Responsibility and CSR Avoidance: A Critique of the Companies Act, 2013,” *National Law School of India Review*, Vol. 34, No. 2 (2022).

<sup>22</sup> NITI Aayog, “Report on India’s Gig and Platform Economy: Harnessing the Potential,” June 2022, available at: [https://www.niti.gov.in/sites/default/files/2022-06/Report\\_Gig\\_Economy\\_28062022.pdf](https://www.niti.gov.in/sites/default/files/2022-06/Report_Gig_Economy_28062022.pdf) (last visited June 24, 2025).

<sup>23</sup> Reserve Bank of India, Guidelines on Digital Lending, 2022, available at: <https://rbi.org.in/Scripts/NotificationUser.aspx?Id=12341> (last visited June 24, 2025).

Comparative jurisdictions offer some guidance. The European Union's **General Data Protection Regulation (GDPR)**<sup>24</sup> and **Digital Services Act (DSA)**<sup>25</sup> seek to pre-empt arbitrage by clearly defining corporate responsibilities. Singapore's regulatory sandbox model provides controlled environments for innovation while maintaining oversight, offering a balance between flexibility and legal clarity.<sup>26</sup>

## Theoretical Framework

To analyse this issue from a socio-legal standpoint, this paper integrates three major theoretical lenses: regulatory theory, legal pluralism, and social justice theory.

### 1. Regulatory Theory

Regulatory theory emphasizes that regulation should promote innovation while also ensuring fairness, safety, and market integrity.<sup>27</sup> In the Indian startup context, many firms justify regulatory avoidance as necessary for innovation and scale. However, regulatory theory warns that such a lack of oversight can lead to market failures, public harm, and erosion of trust. The idea of responsive regulation, where oversight intensity varies depending on the behaviour and risk profile of the entity, can be a valuable model. It suggests that startups should be encouraged to innovate, but with mechanisms that respond to their conduct and impact on society.

### 2. Legal Pluralism

Legal pluralism explores how multiple legal systems coexist in a single society. This is particularly relevant in India's startup ecosystem, where formal law (e.g., Companies Act or IT Act) often operates alongside platform terms of service, self-regulatory codes, and informal norms. Startups frequently design internal governance systems, like grievance redressal cells or privacy policies, that substitute formal legal compliance with soft-law alternatives. Legal pluralism helps explain why regulatory arbitrage thrives, not merely because of absent laws, but because of parallel systems that dilute enforcement and accountability.

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<sup>24</sup> European Union, "General Data Protection Regulation (GDPR)," available at: <https://gdpr.eu/> (last visited June 24, 2025).

<sup>25</sup> European Commission, "The Digital Services Act," available at: <https://digital-strategy.ec.europa.eu/en/policies/digital-services-act> (last visited June 24, 2025).

<sup>26</sup> Douglas W. Arner, Janos Barberis, and Ross P. Buckley, "FinTech and RegTech: Impact on Regulators and Banks," 41 *Journal of Banking Regulation* 1 (2017).

<sup>27</sup> Robert Baldwin, Martin Cave and Martin Lodge, *Understanding Regulation: Theory, Strategy, and Practice* (2nd ed., Oxford University Press, 2012).

### 3. Social Justice Theory

Social justice theory insists that laws and markets must be evaluated not only by their efficiency but by their impact on human dignity, equity, and inclusion.<sup>28 29</sup> In the context of regulatory arbitrage, the social harms are often invisible in economic statistics but very real for vulnerable populations. Gig workers lack social security, low-income borrowers fall into debt traps, and rural students invest in unrecognized courses, all because companies evade legal duties. A social justice lens helps prioritize the protection of these stakeholders and evaluates arbitrage not just as a legal strategy but as a form of structural inequality.

### Regulatory Arbitrage in the Indian Startup Ecosystem

India's tech startup ecosystem has experienced remarkable growth over the past decade, disrupting traditional business models across sectors like finance, education, transportation, and healthcare.<sup>30</sup> While these startups have contributed significantly to job creation and digital inclusion, many have also taken advantage of regulatory loopholes and legal ambiguities to scale rapidly while avoiding compliance obligations.<sup>31</sup> This practice, known as regulatory arbitrage, has become increasingly common across the ecosystem.

A prominent example is the gig economy, where platforms such as Ola and Uber have classified drivers as "independent contractors" rather than employees.<sup>32</sup> This strategic classification allows them to evade labour law requirements, including minimum wages, social security benefits, health insurance, and protections under the Industrial Disputes Act, 1947. Although the platforms exercise significant control over working hours, pricing, and penalties, factors traditionally associated with employer-employee relationships, they escape liability by leveraging legal gaps.<sup>33</sup> Despite court interventions in several jurisdictions worldwide, India still lacks a clear legal framework to regulate platform labour effectively.<sup>34</sup>

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<sup>28</sup> Amartya Sen, *Development as Freedom* (Oxford University Press, 1999).

<sup>29</sup> Martha C. Nussbaum, *Creating Capabilities: The Human Development Approach* (Harvard University Press, 2011).

<sup>30</sup> Startup India, *Action Plan Report*, Department for Promotion of Industry and Internal Trade, available at: <https://www.startupindia.gov.in/> (last visited June 24, 2025).

<sup>31</sup> Chris Brummer, *Why Soft Law Dominates International Finance—and Not Trade*, 13 J. Int'l Econ. L. 623 (2010).

<sup>32</sup> Supriya Routh, *Worker (In)security in the Platform Economy: The Case of Ola and Uber Drivers in Kolkata*, 12(1) Indian J. Lab. Econ. 47 (2016).

<sup>33</sup> V. Venkatesan, *Legal Hurdles in Gig Economy Regulation*, *Frontline*, March 25, 2022, available at: <https://frontline.thehindu.com/cover-story/legal-hurdles-in-gig-economy-regulation/article65249044.ece> (last visited June 24, 2025).

<sup>34</sup> Report of the Expert Committee on Platform Workers, Ministry of Labour & Employment, Government of India (2021).

In the fintech sector, startups like Paytm Postpaid, LazyPay, and others have offered Buy Now, Pay Later (BNPL) services without registering as Non-Banking Financial Companies (NBFCs).<sup>35</sup> Instead, they operate through partnerships with shadow lenders or regulated entities, allowing them to offer credit-like products without being directly accountable to the Reserve Bank of India's (RBI) stringent norms.<sup>36</sup> This arbitrage has led to growing concerns around predatory lending, absence of transparent grievance redressal, and misuse of user data. In response, the RBI issued guidelines in 2022 to tighten oversight,<sup>37</sup> but many newer apps continue to circumvent these norms through innovative structuring.<sup>38</sup>

In edtech, firms like Byju's and Unacademy have marketed educational content and certifications without regulatory approval or academic recognition.<sup>39</sup> By operating outside the purview of bodies like the University Grants Commission (UGC) or the All-India Council for Technical Education (AICTE), these platforms have designed offerings that escape quality regulation and accountability.<sup>40</sup> Aggressive sales practices, refund denial, and unverified claims have led to consumer grievances and even litigation,<sup>41</sup> but the lack of specific regulations for online education has enabled these companies to flourish largely unchecked.

Another area rife with arbitrage is data governance. Startups collect, store, and monetize vast amounts of personal data, often without clear consent or user awareness.<sup>42</sup> Before the enactment of the Digital Personal Data Protection Act, 2023, data privacy laws in India were scattered across the Information Technology Act, 2000, and sectoral guidelines.<sup>43</sup> Many startups used this fragmented regime to bypass data minimization principles, use dark patterns, or share data with third parties. Even now, enforcement remains weak, and compliance structures are evolving slowly.<sup>44</sup>

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<sup>35</sup> Smriti Sharma, *BNPL Firms and Regulatory Grey Areas*, *The Hindu BusinessLine*, February 15, 2023, available at: <https://www.thehindubusinessline.com/> (last visited June 24, 2025).

<sup>36</sup> Reserve Bank of India, *Master Directions on NBFCs*, 2022, available at: <https://rbi.org.in> (last visited June 24, 2025).

<sup>37</sup> Reserve Bank of India, *Guidelines on Digital Lending*, 2022, available at: <https://rbi.org.in/Scripts/NotificationUser.aspx?Id=12341> (last visited June 24, 2025).

<sup>38</sup> Pratik Bhattacharya, *Fintech Apps Find New Routes Amid Lending Curbs*, *LiveMint*, May 1, 2023, available at: <https://www.livemint.com/> (last visited June 24, 2025).

<sup>39</sup> Shilpa Phadke, *EdTech and the Myth of Equal Access*, *The India Forum*, February 3, 2023, available at: <https://www.theindiaforum.in/article/edtech-and-myth-equal-access> (last visited June 24, 2025).

<sup>40</sup> University Grants Commission, *UGC Online Education Guidelines*, 2022, available at: <https://www.ugc.gov.in/> (last visited June 24, 2025).

<sup>41</sup> Bar & Bench, *Consumer Court Orders Refund Against EdTech Firm*, March 2023, available at: <https://www.barandbench.com/> (last visited June 24, 2025).

<sup>42</sup> Reetika Khera, *Aadhaar and the Infrastructural Power of the Indian State*, 19(2) *Contemp. S. Asia* 123 (2020).

<sup>43</sup> Information Technology Act, 2000, No. 21, Acts of Parliament, 2000 (India).

<sup>44</sup> Digital Personal Data Protection Act, 2023, No. 22, Acts of Parliament, 2023 (India).

These examples demonstrate that regulatory arbitrage is not an isolated occurrence but a systemic feature of India's tech-driven growth model.<sup>45</sup> While the state's responses, such as RBI's fintech norms, the Data Protection Act, and new labour codes, indicate growing awareness, enforcement lags behind innovation. Without a coordinated and forward-looking regulatory strategy, arbitrage will continue to flourish, often at the expense of consumers, workers, and public trust.<sup>46</sup>

### Legal and Regulatory Gaps

The Indian legal system, though equipped with a broad range of regulatory instruments, often struggles to keep pace with the rapid innovation and evolving business models of tech startups.<sup>47</sup> The resulting regulatory gaps enable startups to exploit legal grey areas, operate with limited oversight, and avoid compliance costs, giving rise to widespread regulatory arbitrage.<sup>48</sup> One major challenge is the fragmented and sector-specific nature of Indian regulation.<sup>49</sup> Startups operating across sectors often fall between the jurisdictional cracks of multiple regulatory bodies. For instance, a fintech startup offering wallet services may come under the RBI's purview, while one offering investment advisory might fall under SEBI.<sup>50</sup> This fragmentation creates confusion and encourages startups to structure their operations in ways that avoid falling squarely under any one regulator's authority.<sup>51</sup>

The Companies Act, 2013, though robust in setting up governance structures for companies, lacks provisions specifically addressing platform-based or gig economy firms.<sup>52</sup> Many startups strategically keep their financials below CSR or audit thresholds to avoid additional scrutiny, while others take advantage of opaque shareholding or offshore incorporation to obscure

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<sup>45</sup> Arghya Sengupta & Karan Gulati, *Regulatory Arbitrage in the Indian Tech Sector*, Vidhi Centre for Legal Policy, Working Paper (2021).

<sup>46</sup> Niti Aayog, *Draft National Strategy on Artificial Intelligence*, Discussion Paper (2018), available at: <https://www.niti.gov.in/> (last visited June 24, 2025).

<sup>47</sup> Arghya Sengupta & Karan Gulati, *Regulatory Arbitrage in the Indian Tech Sector*, Vidhi Centre for Legal Policy, Working Paper (2021).

<sup>48</sup> Chris Brummer, *Why Soft Law Dominates International Finance—and Not Trade*, 13 J. Int'l Econ. L. 623 (2010).

<sup>49</sup> Rishab Bailey, *Fragmented Regulation and the Platform Economy in India*, *The Leap Blog*, June 2021, available at: <https://www.theleapjournal.org/> (last visited June 24, 2025).

<sup>50</sup> Reserve Bank of India, *Master Direction – Prepaid Payment Instruments*, available at: <https://rbi.org.in/> (last visited June 24, 2025).

<sup>51</sup> SEBI, *Regulatory Framework for Investment Advisers*, 2020, available at: <https://www.sebi.gov.in/> (last visited June 24, 2025).

<sup>52</sup> Companies Act, 2013, No. 18, Acts of Parliament, 2013 (India).

accountability.<sup>53</sup> Similarly, the labour laws, including the new Labour Codes, remain unclear on the status of platform workers, enabling companies to treat them as independent contractors and evade obligations like PF, ESI, and gratuity.<sup>54</sup>

The Information Technology Act, 2000, which governs digital operations and cyber practices, is outdated in its scope and enforcement capacity.<sup>55</sup> Though the Digital Personal Data Protection Act, 2023 is a significant step forward, its implementation remains nascent.<sup>56</sup> Startups have often exploited the lack of comprehensive data protection by engaging in aggressive data harvesting, targeted advertising, and unauthorized sharing of user information.<sup>57</sup>

In education, edtech platforms bypass recognition requirements by avoiding formal degree issuance.<sup>58</sup> The University Grants Commission (UGC) and AICTE have no clear regulatory mechanisms for online-only platforms offering uncertified learning content.<sup>59</sup> Similarly, telemedicine startups have used ambiguities in health data handling norms to operate in grey areas.<sup>60</sup>

Moreover, enforcement is hindered by resource limitations, technological illiteracy among regulators, and the absence of cross-sectoral coordination.<sup>61</sup> As a result, laws are reactive rather than anticipatory, enabling tech startups to innovate faster than the legal system can respond.<sup>62</sup> To address these issues, India needs an integrated, adaptive regulatory approach capable of recognizing hybrid business models, closing legal loopholes, and ensuring accountability without stifling innovation.<sup>63</sup>

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<sup>53</sup> Shruti Bhushan, *Startup Responsibility and CSR Avoidance: A Critique of the Companies Act, 2013*, Nat'l L. Sch. India Rev., Vol. 34, No. 2 (2022).

<sup>54</sup> Code on Social Security, 2020, No. 36, Acts of Parliament, 2020 (India).

<sup>55</sup> Information Technology Act, 2000, No. 21, Acts of Parliament, 2000 (India).

<sup>56</sup> Digital Personal Data Protection Act, 2023, No. 22, Acts of Parliament, 2023 (India).

<sup>57</sup> Reetika Khera, *Aadhaar and the Infrastructural Power of the Indian State*, 19(2) Contemp. S. Asia 123 (2020).

<sup>58</sup> Shilpa Phadke, *EdTech and the Myth of Equal Access*, *The India Forum*, February 3, 2023, available at: <https://www.theindiaforum.in/> (last visited June 24, 2025).

<sup>59</sup> University Grants Commission, *Guidelines for Online Learning Platforms*, 2022, available at: <https://www.ugc.gov.in/> (last visited June 24, 2025).

<sup>60</sup> Ministry of Health and Family Welfare, *Telemedicine Practice Guidelines*, 2020, available at: <https://www.mohfw.gov.in/> (last visited June 24, 2025).

<sup>61</sup> NITI Aayog, *National Strategy on Artificial Intelligence*, 2018, available at: <https://www.niti.gov.in/> (last visited June 24, 2025).

<sup>62</sup> Smriti Sharma, *Laws Can't Catch Up with Startups*, *The Hindu BusinessLine*, May 15, 2023, available at: <https://www.thehindubusinessline.com/> (last visited June 24, 2025).

<sup>63</sup> Arner Douglas W., Janos Barberis & Ross P. Buckley, *FinTech and RegTech: Impact on Regulators and Banks*, 41 J. Bank. Regul. 1 (2017).

## Social Costs of Regulatory Arbitrage

While regulatory arbitrage may provide startups with short-term advantages such as faster scaling, reduced compliance costs, and market disruption, it often imposes disproportionate social costs on workers, consumers, and public institutions.<sup>64</sup> These costs are not always visible in economic data but are deeply embedded in the daily realities of those affected by unregulated or loosely regulated digital services.<sup>65</sup>

One of the most affected groups are gig and platform workers. Companies like Ola, Uber, Swiggy, and Zomato benefit from classifying workers as independent contractors to avoid offering social security, job security, or occupational health protections.<sup>66</sup> This leaves lakhs of gig workers without minimum wage guarantees, accident insurance, or grievance redressal mechanisms.<sup>67</sup> In times of economic stress, such as the COVID-19 pandemic, these workers bore the brunt of income loss without institutional support.<sup>68</sup>

In the financial sector, users of unregulated fintech platforms often face predatory lending practices.<sup>69</sup> Many borrowers, particularly low-income and digitally less literate individuals, are enticed into quick credit schemes without full knowledge of interest rates, repayment terms, or penalties.<sup>70</sup> Harassment over defaults, misuse of contact data, and the psychological burden of debt have led to severe consequences, including reported suicides.<sup>71</sup> The absence of accountability mechanisms exacerbates the problem.<sup>72</sup>

In edtech, consumers, often parents or first-generation learners, invest in courses or coaching services without knowing whether the content is accredited, up to educational standards, or

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<sup>64</sup> Chris Brummer, *Why Soft Law Dominates International Finance—and Not Trade*, 13 J. Int'l Econ. L. 623 (2010).

<sup>65</sup> Arghya Sengupta & Karan Gulati, *Regulatory Arbitrage in the Indian Tech Sector*, Vidhi Centre for Legal Policy, Working Paper (2021).

<sup>66</sup> Supriya Routh, *Worker (In)security in the Platform Economy: The Case of Ola and Uber Drivers in Kolkata*, 12(1) Indian J. Lab. Econ. 47 (2016).

<sup>67</sup> V. Venkatesan, *Legal Hurdles in Gig Economy Regulation*, *Frontline*, March 25, 2022, available at: <https://frontline.thehindu.com/> (last visited June 24, 2025).

<sup>68</sup> NITI Aayog, *India's Gig Economy During the Pandemic*, Policy Brief, 2021, available at: <https://www.niti.gov.in/> (last visited June 24, 2025).

<sup>69</sup> Reserve Bank of India, *Guidelines on Digital Lending*, 2022, available at: <https://rbi.org.in/> (last visited June 24, 2025).

<sup>70</sup> Smriti Sharma, *Predatory Lending in India's Digital Lending Boom*, *The Hindu BusinessLine*, April 10, 2023.

<sup>71</sup> Scroll Staff, *Suicides Linked to Digital Lending Harassment in India*, *Scroll.in*, January 2023, available at: <https://scroll.in/> (last visited June 24, 2025).

<sup>72</sup> Reetika Khera, *Aadhaar and the Infrastructural Power of the Indian State*, 19(2) *Contemp. S. Asia* 123 (2020).

even refundable.<sup>73</sup> Misleading advertisements and coercive sales tactics have caused financial distress and eroded trust in online education.<sup>74</sup> The lack of regulatory scrutiny over such practices harms both learners and the credibility of digital education.<sup>75</sup>

From a data privacy perspective, unregulated collection and monetization of user data by tech startups create long-term risks of identity theft, targeted manipulation, and surveillance.<sup>76</sup> Users rarely have informed consent over how their data is processed or sold.<sup>77</sup> These practices, while profitable for companies, undermine user autonomy and democratic accountability.<sup>78</sup>

Lastly, unchecked regulatory arbitrage contributes to a trust deficit in public institutions.<sup>79</sup> When citizens see companies operating beyond the reach of the law, it weakens the perceived legitimacy of the legal system and reduces the incentive for law-abiding entrepreneurship.<sup>80</sup> In sum, regulatory arbitrage in the tech sector imposes serious and often invisible social costs, particularly on the most vulnerable segments of society, necessitating urgent legal and policy intervention.<sup>81</sup>

## Comparative Jurisprudence

Regulatory arbitrage in tech ecosystems is not unique to India. Several jurisdictions around the world have encountered similar challenges and developed innovative legal responses to balance innovation with accountability.<sup>82</sup> Comparative analysis provides valuable insights into how adaptive regulation can reduce the negative externalities of unchecked digital growth.<sup>83</sup>

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<sup>73</sup> Shilpa Phadke, *EdTech and the Myth of Equal Access*, *The India Forum*, February 3, 2023, available at: <https://www.theindiaforum.in/> (last visited June 24, 2025).

<sup>74</sup> Bar & Bench, *Consumer Court Orders Refund Against EdTech Firm*, March 2023, available at: <https://www.barandbench.com/> (last visited June 24, 2025).

<sup>75</sup> UGC, *Guidelines for Online Learning Platforms*, 2022, available at: <https://www.ugc.gov.in/> (last visited June 24, 2025).

<sup>76</sup> Digital Personal Data Protection Act, 2023, No. 22, Acts of Parliament, 2023 (India).

<sup>77</sup> Reetika Khera, *The Dangers of Digital Profiling*, *Indian Express*, March 2022.

<sup>78</sup> Mozilla Foundation, *Privacy Not Included: Apps and Data Misuse*, 2023, available at: <https://foundation.mozilla.org/> (last visited June 24, 2025).

<sup>79</sup> NITI Aayog, *National Strategy on Artificial Intelligence*, 2018, available at: <https://www.niti.gov.in/> (last visited June 24, 2025).

<sup>80</sup> Rishab Bailey, *Rebuilding Trust in Digital Regulation*, *The Leap Blog*, May 2023.

<sup>81</sup> Douglas W. Arner, Janos Barberis & Ross P. Buckley, *FinTech and RegTech: Impact on Regulators and Banks*, 41 *J. Bank. Regul.* 1 (2017).

<sup>82</sup> Chris Brummer, *Regulatory Arbitrage and the International System*, 14(1) *Chi. J. Int'l L.* 243 (2013).

<sup>83</sup> Arghya Sengupta & Karan Gulati, *Regulatory Arbitrage in the Indian Tech Sector*, Vidhi Centre for Legal Policy, Working Paper (2021).

The European Union has adopted a proactive regulatory stance with frameworks like the General Data Protection Regulation (GDPR) and the Digital Services Act (DSA).<sup>84</sup> The GDPR mandates strict data protection norms, including user consent, data minimization, and the right to be forgotten.<sup>85</sup> Non-compliant companies face heavy penalties, including fines based on global revenue.<sup>86</sup> The DSA, on the other hand, imposes obligations on online platforms to remove illegal content, enhance transparency, and disclose algorithmic decision-making processes.<sup>87</sup> These regulations reflect a rights-based, user-centric approach that aims to preempt arbitrage before harm occurs.<sup>88</sup>

Singapore has become a global model for regulatory innovation through its regulatory sandbox approach.<sup>89</sup> Administered by the Monetary Authority of Singapore (MAS), this mechanism allows fintech startups to test new products in a controlled legal environment under limited regulatory requirements.<sup>90</sup> The approach encourages innovation while allowing regulators to understand emerging risks and develop responsive legal frameworks.<sup>91</sup>

In the United States, although regulation is fragmented, recent efforts by the Federal Trade Commission (FTC) and Securities and Exchange Commission (SEC) reflect growing scrutiny of deceptive practices in data use, gig economy classification, and startup disclosures during IPOs.<sup>92</sup> High-profile enforcement actions against companies like Uber and Facebook signal a shift toward stricter accountability.<sup>93</sup>

These comparative examples highlight the importance of forward-looking, flexible regulation

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<sup>84</sup> Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the Protection of Natural Persons with regard to the Processing of Personal Data and on the Free Movement of such Data (General Data Protection Regulation), OJ L 119/1.

<sup>85</sup> *Ibid.*, Art. 6 and 17.

<sup>86</sup> *Ibid.*, Art. 83.

<sup>87</sup> European Commission, *Digital Services Act: Ensuring a Safe and Accountable Online Environment*, available at: <https://ec.europa.eu/> (last visited June 24, 2025).

<sup>88</sup> Paul de Hert and Vagelis Papakonstantinou, *The New General Data Protection Regulation: Still a Sound System for the Protection of Individuals?*, 32(2) *Comp. L. & Sec. Rev.* 179 (2016).

<sup>89</sup> Monetary Authority of Singapore, *FinTech Regulatory Sandbox Guidelines*, available at: <https://www.mas.gov.sg/> (last visited June 24, 2025).

<sup>90</sup> *Ibid.*

<sup>91</sup> Douglas W. Arner, Janos Barberis & Ross P. Buckley, *FinTech, RegTech and the Reconceptualization of Financial Regulation*, 37 *Nw. J. Int'l L. & Bus.* 371 (2017).

<sup>92</sup> Federal Trade Commission, *Gig Economy Enforcement Reports*, available at: <https://www.ftc.gov/> (last visited June 24, 2025).

<sup>93</sup> Securities and Exchange Commission, *Public Disclosures and Enforcement Actions 2023*, available at: <https://www.sec.gov/> (last visited June 24, 2025).

tailored to the digital economy.<sup>94</sup> India can draw from these models to develop integrated policies that promote responsible innovation while protecting consumer rights, labour dignity, and democratic values.<sup>95</sup>

## Recommendations

To address the growing issue of regulatory arbitrage by tech startups in India, a multi-pronged approach is essential.<sup>96</sup> First, India should consider adopting a regulatory sandbox framework across sectors, not just in fintech, allowing startups to innovate within a controlled legal environment while regulators monitor risks and impact.<sup>97</sup> This ensures flexibility without compromising oversight.<sup>98</sup>

Second, there is a need for a centralized digital regulator or coordination body to streamline jurisdiction between agencies like RBI, SEBI, MCA, and MeitY.<sup>99</sup> A unified regulatory approach will help close gaps exploited by hybrid business models that fall between sectoral regulators.<sup>100</sup>

Third, the government should strengthen enforcement mechanisms by investing in regulatory capacity-building, especially in technology-related areas.<sup>101</sup> Regulators must be equipped with the technical knowledge to assess AI, data practices, and digital consumer harms.<sup>102</sup>

Fourth, the Companies Act, 2013 and labour codes should be amended to clearly define obligations for platform-based and gig economy firms, ensuring that worker rights and social

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<sup>94</sup> Julia Black, *Paradoxes and Failures: 'New Governance' Techniques and the Financial Crisis*, 75 Mod. L. Rev. 1037 (2012).

<sup>95</sup> NITI Aayog, *Strategy for New India @75*, 2018, available at: <https://www.niti.gov.in/> (last visited June 24, 2025).

<sup>96</sup> Chris Brummer, *Regulatory Arbitrage and the International System*, 14(1) Chi. J. Int'l L. 243 (2013).

<sup>97</sup> Monetary Authority of Singapore, *FinTech Regulatory Sandbox Guidelines*, available at: <https://www.mas.gov.sg/> (last visited June 24, 2025).

<sup>98</sup> Douglas W. Arner, Janos Barberis & Ross P. Buckley, *FinTech, RegTech and the Reconceptualization of Financial Regulation*, 37 Nw. J. Int'l L. & Bus. 371 (2017).

<sup>99</sup> Rishab Bailey, *Regulating India's Digital Economy: Towards an Integrated Regulator*, *The Leap Blog*, July 2022, available at: <https://www.theleapjournal.org/> (last visited June 24, 2025).

<sup>100</sup> NITI Aayog, *Strategy for New India @75*, 2018, available at: <https://www.niti.gov.in/> (last visited June 24, 2025).

<sup>101</sup> Julia Black, *Enrolling Actors in Regulatory Systems: Examples from UK Financial Services Regulation*, 29(1) Pub. L. 63 (2005).

<sup>102</sup> Reetika Khera, *Digital Governance and the Future of State Regulation*, *Economic & Political Weekly*, Vol. 58, No. 12 (2023).

security are legally protected.<sup>103</sup>

Finally, mandatory ESG and data ethics reporting for startups above a certain threshold should be introduced, promoting transparency and accountability in corporate conduct.<sup>104</sup>

Together, these measures can help create a balanced legal ecosystem where innovation thrives without eroding public trust or social welfare.<sup>105</sup>

## Conclusion

The Indian startup ecosystem has become a symbol of economic dynamism, technological advancement, and entrepreneurial energy.<sup>106</sup> However, the rapid pace of digital innovation has outstripped the ability of traditional regulatory frameworks to respond in a timely and effective manner.<sup>107</sup> This mismatch has created fertile ground for regulatory arbitrage, where tech startups strategically exploit legal loopholes, jurisdictional overlaps, and ambiguous definitions to avoid compliance, reduce liability, and maximize profits.<sup>108</sup> While often defended in the name of innovation and scale, such practices carry substantial social and legal consequences.<sup>109</sup> This paper has demonstrated that regulatory arbitrage is not an isolated or accidental occurrence but a systemic feature of India's startup-driven growth.<sup>110</sup> Sectors such as the gig economy, fintech, and edtech have shown how startups bypass labour laws, financial regulations, and consumer protections by relying on informal classifications, opaque business models, and underdeveloped legal frameworks.<sup>111</sup> The resulting social costs, ranging from worker precarity and consumer harm to erosion of data privacy and public trust, disproportionately affect vulnerable populations with limited access to redress or bargaining power.<sup>112</sup>

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<sup>103</sup> Code on Social Security, 2020, No. 36, Acts of Parliament, 2020 (India); Companies Act, 2013, No. 18, Acts of Parliament, 2013 (India).

<sup>104</sup> Ministry of Corporate Affairs, *Report of the Committee on Business Responsibility Reporting*, 2020, available at: <https://www.mca.gov.in/> (last visited June 24, 2025).

<sup>105</sup> Arghya Sengupta & Karan Gulati, *Regulatory Arbitrage in the Indian Tech Sector*, Vidhi Centre for Legal Policy, Working Paper (2021).

<sup>106</sup> Ministry of Commerce & Industry, *Startup India Action Plan*, Government of India, 2016.

<sup>107</sup> Rishab Bailey, *Regulating India's Digital Economy: Towards an Integrated Regulator*, *The Leap Blog*, July 2022.

<sup>108</sup> Chris Brummer, *Regulatory Arbitrage and the International System*, 14(1) *Chi. J. Int'l L.* 243 (2013).

<sup>109</sup> Arghya Sengupta & Karan Gulati, *Regulatory Arbitrage in the Indian Tech Sector*, Vidhi Centre for Legal Policy, Working Paper (2021).

<sup>110</sup> Smriti Sharma, *India's Regulatory Gaps in the Platform Economy*, *The Hindu BusinessLine*, April 2023.

<sup>111</sup> Supriya Routh, *Worker (In)security in the Platform Economy: The Case of Ola and Uber Drivers in Kolkata*, 12(1) *Indian J. Lab. Econ.* 47 (2016).

<sup>112</sup> NITI Aayog, *India's Booming Gig and Platform Economy*, Policy Report, 2022.

A socio-legal perspective reveals that regulatory arbitrage cannot be addressed solely through punitive legal action.<sup>113</sup> Instead, it requires structural reforms that align law with evolving business realities.<sup>114</sup> Drawing from global best practices, India must prioritize adaptive regulation, legal clarity, and technological literacy within regulatory bodies.<sup>115</sup> Regulatory sandboxes, centralized oversight, and enforceable social accountability standards are essential tools to mitigate the risks posed by unchecked innovation.<sup>116</sup>

Furthermore, integrating social justice principles into corporate regulation ensures that the benefits of innovation are not achieved at the cost of human dignity, fairness, or democratic legitimacy.<sup>117</sup> Workers' rights, consumer safety, and digital wellbeing must be central to the legal framework governing startups.<sup>118</sup>

In conclusion, the challenge is not to halt innovation but to govern it responsibly.<sup>119</sup> A future-ready regulatory ecosystem must balance growth with accountability, opportunity with equity, and freedom with ethical constraints.<sup>120</sup> Only then can India's startup revolution sustain its promise, not just as a driver of profit, but as a force for inclusive, lawful, and socially conscious development.<sup>121</sup>

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<sup>113</sup> Julia Black, *Paradoxes and Failures: 'New Governance' Techniques and the Financial Crisis*, 75 Mod. L. Rev. 1037 (2012).

<sup>114</sup> Douglas W. Arner, Janos Barberis & Ross P. Buckley, *FinTech, RegTech and the Reconceptualization of Financial Regulation*, 37 Nw. J. Int'l L. & Bus. 371 (2017).

<sup>115</sup> Monetary Authority of Singapore, *FinTech Regulatory Sandbox Guidelines*, 2020.

<sup>116</sup> European Commission, *Digital Services Act*, available at: <https://ec.europa.eu/> (last visited June 24, 2025).

<sup>117</sup> Amartya Sen, *Development as Freedom*, Oxford University Press (1999).

<sup>118</sup> Martha C. Nussbaum, *Creating Capabilities: The Human Development Approach*, Harvard University Press (2011).

<sup>119</sup> Reetika Khera, *Digital Governance and the Future of State Regulation*, *Economic & Political Weekly*, Vol. 58, No. 12 (2023).

<sup>120</sup> Paul de Hert and Vagelis Papakonstantinou, *The New General Data Protection Regulation: Still a Sound System for the Protection of Individuals?*, 32(2) Comp. L. & Sec. Rev. 179 (2016).

<sup>121</sup> NITI Aayog, *Strategy for New India @75*, 2018.