TeamLease® RegTech
Helping India Comply

Decoding Compliance for Manufacturing MSMEs in India

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Executive Summary

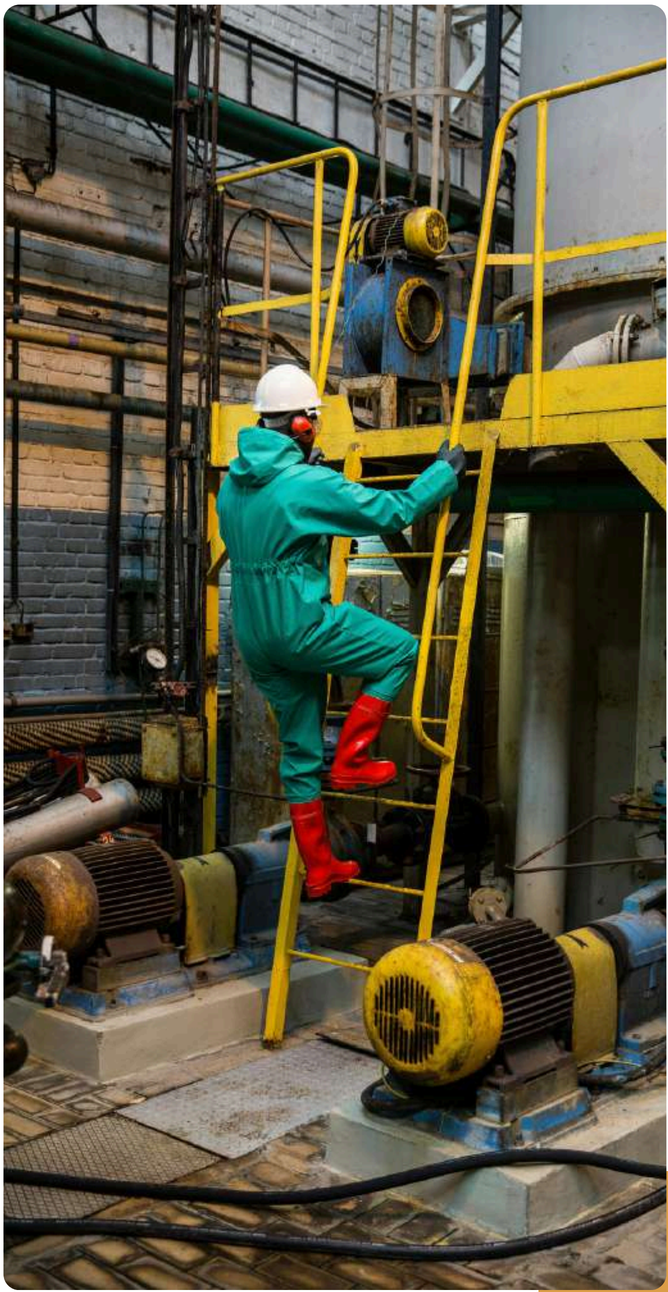
India's entrepreneurial spirit finds its truest expression in its Micro, Small, and Medium Enterprises (MSMEs), dynamic businesses that operate with ambition but often without adequate institutional support. These enterprises are not just economic entities; they represent the aspirations of millions. Yet, their growth is stifled not by market forces alone but by a dense forest of regulatory obligations that are difficult to navigate and expensive to maintain.

This report deciphers the intricate web of compliance obligations, encompassing licenses, approvals, registrations, and permissions, that MSMEs must navigate throughout the lifecycle of setting up, operating, and closing an enterprise. A typical manufacturing MSME with a single unit in one state is subject to over 1,450 compliance obligations annually, cutting across seven categories of law. These include 59 types of inspectors coming at different intervals with different requirements, 48 different registers, and 486 imprisonment clauses, many for procedural lapses.

The compliance burden is not only intricate but also expensive. The annual cost of meeting these requirements ranges between ₹13 to ₹17 lakh, straining enterprises with limited resources and minimal in-house expertise.

Labour laws alone account for 66% of all imprisonment-linked compliance, highlighting the excessive criminalisation embedded in the regulatory framework.

MSMEs can variably become the engines of growth if their compliance burden is reduced. A significant amount of policy reforms can unleash their potential. The report concludes with actionable recommendations for the same, on how a conducive business environment can be created with the help of certain stepping stones.



Overview of MSMEs

MSME stands for Micro, Small, and Medium Enterprises. These enterprises are classified based on their investment in plant and machinery/equipment and annual turnover. The classification has been made to determine eligibility for government schemes, incentives, and regulatory benefits aimed at promoting and supporting MSMEs. According to the latest data as per Udyam Portal registrations, there are more than 63 million enterprises registered as MSMEs in the country.

Figure 1. Revised Classification applicable w.e.f 1st April 2025

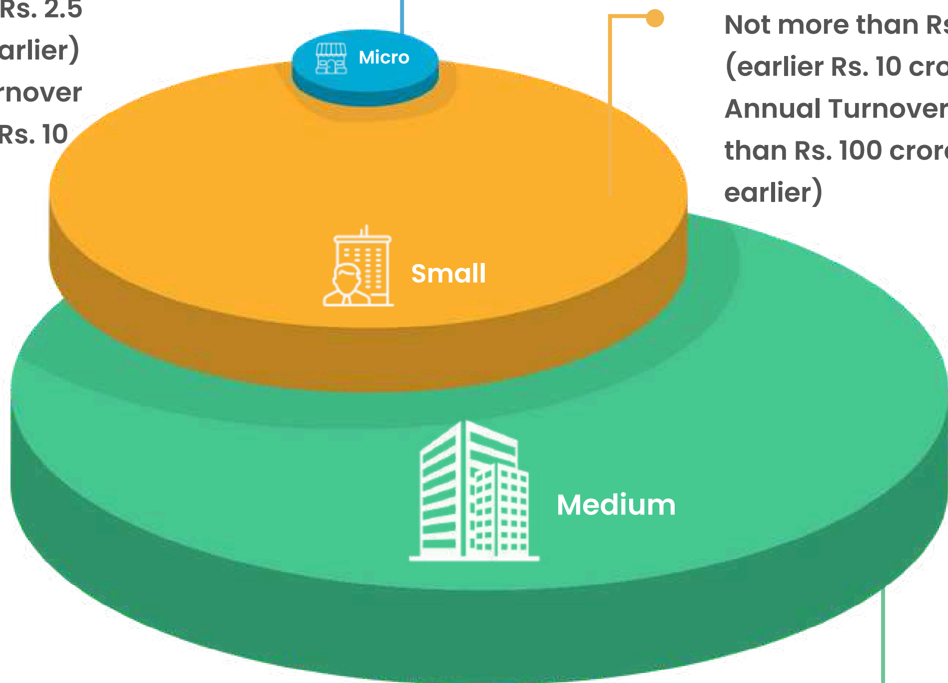
Manufacturing Enterprises and Enterprises rendering Services

Investment in Plant and Machinery or Equipment:

Not more than Rs. 2.5 crore (1 crore earlier) and Annual Turnover not more than Rs. 10 crore (5 crore earlier)

Investment in Plant and Machinery or Equipment:

Not more than Rs. 25 crore (earlier Rs. 10 crore) and Annual Turnover not more than Rs. 100 crore (10 crore earlier)



Investment in Plant and Machinery or Equipment:

Not more than Rs. 125 crore (50 crore earlier) and Annual Turnover not more than Rs. 500 crore (250 crore earlier)

Number of MSMEs in India

States/UTs with the highest number of MSMEs(as per Udyam portal registrations)

(Count in Lakhs)

West Bengal	45,07,903
Uttar Pradesh	69,46,135
Maharashtra	84,35,475
Karnataka	42,85,360
Madhya Pradesh	40,81,847

States/UTs with the lowest number of MSMEs (as per Udyam portal registrations)

(Count in Thousands)

Lakshadweep	2,173
Ladakh	18,406
Mizoram	44,399
Andaman & Nicobar Islands	19,128
Sikkim	28,595

Entry and Exit Processes

The process of registering an MSME requires going through some steps prescribed by the government. However, the process of exiting is more extensive for these enterprises.

BECOMING AN MSME (MICRO, SMALL OR MEDIUM ENTERPRISE) REQUIRES THE FOLLOWING STEPS:

- Apply online on the Udyam Registration portal through self-declaration; no documents are needed
- Upon registration, the enterprise receives a permanent Udyam Registration Number
- After successful registration, an Udyam Registration Certificate is issued

The process of registration incurs no charges and must be done using the form on the Udyam portal

REGISTRATION

Aadhaar number is mandatory

- Proprietor (proprietorship)
- Managing partner (partnership)
- Karta (HUF)

For companies, LLPs, societies, trusts, etc., Aadhaar, PAN, and GSTIN must be provided.

In case an enterprise is duly registered as an Udyam with PAN, any deficiency of information for previous years when it did not have PAN shall be filled up on self-declaration basis

CANCELLING AN MSME REGISTRATION

Step-by-Step Process to Cancel MSME Registration

- Visit the Udyam Registration Portal
- Log in using your Udyam Registration Number and linked Aadhaar (OTP verification required)
- Go to 'Update or Cancel Registration' and select Deregistration
- Enter business details: Udyam number, PAN, GST (if applicable), and reason for cancellation.
- Upload documents (as applicable)
  - Business closure certificate
  - Financials showing turnover beyond MSME limits
  - Merger/acquisition papers
  - Legal orders
- Submit the cancellation request and download the acknowledgement

It takes about 7-15 business days for the request to be reviewed. Upon approval, a confirmation email is received. These are the entry and exit steps for these enterprises.

The operations in between extract a heavy toll, both in terms of the labyrinth and the cost of compliance requirements. Multiple licenses and approvals have to be obtained under many acts and categories of law.

Regulatory Landscape for Manufacturing MSMEs in India

The regulatory landscape for MSMEs is vast in India. There are various requirements that they need to fulfill to start, manage, and operate an enterprise. Similarly, for dissolving the organisation, an array of processes is required to be fulfilled.

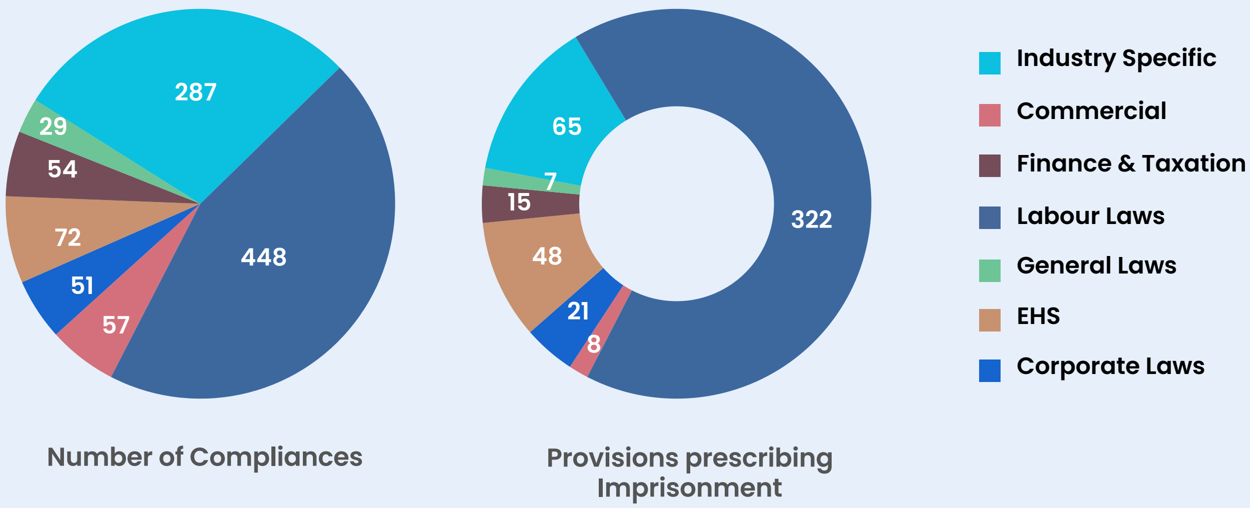
This year's Economic Survey mentioned that regulatory compliance burden holds back formalisation and labour productivity, limits employment growth, chokes innovation and depresses growth.

One of the biggest hurdles is the ever-evolving and changing ground for implementation. An average of 42 regulatory updates per day fog the entire ecosystem. FY 2024-25 alone saw 9,331 updates across seven categories of law.
These updates come from different ministries, departments and regulatory bodies and impact all levels of enterprise. MSMEs in particular are affected by at least 90% of these updates, given the country has a total of 6,45,22,249 of such enterprises.

Compliance Framework

To highlight the magnitude of compliance requirements for micro, small and medium enterprises, the illustrative lists of different obligations below can be referred to:

Figure 2. Compliance bifurcation for a factory in a single state*



*The enterprise operates a single manufacturing facility located in a single state

Table 1. Frequency of compliance bifurcation for a factory in a single state*

Frequency	Annually	Half-Yearly	Quarterly	Monthly	Others	Total
Unique compliance obligations	83	12	20	31	852	**998**
Total annual compliance obligations	83	24	80	372	897	**1,456**

*The enterprise operates a single manufacturing facility located in a single state

A single manufacturing unit of an MSME must comply with 998 unique obligations and over 1,450 total obligations annually. These requirements are segregated across seven categories of law and apply to different establishments. These also subsume over 480 imprisonment clauses, mostly for procedural lapses.

Approvals/Registrations/Permissions

Table 2. List of Approvals/Registrations/Permissions to be obtained by an MSME*

	Approvals/Permissions /Registrations
Categories	Count
Commercial	14
Corporate	3
Environment, Health & Safety	17
Finance and Taxation	4
Industry Specific	7
Intellectual Property	1
Labour	12
Local	19
General	-
Grand Total	77

*The entity has a manufacturing unit and a corporate office in the state of Karnataka

MSMEs in different sectors are subject to obtaining licenses, permissions, approvals, and registrations under different stages of production and operations, timelines, acts, and levels of governance. For example, on average, an MSME with a manufacturing unit and a corporate office in a single state is easily subject to 70 odd one-time registrations and approvals across four stages- Setting Up, Pre-Commissioning, Post-Commissioning and Ongoing. These approvals relate to land allotment, project-related approvals, construction approvals, approvals related to labour, safety and health, tax-related registrations, etc. Then there are the ongoing compliances which the company must adhere to at every stage of production. These include a mix of Central and state-specific compliances. These are in addition to the Types of Compliance that these enterprises have to adhere to. This increases the number of requirements, and the capacity to meet these becomes another requirement for enterprises to cater to.

Labour Compliance Challenges

Among India's 63 million enterprises, only 1 million are formal enterprises covering their workforce under labour laws. 62 million enterprises are small and informal and over 90% of India's labour force works in them. As a result, only approximately 9% of India's workforce benefits from the labour laws.

Labour laws form the single largest component of compliance obligations, accounting for roughly 45% of all requirements. Manufacturing MSMEs must contend with a host of labour laws and regulations at both central and state levels. These include requirements for registering establishments, maintaining extensive records and returns, adhering to rules on wages, working hours and worker benefits, etc. Key labour compliance challenges include:

Multiplicity of registrations

A small manufacturing unit often needs to obtain multiple statutory registrations and licenses before it can operate. These may include registering under the Factories Act, or alternatively under the local Shops and Establishments Act for smaller workshops. If the enterprise crosses certain employment thresholds, it must register with social security organizations, for example, obtaining an Employees' Provident Fund (EPF) code if it has 20 or more employees, and registering for Employees' State Insurance (ESI) if it has 10 or more employees. For instance, a pharmaceutical MSME with a single corporate office, and a single manufacturing facility in the state of Maharashtra has to obtain 4 licences and registrations.

Concurrent Subject

Labour is a concurrent subject meaning both central and state governments can enact laws, leading to overlaps. An MSME may have to comply with central acts like the EPF Act, ESI Act, Minimum Wages Act, etc., as well as state-specific rules such as state labour welfare fund acts or shops act provisions.

Multiple registers and returns

Under labour laws, companies are required to maintain a register of employees or workers on their roll. Leave records of employees or workers must also be maintained in registers. Employers are also required to maintain records of the dates of whitewashing, varnishing, and colour-washing among others under the Factories Act, 1948. In addition, they are also required to maintain a register of accidents, a record of the examination of hoists or lifts, an overtime register, a maintenance book, and a leave with wages register among others. For instance, a pharmaceutical MSME has to comply with 49 displays and 72 registers and records requirements related to labour obligations.

In addition to maintaining statutory registers, employers are also required to file various returns under multiple labour laws. These include annual returns under the Employees' Compensation Act, Maternity Benefit Act, etc. Employers must also submit a unified annual return under the Contract Labour Act, register an equal opportunity policy under the Rights of Persons with Disabilities Act, and ensure the Internal Committee submits its annual report under the POSH Act.

While not every MSME falls under all these laws, even a small factory can easily be subject to a dozen or more Acts, each with its own reporting requirements. This cumulative burden of maintaining registers and submitting forms to various authorities adds to the complexity.

A step towards rationalisation of these requirements:

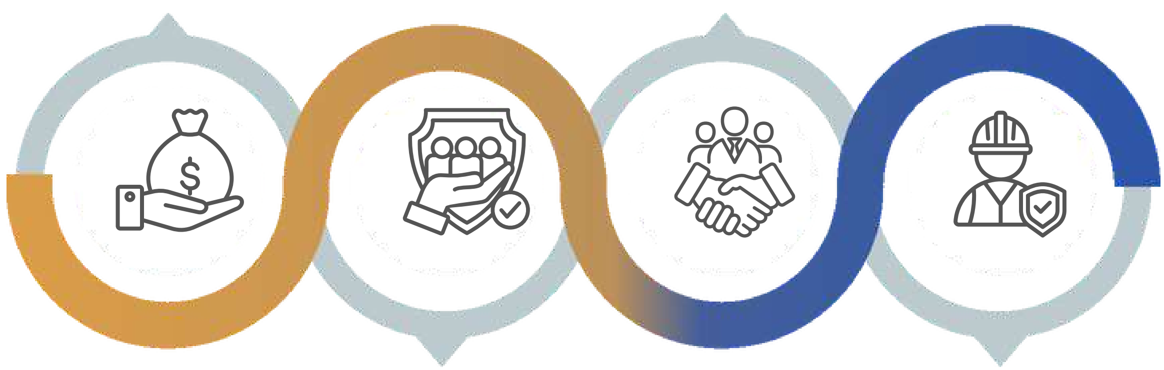
The implementation of the new labour codes in India is expected to significantly reduce the compliance burden on enterprises by consolidating and streamlining various regulatory requirements.

01

The **Code on Wages** merges multiple annual returns and reduces the number of registers employers must maintain from 12 to 4, with the possibility of further reducing them to just one.

03

The **Code on Industrial Relations** also simplifies trade union registration and has reduced the 2 registrations required by the trade unions to 1.



02

The **Code on Social Security** consolidates 36 annual returns required under nine separate Acts into a single return, slashing the number of remittances, returns, and register submissions by over 90%.

04

The **OSH &WC Code**, which governs occupational safety and health, cuts down licenses from 4 to 1, registrations from 11 to 1, returns from 22 to 1, and registers from 76 to as few as 2 or 3 effectively reducing the compliance load by over 90%.

Collectively, these reforms promise to ease administrative overhead for businesses, especially MSMEs, and promote a more transparent and efficient regulatory environment.

Element of Criminality

The most aggravating feature of this vast and uncertain compliance universe is the risk of imprisonment that looms large over entrepreneurs. The number of jail provisions that have been woven into the fabric of India's business laws provides some startling insights. Currently, 26,134 imprisonment clauses are contained in 843 (or 54.9 percent) of these laws. Almost 80 percent of the total criminality in India's business laws is contained in 20,895 jail provisions spread over 599 State laws, while the rest 20 percent falls within 5,239 imprisonment clauses under 244 Union laws. Overall, almost two out of every five compliances carry jail terms for violations. As a result of this hostility in an already overregulated space, the steady creation of new enterprises and the organic growth of existing businesses have been restricted to a considerable extent.

The foregoing are just some of the many unique observations made in a monograph titled Jailed for Doing Business which diagnoses India's business compliance framework with "regulatory cholesterol" that has precluded the seamless flow of innovation and entrepreneurship and hindered the dynamic process of job and wealth creation. It dives deep into the unchartered territory of imprisonment clauses in business laws and argues that the criminalisation of business laws is antithetical to the objectives of Ease of Doing Business.

Criminality in Labour Laws

Labour laws form the most significant part of compliance-related burdens in India's regulatory framework for businesses. Labour accounts for 463 acts (30.1%), 32,542 compliances (47%) and 3,048 (46%) filings. Of these, 17,819 (54%) carry imprisonment as a penalty for non-compliance. Out of the total compliances that prescribe jail term, 68% of them belong to labour.

» An MSME with a single manufacturing operation and corporate office in a single state deals with 998 compliances in a year. Among them, 486 (or 48.7%) compliances contain imprisonment clauses. Out of 998 compliances, 448 are labour-related, and 322 specifically impose imprisonment for contraventions. This indicates that nearly 66% of all imprisonment-linked compliances in the pharmaceutical sector stem from labour laws alone.

Cost of Compliance

Compliance is a costly affair and requires input from many variables. These further segregate into both direct and indirect costs. There are direct and indirect costs associated. Direct costs arise from not meeting the compliance requirements. A company becomes liable to pay a penalty or fine if it fails to meet a certain requirement. For example, if a company fails to provide basic canteen facilities to its employees, it is subject to a penalty. Indirect costs arise from the process of building a process or team that helps meet the compliance requirements. Training personnel or upgrading software to meet these requirements incurs a significant cost. Remuneration to employees and technology upgrade expenses can add to the indirect costs of organisations.

To obtain an average idea, the compliance costs for a small manufacturing MSME with the following assumptions are provided in the table below:

Revenue
up to **100 Cr**

Employee Strength
up to **150**

Operational Details

One head office in a metro city

2 Factories

1 Warehouse

1 Regional Office

Private Limited Company with MSME status

Hires a combination of full-time employees & third-party consultants

Table 3: An illustrative example of costs of compliance for a small manufacturing MSME

	Category	External Annual Cost	Internal Annual Cost	Total
	Labour and Industrial Licensing (Not including EHS)*	615,000	142,358	757,358
	Finance and Tax	240,000	90,000	330,000
	Environment Health & Safety	168,000	120,000	288,000
	Secreterial (Company Law)	60,000	120,000	180,000
	Total	**1,083,000**	**472,358**	**1,555,358**

*Labour and Industrial Licensing (excluding EHS) includes subcategories such as Payroll Compliances, Factory Compliances / Industrial Licensing, Shops & Establishment Compliances, and POSH Compliances. The total external cost incurred per month for managing these compliances is ₹51,250, which comprises ₹12,750 for advisory services, ₹30,000 for periodic time-based compliances, and ₹8,500 for notice and inspection management services.

Based on the detailed compliance cost calculation outlined above, the final cost can vary within a range of 13 Lakhs to 17 Lakhs.

Inspections

MSMEs across sectors are subjected to inspection under different categories of law, legislation, timelines, authorities, etc. For instance, the table below highlights inspection instances for an MSME with a factory and head office, the Labour category accounts for the highest number of inspections, with a total of 21 inspectors or authorities involved. This reflects the extensive regulatory oversight in the labour sector, encompassing roles such as the Assistant Labour Commissioner, Labour Inspectors, Chief Inspector of Factories, and officers from bodies like the EPFO and ESIC. EHS (Environment, Health, and Safety) comes next with 18 authorities, highlighting growing environmental and safety compliance needs. Commercial inspections, which include checks by authorities like the Chief Controller of Explosives and Transport Authorities, stand at 9, while Industry-specific inspections—covering areas like food safety and narcotics, are at 5. General and Finance & Taxation have relatively fewer inspections, with 4 and 2 respectively.

Figure 3: Inspection instances for an MSME with a factory and a head office

Industry Specific 8.5%

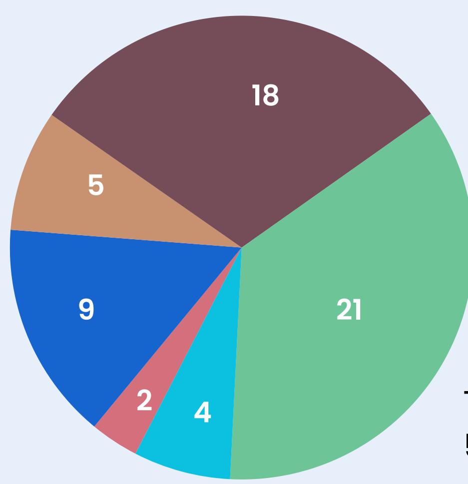
EHS 30.5%

Commercial 15.3%

General 6.8%

Finance & Taxation 3.4%

Labour 35.6%



Total 59

Challenges

Apart from the specific challenges mentioned above, there are broader challenges that these enterprises face:

Tax Compliance- Taxes and the economy are closely interconnected, and whenever there is a significant change in the tax system, it becomes crucial to assess its impact on the relevant industry and the associated businesses. They face major challenges in GST compliance due to frequent regulatory changes, limited digital infrastructure, and a lack of trained resources. Issues like timely return filing, invoice accuracy, ITC reconciliation, and adopting e-voicing requirements further strain their capacity to stay compliant. Tax systems for MSMEs should be designed to align tax compliance requirements with the capacity of SMEs as it brings more enterprises into the formal sectors, providing better access to finance, and opportunities for collaboration.

Lack of awareness/resources- MSMEs generally don't have adequate awareness regarding their compliance requirements.
They tend to focus more on growing their business and understand the cost of non-compliance to be meagre as compared to the cost of meeting such requirements. This leads to lack of a tone-from-the-top with lesser allocation of resources to building a team/adopting necessary technology to stay on the right side of the law.

Technology and Innovation- Given the significance of the MSME sector, it is crucial to ensure the competitive position of Indian SMEs, both on the national and international stages, with technology and innovation serving as pivotal factors. However, scalability in terms of adoption of technology by these enterprises remains low due to budget constraints.

Transition to greener practices- The impact of climate change and sustainability concerns now requires MSMEs to transition to greener practices. These enterprises, especially in developing countries, are often concentrated in climate-dependent sectors like agriculture, fisheries and tourism, making them highly vulnerable to climate change impacts such as extreme weather events and rising temperatures.

Government Initiatives

The government has been constantly putting efforts towards creating a business-conducive environment in the country. The 2025-26 budget saw the introduction of several schemes to enable ease of doing business.

Below is the estimated budget average over the last five years that was allocated to MSMEs by the Ministry of MSMEs[1]:

Table 4. Budgetary allocation by the Ministry of MSMEs

Financial Year	Budget (in cr.)	Revised Estimates
2025-26	23,168.15	-
2024-25	22,137.95	17,306.70
2023-24	22,137.95	22,138.01
2022-23	21,422.00	23,628.73
2021-22	15,699.65	5,664.22

1 https://www.pib.gov.in/FactsheetDetails.aspx?Id=149117

Below are some government initiatives striving to ease doing business for MSMEs:

Udyam Registration Portal

Launched on July 1, 2020, the Udyam Registration Portal serves as a pivotal platform for facilitating the registration of enterprises across India. The portal encourages enterprises previously registered under the Udyog Aadhaar Memorandum and Entrepreneurship Memorandum-II to migrate to this new system. It offers a free, paperless, and self-declaration-based registration process, eliminating the need for document uploads, thus simplifying the formalisation of businesses

Public Procurement Policy for Micro and Small Enterprises

The Ministry of MSME, Government of India, notified the Public Procurement Policy for Micro and Small Enterprises (MSEs) in 2012. This policy mandates that 25% of annual procurement by Central Ministries, Departments, and Central Public Sector Enterprises (CPSEs) must be sourced from MSEs.

Pradhan Mantri Mudra Yojana

The primary offering of MUDRA (under the Pradhan Mantri MUDRA Yojana) is to provide refinance support for loans to micro businesses and entrepreneurs. It offers three categories of loans based on the stage of business growth: 'Shishu' for loans up to ₹50,000, 'Kishor' for loans between ₹50,001 and ₹5 lakh, and 'Tarun' for loans above ₹5 lakh up to ₹10 lakh.

Development of Industrial Infrastructure for MSME sector

Under this, financial assistance is provided for the setting up of industrial estates or development of industrial areas, including projects eligible under the KVIC model. The support is aimed at promoting industrial infrastructure, and promoters of such infrastructure projects can apply through State Financial Corporations (SFCs), State Industrial Development Corporations (SIDCs), or banks.

Fast Track Exit Mode

This scheme facilitates an easy exit for non-operating companies that have no business activity and nil assets and liabilities. Assistance is provided by NSIC, and eligible companies can apply by approaching the nearest NSIC branch.

1 https://www.pib.gov.in/FactsheetDetails.aspx?Id=149117

Recommendations

Digitisation: It can help accelerate end-to-end digitisation of compliance processes across government departments and regulatory bodies. Digitisation ensures real-time compliance tracking, reduces paperwork, eliminates manual errors and enables timely submissions, especially critical for MSMEs with limited resources and capacity. The implementation of the following may help MSMEs scale their operations:

PAN 2.0 (Common Business Identifier)

India's complex identification framework with 23 overlapping central and state identities adds to regulatory cholesterol for businesses. Both central and state governments require businesses to create at least 23 identities, including PAN, GSTN, LIN and Professional Tax Number, Factory license number, Shop & Establishment Registration. These layers weave a vast web of redundancies that tangles up the enterprises in justifying their presence. The introduction of PAN 2.0, similar to a Unique Enterprise Number (UEN), comes as a timely solution, integrating a secure, technology-driven framework with features like a unified portal and QR codes. Consolidating core and non-core PAN and TAN activities will form one common identifier for businesses.

EntityLocker

The EntityLocker will serve as a centralised repository for legitimate documents, including but not limited to licences, registrations, permissions, NOCs, and consent orders. Subsequently, these genuine digital documents may be employed in compliance and verification procedures. By granting consent to service providers, organisations can streamline the approval, registration, and clearance processes, among others. Additional support for the document's authenticity can be obtained by implementing a transparent, verifiable, and tamper-proof storage system. This will substantially diminish the occurrences of fraudulent activities involving falsified and counterfeit documents to acquire licences, registrations, and approvals.

NOCG

National Open Compliance Grid (NECG) would allow straight-through processing of filings and regulatory changes, communicate notices for inspections and maintain audit trails, leveraging the UEN and DigiLocker systems. This tech-driven solution would reduce delays, provide real-time regulatory updates, and help track compliance obligations for employers, service providers, and government bodies. It will help integrate employers' compliance needs across various legal categories—such as labor, finance, tax, environmental health and safety (EHS), commercial, secretarial, and industry-specific laws—at central, state, and local levels. This would create a cashless, paperless, and presence less compliance in digital India.

Simplified Unified Regulatory Update Platform

There should be a single digital portal for the centralised publishing of all regulatory updates across various departments and ministries and at all governance levels. It should be capable of providing automated alerts for every new notification, circular, direction, and draft, among others. A digital platform to automate the generation of all regulatory records for compliance should also be created. It should also facilitate the safe storage and authentication of such records.

Rationalisation: There is a lot of duplication, redundancy, and overlap in the compliance obligations within the business regulatory framework. There are increasing calls for a risk-based, faceless, presence-less, and cashless inspection process. As such, digital interfaces for new license applications, license renewals, return filings, and inspection requests, among others, must be developed. Enforcement of Compliance requires regulatory capacity in the government. Unfortunately, the current installed capacity is far behind the Industrial demand. Allowing enterprises to self-certify and undergo third-party inspections will further improve the ease of doing business.

Decriminalisation: The introduction of Jan Vishwas has reversed the gaze by eliminating employer jail provisions by applying specific filters. Jail penalties should only apply to offenses involving physical harm to individuals, intentional fraud against stakeholders such as employees, lenders, shareholders, or the government, or large societal externalities that cannot be compensated, such as those affecting public order, national integrity, or trust in property rights. Provisions in general clauses that either fail to specify the crime or define it too broadly should be removed, along with penalties for procedural issues such as delayed or inaccurate filings, incorrect calculations, or errors in formatting. This approach seeks to rationalise penalties, ensuring accountability without excessive criminalisation. The initiation of Jan Vishwas 2.0 further aims to decriminalise procedural lapses after the success of Jan Vishwas 1.0. As mentioned above, MSMEs are subject to 216 imprisonment clauses across different categories of law.

Creating a culture of compliance: Top management must champion a culture of compliance within the organisation. A proactive approach, coupled with a positive attitude towards compliance, is essential. Organisations can encourage compliance-positive behaviour by involving top management in the compliance process and setting a positive tone. This culture, rooted in the organisation's values and supported by its personnel, can be effectively implemented through technology. Emphasising compliance from the onset of an employee's tenure, with regular training sessions, helps instil the importance of compliance.

One date-one application: One date of implementation and applicability of all regulatory changes related to MSMEs should be provided. FSSAI has finalised 1st July as the implementation date for all the changes made by the regulator.

Buffer period for implementation: Also, when some changes are introduced, some buffer period should be provided to the organisations to transition. This would not lead to retrospective implementation of these changes leading to financial or reputational losses for organisations.

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