



Press Release

## Does the regulatory environment in India handicap MSMEs? Research demonstrates urgent need for deregulation of the sector

Against the post-New Industrial Policy (1991) growth witnessed in large-scale industries, a corresponding boom in the small and mid-sized domestic industry has been conspicuously absent. CCS's latest research seeks to document the causes for this disparity in growth. Indian MSMEs have also been compared with those operating in other BRICS nations in an attempt to understand the overall effect of the business, policy and legal/regulatory environment on the growth of MSMEs.

The key findings of our study are as follows:

1. The effect of liberalisation on MSMEs, vis-à-vis large-scale units, has been skewed in favour of the latter, as is rather evident from the following statistics discovered through the course of the paper:

| Years              | Factories (%) |       | Employees (%) |       | Gross Output (%) |       |
|--------------------|---------------|-------|---------------|-------|------------------|-------|
|                    | SSI           | Large | SSI           | Large | SSI              | Large |
| 1980-81 to 1984-85 | -0.6          | 11.9  | -2.1          | 2.1   | 0.6              | 8.7   |
| 1985-86 to 1990-91 | 0.7           | 15.0  | 1.5           | 0.5   | 7.9              | 9.6   |
| 1990-91 to 1995-96 | 0.2           | 13.7  | 0.1           | 1.1   | 5.0              | 9.3   |

2. The regulatory norms governing the entry of MSMEs extend to: registration, licensing and procedural norms associated with starting a business, acquiring a construction permit and registering property. It is interesting and significant to note that while starting a business involves 12 steps in India, acquiring a construction permit takes 27 procedures and registering property spreads across 7 steps. These barriers are seen to restrict entry into the MSME sector.
3. The continuance of MSME units is influenced largely by legal stipulations corresponding with labour, credit and taxation. Taxation poses a hindrance to MSMEs in terms of the number and protracted nature of payments to be made: on an average, firms in India make 33 tax payments annually; spend 243 hours a year filing and paying taxes and the total tax payment amounts to 61.7% of profit.



So far as labour is concerned, MSMEs are hit by the 'over-legislation' that we witness in the field of labour law, with 44 central legislations and over 150 state legislations in place currently. Most of these laws are redundant and inapplicable to the micro and small units. Further, the scattered nature of this plethora of statutes makes compliance challenging for MSME units. Problems associated with credit include low credit availability, coupled with high credit cost.

4. The absence of a defined exit procedure, despite Section 25 of the MSMED Act, 2006 requiring the formulation of one on part of the Central Government within one year of its enactment, is significant. This allows for arbitrariness on part of banks when resolving insolvency and finalising exit proceedings. A statutory framework focusing on facilitating revival, or at least an easy exit, is imperative.
5. India's performance in 2014 fell two rank points from 2013 on the Ease of Doing Business Index, from 140th to 142nd.
6. In order to gauge the movement of India along the Doing Business Index, and assessing its progress in terms of establishing a more conducive regulatory environment to MSME growth, the Distance to Frontier score serves as a more suited yardstick, as against the Doing Business Rank. It is observed that India presents a promising picture here; starting a business, dealing with construction permits, getting electricity, trading across borders and resolving insolvency have all become easier to negotiate.
7. Taking into consideration the above-stated prime findings, as also other secondary data studied as part of the research, policy recommendations were moved to the following effect: the need to draw up a distinction between micro, small and medium enterprises, on a policy level; was recognised; minimisation of procedural compliances required for starting a business; more evolved monitoring mechanism with respect to finance for MSMEs; simplification of the labour regulatory framework; requirement for a simpler taxation procedure, along with non- ambiguity in taxation laws; establishing a sound legal framework for an exit scheme.

The study has been conducted by Amit Chandra, Senior Manager, CCS Academy and Research Intern Vrinda Pareek. The complete paper can be accessed on [our website](#).