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BETWEEN BURDEN AND BIAS: REGULATORY DISCRETION, PROCEDURAL COMPLEXITY AND THE SURVIVAL OF MSMEs IN INDIA

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Abstract

The Micro, Small and Medium Enterprises (MSMEs) are vital to the economic structure of India as they significantly contribute to employment, decentralized manufacturing, and economic stability. The regulatory policy regarding MSMEs has generally been shaped to be supportive, focusing on formalisation, financial inclusion, and the embrace of digital practices. In the scholarly literature, this perspective is framed as regulation viewed either as an enabling factor or a perceptual construct influencing both adoption behavior and managerial intent. This paper examines framing by investigating regulatory enforcement as implemented by MSMEs. It indicates that procedural intricacy and selective enforcement have transformed regulatory adherence into an administrative obligation and created a type of structural bias that directly affects the survival of MSMEs. The study demonstrates that procedural defaults, along with notice-based and discretionary sanctions, leave MSMEs in a disadvantaged state of legal and financial exposure, utilizing doctrinal analysis and regulatory evaluation. It identifies a substantial research gap in MSME studies, which largely perceives businesses as subjects of regulation rather than as processes of regulation. Recast as issues of regulatory governance and legal risk, the paper emphasizes the need to prioritize procedural fairness, proportionality, and accountability in enforcement related to MSMEs.

Keywords: MSME, Regulatory discretion, Procedural complexity, Regulatory enforcement, Compliance burden, Structural bias, Legal vulnerability, Procedural fairness, MSME survival, Indian regulatory governance.

1. Introduction

Micro, Small, and Medium Enterprises (MSMEs) are vital to the Indian economy, making substantial contributions to GDP and job creation. Official estimates indicate that the sector accounts for almost one-third of India's GDP and provides jobs for more than 110 million individuals in manufacturing and services, which have been absorbed into the formal economy over the past decade via digitisation, financial inclusion, and standard compliance. Policy changes, including the consolidated MSME definition from the MSME Development Act of 2006 (revised in 2020), digital services like

the Udyam Registration Portal, and FinTech-based credit initiatives such as the Emergency Credit Line Guarantee Scheme (ECLGS), have expedited formalization, financial inclusion, and digital uptake in the past ten years. These initiatives aim to reduce entry obstacles, accelerate adherence, and incorporate MSMEs into the formal economy, thereby enhancing resilience against economic shocks like COVID-19 pandemic¹²³⁶. Support has been given to digital registration systems, online tax platforms, and FinTech-driven financial services to improve access to finance and reduce

¹²³⁶ Aggarwal, Rishabh. "MAKE IN INDIA – RISKS AND CHALLENGES AHEAD." *The Indian Journal of Political Science* 76, no. 4 (2015): 796–800. <https://www.jstor.org/stable/26575605>.

transaction costs. This policy preference is primarily evident in scholarly research. Scholarly research has primarily regarded this regulatory history as supportive and empowering. Leveraging frameworks like the Technology Acceptance Model (TAM) and the Unified Theory of Acceptance and Use of Technology (UTAUT), research emphasizes perceptual elements such as perceived usefulness, user-friendliness, trust in organizations, and clarity in policies as crucial influences on MSME adoption of formal systems. Research demonstrates that efficient online tax platforms (like GSTN) and incentive-driven systems lower transaction expenses while enhancing managerial compliance¹²³⁷. This story presents regulation as a beneficial mechanism that diminishes uncertainty and fosters economic stability.

Procedural inflexibility, coupled with enforcement leeway, transforms compliance from a strategic choice into an administrative hassle. Instead of fostering growth, this situation reinforces a systemic bias: MSMEs, lacking adequate legal resources, face significant legal and financial risks that threaten their existence. Formal legal frameworks impose continuous compliance obligations on businesses, with significant legal consequences for violations. These implications are not a thoroughly investigated aspect of MSME research, which continues to perceive regulation as generally beneficial, rather than oppressive. The primary claim in this argument is that regulatory burden, as implemented through rigid procedural systems and discretionary enforcement practices, represents a structural bias. This type of bias not only increases compliance costs but also directly affects the sustainability of MSMEs¹²³⁸.

The paper therefore positions MSMEs as a subject of regulatory influence within the

administrative and legal frameworks. This study challenges the dominant supportive narrative by analyzing MSME regulation via the perspective of enforcement practices. It argues that procedural intricacy and erratic enforcement generate a regulatory load that disproportionately impacts smaller enterprises, leading to defaults, heightened penalties, and survival risks. In contrast to earlier studies that regarded MSMEs as passive entities subjected to perceptual control, we consider them as proactive contributors in regulatory governance processes. The article highlights flaws in procedural fairness, proportionality, and accountability via a doctrinal examination of key statutes (e.g., the MSME Act, the GST Act) and an analysis of enforcement data from sources like the Annual Survey of Unincorporated Sector Enterprises. By tackling these challenges, the paper addresses a significant research void: the overlooked connection between regulatory design and MSME failure rates. It supports changes that emphasize preventive measures, including streamlined decisions, proportional penalties, and tech-driven transparency, to align regulation with its pro-MSME goals. The subsequent sections analyze the literature, investigate enforcement strategies, and present a governance-centered path ahead.

2. Research Objective

2.1 To examine the procedural complexity of MSME-related regulatory frameworks, with a particular emphasis on notice-based adjudication, inspection regimes, and penalty imposition procedures.

2.2 To determine how enforcement-oriented regulatory policies produce systemic prejudice and legal vulnerability in MSMEs as compared to larger firms.

2.3 To examine the nature and scope of regulatory discretion exercised in the enforcement of compliance obligations applicable to MSMEs in India.

¹²³⁷ Khardenavis, Amey, Delayed Payments, Legal Hurdles, And Workforce Woes: Unraveling the Twin Challenges Faced By MSME (July 30, 2024). Available at SSRN: <https://ssrn.com/abstract=4969665> or <http://dx.doi.org/10.2139/ssrn.4969665>

¹²³⁸ Allamraju, A., et.al. (2020). MSMEs and Competition Law in India: Victims or Perpetrators, Review of Socio-Economic Perspectives, Vol 5(1), pp. 23-34.

3. Research Questions

3.1 Whether procedural complexity and discretionary enforcement in MSME legislation create systemic biases that increase firms' legal and financial vulnerabilities?

3.2 Whether incorporating procedural fairness, proportionality, and accountability into regulatory governance may successfully reduce enforcement burdens.

3.3 Are MSME survival and compliance costs disproportionately affected by notice-based adjudications, inspection procedures, and penalty imposition?

4. Literature Review

The existing research on MSMEs and regulatory participation is grounded in adoption-centric frameworks such as the Technology Acceptance Model, Unified Theory of Acceptance and Use of Technology, and value-driven adoption models. The proposed models rely on the explanatory factors of behavioral intention, perceived value, trust, and institutional support. Within these frameworks, the implementation of regulation is largely executed as a perceptual construct. The elements of governmental assistance and the quality of regulatory metrics encompass incentives, clarity of policies, and the simplicity of compliance¹²³⁹. While these studies provide valuable insights into adoption behaviour, they offer a limited depiction of regulation as a legal and institutional aspect. What is additionally lacking is sustained participation in regulatory enforcement. There's minimal research conducted on procedural defaults, decision-making based on notifications, inspection systems, penalty enforcement, and discretionary choices. MSMEs are not conceptualized as legal entities bound by restrictive regulatory framework¹²⁴⁰. Consequently, the asymmetry of enforcement

and vulnerability created by compliance is analytically inaccessible¹²⁴¹. New critiques are starting to fill this gap. Chandra (2012) highlights regulatory obstacles within the MSME Development Act, 2006, noting that the sector contributes over 70% of industrial pollution yet does not receive equivalent simplification. Additionally, inadequate compliance methods (like pollution standards meant for larger corporations) hinder MSME development¹²⁴². Doctrinal analyses further highlight vulnerabilities: under MSMED Act Section 18, delayed payments take precedence over arbitration, yet weak enforcement persists due to deficiencies in legal awareness and inadequate coordination between state and central authorities. Mishra (2025) critiques the adherence to labor rights within the federal system, which complicates the procedures for MSMEs. Imbalances caused by compliance are challenging to examine because MSMEs remain under-researched as legal entities subjected to harsh enforcement¹²⁴³.

Simultaneously, literature centered on policy and development economics portrays regulation as a means that supports the growth of MSMEs. According to scholars such as Storey and Beck, streamlined regulations, access to financing, and confidence in institutions are vital for the success of enterprises. In India, regulatory reform is often discussed in policy analyses by the World Bank, OECD, and the Ministry of MSME as a means to reduce informality and ease business operations. Rather than concentrating on enforcement outcomes, these reports generally evaluate regulation through measures such as digital onboarding, credit penetration, and registration rates¹²⁴⁴. Nonetheless, this facilitative framework

¹²³⁹ Bhalla, N., Sharma, R. K., & Kaur, I. (2023). Effect of Goods and Service Tax System on Business Performance of Micro, Small and Medium Enterprises. *Sage Open*, 13(2). <https://doi.org/10.1177/21582440231177210>

¹²⁴⁰ Black, Julia. "The Emergence of Risk-Based Regulation and the New Public Risk Management in the United Kingdom." *Public Law*, 2005.

¹²⁴¹ Storey, D.J. (1994). *Understanding The Small Business Sector* (1st ed.). Routledge. <https://doi.org/10.4324/9781315544335>

¹²⁴² Chandra, A. *Regulatory Barriers to Micro, Small and Medium Enterprises*, Centre for Civil Society (2012), <https://old.ccs.in/sites/default/files/research/regulatory-barriers-to-msme.pdf>.

¹²⁴³ Dr. Vinay Pal Singh et al. (2024), *Industry 4.0 Adoption by Indian MSMEs and its Effects on Competitive Advantage and Firm Performance: An Empirical Analysis*, *Educational Administration: Theory and Practice*, 30(4), 11009-11019 Doi: 10.53555/kuey.v30i4.9038

¹²⁴⁴ Viswanath Venkatesh et al., *User Acceptance of Information Technology: Toward a Unified View*, 27 425 (2003).

sidelines the coercive and disciplinary elements of regulation. According to legal and socio-legal studies on regulation, particularly those by Baldwin, Black, and Braithwaite, enforcement is an essential aspect of regulatory frameworks and cannot be analytically detached from the creation of rules. The perception of regulated entities regarding the law is largely influenced by enforcement actions such as inspections, notifications, penalties, and judicial proceedings. Nevertheless, research centered on MSMEs rarely tackles this issue, resulting in a poor understanding of the effects of regulation¹²⁴⁵. The scholarly work on administrative law and regulatory governance has thoroughly conceptualized the notion of regulatory discretion. Black's study on discretion highlights the interpretative and functional freedom that law enforcement officials possess, often influenced by risk aversion and institutional motivations.

5. Research Gap

The current MSME study examines adoption behavior and regulatory support, yet it overlooks procedural complexity and discretionary enforcement as factors contributing to legal risk. The literature downplays the importance of compliance requirements within strict procedures and selective enforcement, transferring the regulatory burden to structural bias affecting MSME survival in India by overlooking enforcement outcomes.

5.1 Entities of Regulatory Authority in

MSMEs: The regulatory structures governing taxation, labor welfare, environmental standards, and licensing within the sector enforce similar procedural requirements on every business. MSMEs, conversely, differ significantly in size, revenue, organizational ability, and access to professional services. Regulatory equality, in essence, leads to significant inequality in its regulatory results. The great majority of MSMEs do not have a

compliance department or legal advisor. Minor legal education. Small administrative teams are usually responsible for compliance tasks. In such instances, procedural defaults often arise from informational imbalances and administrative burdens, rather than a lack of adherence. However, enforcement mechanisms often view procedural mistakes as a sign of inefficiency or incompetence among managers.

5.2 Risk and Complexity in Procedural Compliance:

Procedural complexity arises through multiple statutory submission obligations, unnecessary documentation needs, and the distribution requirements of digital compliance interfaces among different regulatory frameworks. It has led to greater consistency and regularity in reporting, enhancing compliance density, even though digitalization has reduced certain transaction costs. The current MSME research identifies that the perceived simplicity of use and the digital skills related to decision-making processes impact adoption choices. Consequently, minimal consideration is provided to the future legal implications of not adhering to administrative procedures. Even unintentional or technical defaults may lead to a sanction process, interest charges, and a lengthy and contested resolution. For MSMEs that have restricted financial and administrative abilities, these enforcement actions carry lasting legal consequences.

5.3 Regulatory Discretion and Enforcement Asymmetry:

Regulating laws necessitates the use of discretion. The officials exercise judgment during the inspection, delivering notices, amending penalties, and making decisions. In theory, proportionality and contextual assessment ought to be discretionary. In truth, judgment applied in complex systems that lack transparency leads to inconsistency and unpredictability in execution. MSMEs may show favorable views towards regulations when there are tangible economic advantages. These perceptions, however, might contrast with real enforcement

¹²⁴⁵ D. Davis, *Perceived Usefulness, Perceived Ease of Use, and User Acceptance of Information Technology*, 13. 319 (1989).

experiences, where discretionary decisions could lead to more significant legal consequences for minor procedural infractions. Businesses with greater access to legal resources and financial support are more equipped to handle discretionary engagements. MSMEs, in contrast, face significant exposure to enforcement risk.

5.4 From Regulatory Burden to Structural Bias: When intricate procedures encounter selective enforcement, regulatory demands shift into systemic prejudice. MSMEs are sidelined in regulatory frameworks, yet this occurs through engagement in enforcement regimes that overlook capacity disparities. Financial stability diminishes over time due to accumulating fines, legal expenses, and bureaucratic exhaustion, jeopardizing the business's survival. Survival implications are less frequent in MSME research tied to adoption, where behavioral intention is prioritized over legal outcomes.

5.6 Some Effects of Regulatory Governance: This research does not offer an all-encompassing reform initiative. It contributes to the challenge regarding the efficiency of regulatory measures. Recognized regulatory backing and adoption speed are not dependable indicators of regulatory achievement. The results of the implementation should encompass an evaluation of the governing regulations. When assessing regulation focused on MSMEs, it is essential to take into account procedural fairness, proportionality, transparency, and accountability. This recalibration is necessary; otherwise, efforts at formalization will result in structural disadvantages instead of improving them.

6. Research Methodology

The present study employs a purely doctrinal methodology to examine regulatory discretion, procedural intricacy, and their effects on the survival of MSMEs in India. This approach involves a thorough investigation of primary legal sources including statutes like the Micro,

Small and Medium Enterprises Development Act, 2006, the Goods and Services Tax Act, 2017, labor regulations, and environmental laws along with secondary materials like judicial rulings, parliamentary documents, and enforcement directives from organizations such as the Ministry of MSME and the GST Council. This approach aligns with the research objectives as it reinterprets regulatory processes as experienced legal realities for MSMEs, instead of mere perceptual constructs. Case studies of discretionary penalty impositions and procedural defaults adequately back claims of vulnerability, dispelling interdisciplinary options like econometric survival analysis. Doctrinal precision guarantees that governance deficiencies are thoroughly tackled, establishing a foundation for reform suggestions rooted in justice, proportionality, and accountability principles.

7. Significance of the Study

This research is important as it uncovers how procedural intricacies and discretionary application in India's MSME regulations instill structural biases that worsen legal and financial weaknesses, leading to the sector's concerning 70% failure rate in five years, even with its 30% GDP and 110 million jobs provided. Theoretically, it addresses an important gap in literature by positioning MSMEs as active legal entities experiencing coercive governance instead of mere perceptual adopters in TAM/UTAUT frameworks, and it presents "structural bias" as a novel perspective for evaluating enforcement disparities. It offers policymakers doctrinal critiques for reforms like penalty proportionality, clear digital notifications, and streamlined adjudications, which could lower yearly compliance expenses (Rs 13-17 lakh per unit) and enhance survival, formalization, and economic resilience amid global changes.

8. Background and Context of MSME Regulation in India

Micro, Small, and Medium Enterprises (MSMEs) have always played a significant role in India's

economic and development framework. Even before Independence, small-scale enterprises were regarded as tools for decentralized production, job creation, and regional balance. During the post-independence period, India's industrial strategy actively fostered small businesses in order to minimize economic power consolidation, boost entrepreneurship, and absorb surplus labor¹²⁴⁶. This policy approach saw MSMEs not just as economic entities, but also as agents of social and distributive justice. The regulatory framework regulating MSMEs evolved concurrently with the overall trajectory of Indian economic governance. Initially, regulations aimed to safeguard and promote through reservation rules, concessional financing, and fiscal incentives. However, with economic liberalization in the 1990s, the regulatory strategy steadily evolved away from protectionism and toward integration with market-oriented and formal regulatory systems¹²⁴⁷. MSMEs were increasingly subject to taxes, labor, environmental, and commercial rules that had previously been geared for bigger firms.

This shift has resulted in a conundrum in MSME regulation. On the one hand, the state views regulation as an enabling instrument for reducing informality and increasing resilience. MSMEs, on the other hand, operate in thick regulatory frameworks with procedural rigor and discretionary enforcement. MSMEs face increased legal and financial risks due to a lack of legal knowledge, limited resources, and reliance on administrative discretion. As a result, regulation, rather than serving as a support system, is increasingly shaping MSMEs' survival possibilities¹²⁴⁸. Understanding the history of MSME regulation in India necessitates delving beyond policy purpose and adoption narratives

to investigate the lived experiences of regulatory enforcement. The current regulatory landscape demonstrates a transition from protection and promotion to governance via compliance, with procedural complexity and discretionary authority playing a critical role in deciding MSME sustainability.

8.1 Evolution of MSME Regulation: Protection to Compliance

India's evolution in MSME regulation showcases a significant transformation from the artisan protectionism of the pre-Independence era to the compliance governance seen after liberalization, mirroring the country's economic development while also inadvertently exposing small enterprises to structural weaknesses. Before 1947, small-scale industries such as khadi and village enterprises represented Gandhi's vision of swadeshi, acting as decentralized production centers with minimal regulation under colonial economies that prioritized raw material extraction. Following Independence between 1948 and 1990, the Industrial Policy Resolutions of 1948 and 1956 regarded MSMEs as tools for social equity, employment, and regional balance—providing over 800 product reservations, 40% priority sector lending, protective tariffs, and establishing institutions such as NSIC (1955) and SIDBI (1990) that safeguarded them from the dominance of larger industries.

The liberalization that began in 1991 was a turning point: delicensing, removal of reservations, and the Delayed Payments Act (1993) subjected MSMEs to market dynamics while imposing formal responsibilities, such as taxes that had been shouldered by larger companies¹²⁴⁹. The MSME Development Act of 2006 solidified this transition—integrating manufacturing/service definitions, establishing a National Board, and initiating Udyog Aadhaar (2015)—while increasing procedural requirements. The digital compliance age from

¹²⁴⁶ Anstey, Vera. "Indian Economic Planning." *Pacific Affairs* 23, no. 1 (1950): 83–86. <https://doi.org/10.2307/2753758>.

¹²⁴⁷ https://www.researchgate.net/publication/5125123_Informality_and_Regulations_What_Drives_Firm_Growth

¹²⁴⁸ MANNA, G C. "Current Status of Industrial Statistics in India: Strengths and Weaknesses." *Economic and Political Weekly* 45, no. 46 (2010): 67–76. <http://www.jstor.org/stable/25764127>.

¹²⁴⁹ Coad, Alex, and Jaganaddha Pawan Tamvada. "Firm Growth and Barriers to Growth among Small Firms in India." *Small Business Economics* 39, no. 2 (2012): 383–400. <http://www.jstor.org/stable/41682804>.

2014–2026 within Atmanirbhar Bharat heightened formalization: Udyam Portal (2020, turnover-based criteria: Micro $\leq ₹1/5cr$, Small $\leq ₹10/50cr$, Medium $\leq ₹50/250cr$), GST (2017), four Labour Codes (2019–20, merging 29 laws while maintaining 486 imprisonment clauses), and ECLGS credit linked to registration. This shift—from protective nurturance to compliance enforcement—promised “ease of doing business” but resulted in over 1,450 annual requirements, turning MSMEs from policy beneficiaries to regulatory subjects trapped in notice-based enforcement, where scale-neutral regulations generate significant inequality.

9. Conceptual Framework: Regulation, Enforcement, and Structural Bias

The conceptual framework of this study is based on the interaction between regulation, enforcement, and the establishment of structural bias in regulatory governance that affects MSMEs. Regulation, in its classical definition, refers to the State's establishment of legal rules, standards, and processes to regulate economic and social behavior. Regulation of MSMEs is officially described as facilitative, with the goal of promoting formalisation, ensuring access to funding, standardising compliance, and integrating firms into the formal sector. However, regulation cannot be reduced to rule-making alone; its true influence is decided by how those regulations are applied. Enforcement is the operational dimension of regulation¹²⁵⁰. It comprises inspections, notice issuing, adjudication, penalty imposition, and regulatory bodies' discretionary decision-making. In terms of legal governance, enforcement is more than just mechanical implementation; it is an exercise of administrative authority that involves judgment, interpretation, and discretion. While discretion is inherent and frequently required in regulatory systems, its

use within procedurally complicated frameworks can result in uneven outcomes when applied to entities with dramatically differing capacities, such as MSMEs and major corporations.

Structural bias occurs when ostensibly neutral regulatory systems produce consistently uneven outcomes. MSME regulations are often consistent and capacity-neutral, assuming equal ability to comply¹²⁵¹. However, MSMEs differ greatly from bigger businesses in terms of financial resources, legal competence, administrative infrastructure, and risk-absorption ability. When compliance duties are thick, timeframes are rigorous, and fines are automated, MSMEs are disproportionately vulnerable to procedural errors. These defaults are subsequently considered regulatory infractions, resulting in enforcement processes that heighten legal and financial vulnerability. The interplay of procedural complexity and regulatory discretion is critical to the emergence of structural bias. Multiple filings, overlapping jurisdictions, frequent law changes, and technologically driven compliance systems all contribute to procedural complexity. Discretion functions at several phases, including inspection selection, interpretation of compliance failures, penalty calculation, and adjudicatory results. In the absence of strong protections such as proportionality, openness, and rational decision-making, discretion can exacerbate rather than correct imbalances.

9.2 Nature of Discretion in Regulatory Enforcement

Administrative authorities must utilize discretion while enforcing regulatory requirements. Discretion is the legally sanctioned discretion of regulators to select between numerous lawful courses of action while enforcing legislative obligations. In the context of MSME regulation, discretion is used at many phases of enforcement, such as inspection, notice issuing,

¹²⁵⁰ Ramakumar, R., and Tejal Kanitkar. “IMPACT OF COVID-19 PANDEMIC ON THE INDIAN ECONOMY: A CRITICAL ANALYSIS.” *Investigación Económica* 80, no. 315 (2021): 3–32. <https://www.jstor.org/stable/26965501>.

¹²⁵¹ Coad, Alex, and Jaganaddha Pawan Tamvada. “Firm Growth and Barriers to Growth among Small Firms in India.” *Small Business Economics* 39, no. 2 (2012): 383–400. <http://www.jstor.org/stable/41682804>.

compliance requirement interpretation, violation adjudication, and penalty implementation. While discretion is required to provide flexibility and contextual decision-making, uncontrolled or inconsistent use can result in arbitrariness and uneven consequences¹²⁵². In theory, regulatory discretion allows authorities to adapt enforcement actions based on the magnitude of the infringement, the regulated entity's purpose, and the circumstances. The principles of proportionality, rationality, and natural justice are supposed to govern this judgment. However, in practice, discretion is frequently used in procedurally strict and resource-constrained administrative organizations. Enforcement authorities are influenced by institutional constraints, performance expectations, risk-averse bureaucratic attitudes, and inadequate supervision, all of which determine how discretion is used on the ground.

For MSMEs, the discretionary nature of enforcement increases their susceptibility. Decisions on whether to conduct inspections, issue show-cause notices, excuse procedural violations, or apply fines are usually ambiguous and unexpected. Minor or unintended procedural defaults, such as late files, typographical mistakes, or technical noncompliance, may be construed as substantive infractions, resulting in fines disproportionate to the harm caused. The lack of clear statutory rules distinguishing between deliberate non-compliance and capacity-induced default exacerbates the situation. Furthermore, discretion exerted via automatic or semi-automated digital technologies adds a new level of enforcement risk. Algorithm-driven alerts and uniform punishment systems decrease human judgment while eliminating contextual evaluation, thereby turning discretion into inflexible consequences. MSMEs,

who are inexperienced with digital compliance interfaces or frequent regulatory changes, are disproportionately affected by these systems. Thus, discretion in regulatory enforcement is not neutral. When discretion is incorporated in complicated procedural systems and used without proper protections, it becomes a point where regulatory purpose differs from regulatory impact. In the MSME context, this disparity leads to structural bias, transforming regulation from a facilitative tool to a source of legal ambiguity and survival risk¹²⁵³. For MSMEs, the discretionary nature of enforcement increases their susceptibility. Decisions on whether to conduct inspections, issue show-cause notices, excuse procedural violations, or apply fines are usually ambiguous and unexpected. Minor or unintended procedural defaults, such as late files, typographical mistakes, or technical noncompliance, may be construed as substantive infractions, resulting in fines disproportionate to the harm caused¹²⁵⁴. The lack of clear statutory rules distinguishing between deliberate non-compliance and capacity-induced default exacerbates the situation.

Discretion appears asymmetrically between companies. Larger companies, which have access to legal counsel and compliance infrastructure, are better positioned to interact with regulators, seek clarity, negotiate results, and fight enforcement actions. In contrast, MSMEs frequently lack the institutional infrastructure to challenge discretionary choices, rendering them more vulnerable to negative enforcement results.

9.3 MSMEs: Subjects of Regulatory Power

MSMEs are frequently represented in policy discourse as the recipients of regulatory assistance and facilitative governance. However, in terms of legal and regulatory

¹²⁵² Amaeshi, Kenneth, Emmanuel Adegbite, Chris Ogbecchie, Uwafiokun Idemudia, Konan Anderson Seny Kan, Mabumba Issa, and Obianuju I. J. Anakwue. "Corporate Social Responsibility in SMEs: A Shift from Philanthropy to Institutional Works?" *Journal of Business Ethics* 138, no. 2 (2016): 385–400. <http://www.jstor.org/stable/24755875>.

¹²⁵³ Pyngavil, Rajesh S. "Leadership Dimensions & Organizational Commitment in Small Scale Enterprises in Delhi." *Indian Journal of Industrial Relations* 50, no. 3 (2015): 479–93. <http://www.jstor.org/stable/24549109>.

¹²⁵⁴ Dey, Debanjana. "Are Small-Sized Firms Really Innovative? Understanding the Indian Scenario." *Current Science* 112, no. 6 (2017): 1121–26. <http://www.jstor.org/stable/24912636>.

governance, MSMEs are more than just receivers of incentives; they are also regulated subjects. This orientation becomes clear when MSMEs are analyzed through the perspective of enforcement, compliance duties, and administrative control rather than just legislative purpose. Regulatory authority functions through legislative norms, procedural constraints, and enforcement mechanisms that shape how businesses run. As MSMEs enter the formal economy, they are susceptible to ongoing regulatory monitoring in a variety of areas, including taxes, labor welfare, environmental compliance, licensing, and industry-specific legislation. Compliance is continuous, involving regular filings, disclosures, audits, and conformity to changing regulatory criteria. In this approach, MSMEs are regulated by compliance protocols that discipline organizational behavior.

The subjectification of MSMEs happens when regulatory compliance is transformed into a need for legal and economic existence. Registration under schemes such as Udyam, GST enrollment, and labour law digitalization not only provides advantages, but also integrates businesses into enforcement networks¹²⁵⁵. Noncompliance, whether procedural or accidental, results in regulatory repercussions such as notifications, fines, interest obligations, and legal procedures. These processes establish MSMEs as accountable legal persons whose survival is dependent on continued procedural compliance. Unlike bigger businesses, MSMEs face regulatory authority asymmetrically. Their insufficient administrative capacity, lack of in-house legal experience, and budgetary restrictions hinder their ability to grasp complicated regulations, respond effectively to enforcement activities, or defend adverse rulings. As a result, regulatory power is perceived as a coercive force that molds management decision-making, risk behavior,

and operational goals, rather than as a neutral governance instrument. Compliance becomes defensive, aiming to avoid fines rather than achieving progress.

Furthermore, regulatory power is applied through the discretionary authority granted to enforcement personnel. MSMEs rely on administrative judgment since they can inspect, issue notifications, condone defaults, or apply fines. This reliance is stronger when procedural protections are lax or inconsistently enforced. The absence of open criteria for enforcement decisions increases MSMEs' uncertainty and compliance concerns¹²⁵⁶. Viewing MSMEs as regulatory subjects suggests a movement away from protection-oriented regulation and toward governance through enforcement. Regulation does more than just promote market participation; it actively shapes the circumstances under which MSMEs operate, survive, and depart the market. This viewpoint emphasizes the need to rethink MSME regulation not only in terms of economic incentives and adoption rates, but also in terms of power dynamics, legal vulnerability, and procedural fairness within regulatory frameworks.

9.4 Procedural Complexity as a Regulatory Hazard

Procedural intricacy in India's MSME regulatory framework appears as a tangled network of statutory submissions, unnecessary paperwork, conflicting jurisdictional demands, and excessively frequent reporting duties that turn ordinary compliance into a formidable administrative challenge¹²⁵⁷. Manufacturing MSMEs face more than 1,450 unique regulatory requirements each year across seven legal categories—labor, taxation, environment, factories, shops/establishments, electricity duties, and boiler regulations—requiring oversight of 48 registers and interactions with

¹²⁵⁵ Comyn, Paul. "Linking Employment Services, Skills Development & Labor Market Needs: Issues for India." *Indian Journal of Industrial Relations* 49, no. 3 (2014): 378–88. <http://www.jstor.org/stable/24546984>.

¹²⁵⁶ Deshpande, Ashwini, and Smriti Sharma. "Disadvantage and Discrimination in Self-Employment: Caste Gaps in Earnings in Indian Small Businesses." *Small Business Economics* 46, no. 2 (2016): 325–46. <http://www.jstor.org/stable/43895708>.

¹²⁵⁷ MAIRA, ARUN. "Jobs, Growth, and Industrial Policy." *Economic and Political Weekly* 49, no. 34 (2014): 35–39. <http://www.jstor.org/stable/24480913>.

59 types of inspectors. Digitalization through GSTN portals, Udyam registration, and Shram Suvidha worsens this complexity instead of simplifying it: GST requires over 37 returns in a three-level cascade (GSTR-1, 3B, reconciliation), while labor codes necessitate 29 combined returns that still involve more than 100 data points every month. Procedural inflexibility escalates with the 9,331 regulatory updates for FY 2024-25 with 90% affecting MSMEs directly, resulting in continuous "regulatory whiplash," where compliance from yesterday turns into today's infringement. This complexity raises compliance from mere operational cost to an existential risk, as MSMEs—without specialized compliance teams or internal legal advisors—spend 8-12% of turnover to manage informational disparities and bureaucratic burden. Technical defaults prevail: delayed GSTR-3B submissions, discrepancies in invoice reconciliations, or missing Form-V in pollution consents result in automated notifications under GST Section 122 or EPA 1986, regardless of significance. In contrast to large organizations that have ERP-integrated compliance teams, MSMEs depend on local CAs managing various clients, resulting in 85% defaults due to capacity limitations rather than intentional avoidance. Enforcement views these as significant violations, starting notice-driven adjudications that shift the burden of proof—MSMEs are required to refute infractions in 15-30 day periods with responses over 100 pages, depleting working capital through 18% interest accumulation and legal costs.

The risk materializes in escalating enforcement: one procedural misstep leads to widespread multi-jurisdictional examination. GST late fees result in Section 73/74 show-cause notices, inconsistencies in labor registers lead to imprisonment risks under Code on Wages Section 59, and delays in environmental Form submissions cause Pollution Control Board shutdowns. In the absence of legal differences between capacity-related mistakes and intentional non-compliance, MSMEs fall into "penalty debt traps" where accumulated fines

diminish liquidity, leading to reductions in output of 20-30% or business closures. This procedural maze contradicts the purpose of regulation: formalization initiatives such as Udyam connect MSMEs to compliance frameworks without enhancing capacity, making "ease of doing business" a disguise for life-threatening intricacy.

10. Conclusion

This research fundamentally contests the prevailing facilitative narrative regarding India's MSME regulatory framework, demonstrating through doctrinal analysis how procedural intricacy and discretionary enforcement have altered intended economic empowerment into systemic subjugation. Through the evolutionary trajectory outlined—from pre-Independence protection to the market exposure of liberalization and now to the current complexity of digital compliance MSMEs have transitioned from policy beneficiaries with product reservations and preferential lending to subjects under regulation burdened by over 1,450 annual obligations related to GST layers, labor code inspections, MSME Act payment challenges, and environmental approvals. The theoretical framework highlights this contradiction: rules that are neutral in scale, executed via strict procedures and unstructured discretion, consistently result in significant inequality, favoring "Repeat Players" equipped with compliance systems while penalizing "One-Shotters" whose 85% defaults arise from limited capacity instead of avoidance. Crucial observations validate the main argument—regulatory strain emerges as systemic bias when notification-driven judgments reverse proof burdens, technical errors lead to excessive penalties, and enforcement discretion is devoid of proportionality measures, exacerbating the industry's 70% attrition rate over five years despite accounting for 30% of GDP and creating 110 million jobs. Literature deficiencies are addressed by transforming MSMEs from TAM/UTAUT conceptual adopters into proactive entities of regulatory influence, where protective compliance replaces growth

and "ease of doing business" appearances conceal bureaucratic difficulties. Research goals achieved: procedural dangers measured, enforcement disparities revealed, and discretion's variable range doctrinally analyzed, addressing whether these dynamics increase vulnerabilities and whether fairness principles can alleviate burdens).

The importance strikes a chord theoretically, practically, and normatively—providing "structural bias" as an analytical framework for regulatory governance while furnishing policymakers with recalibration mechanisms: penalty caps tied to turnover, MSME ombudspersons, digital transparency dashboards, and thresholds for decriminalization. Without these, formalization undermines its beneficiaries, diminishing economic resilience in the face of global supply chain pressures.

11. Key findings

The study concludes that, although being supposed to be "scale-neutral", India's regulatory frameworks produce substantively uneven outcomes. The study demonstrates that the present legal architecture benefits "Repeat Players" while punishing "One-Shotters" (MSMEs). Large corporations can bear compliance expenses and negotiate discretionary results, but SMEs lack the in-house legal competence and financial strength to do so. As a result, what appears to be a neutral regulation on paper becomes a structural bias in practice, since the regulatory system unintentionally targets smaller enterprises' capacity restrictions rather than their willingness to comply. Contrary to the official narrative of "ease of doing business," the report discovers that the push for formalization has resulted in a situation of "compliance density." MSMEs face about 1,450 legal duties and hundreds of regulatory changes each year in labor, tax, and environmental regimes. The data show that compliance has evolved from a strategic business decision to an "administrative nightmare." The complexity

stems not only from the legislation themselves, but also from redundancy in paperwork, the frequency of necessary filings, and overlapping jurisdictional requirements. Crucially, the article discovers that the majority of procedural defaults by MSMEs are caused by "informational asymmetry" and "administrative overload" (incapacity), yet enforcement mechanisms perceive these technical errors as serious as purposeful disobedience.

The study cites regulatory discretion and the flexibility given to enforcement officials as a major source of legal vulnerability for MSMEs. In the lack of clear proportionality rules, enforcement authorities frequently use arbitrary power during inspections and penalty assessments. The system has gradually turned toward "notice-based adjudication," in which the burden of evidence is essentially flipped, locking MSMEs in a loop of responding to show-cause notifications to demonstrate their innocence. The findings reveal a major problem in the enforcement mechanism: it fails to discriminate between unintentional procedural breaches and substantive infractions, penalizing both equally harshly. Finally, the findings call for a theoretical shift in how MSMEs are perceived in legal literature. The article contends that MSMEs should no longer be considered as "beneficiaries" of government schemes or passive users of technology, but rather as "subjects of regulatory power." They are perpetually defensive, preferring penalty avoidance over corporate development. The study reveals a severe governance vacuum, highlighting the existing regime's lack of procedural fairness, accountability, and openness. The MSME is therefore placed in a position of legal fragility, with its survival endangered not just by market competition, but also by the State's administrative apparatus.

12. Suggestions and Recommendations

To address the structural biases noted in this study and realign India's MSME regulatory framework with its intended facilitative purpose, policymakers need to execute a comprehensive

reform strategy highlighting statutory proportionality, institutional accountability, digital transparency, and capacity-building protections. These actions would reduce excessive penalties that presently take up 8-12% of micro-unit turnover, recovering over ₹50,000 crore in locked working capital each year while maintaining a deterrent against significant non-compliance.

Institutionally, create District-Level MSME Regulatory Ombudsmen modeled after RBI's banking ombudsman, authorized to suspend penalties over ₹1 lakh, require reasoned orders within 30 days, and perform random audits of enforcement discretion—diminishing unpredictability in inspection triggers and notice issuance. Enhance this by adding a National Enforcement Transparency Dashboard that merges GSTN, Shram Suvidha, and Pollution Control Board data to publicly reveal risk-assessment standards, officer decision logs, quarterly penalty statistics, and MSME appeal success rates, promoting accountability and facilitating peer comparison. Implement a Unified MSME Compliance Assistant digitally as an AI chatbot that consolidates 80% of 1,450 obligations into yearly filings with pre-filled templates, multilingual assistance, and predictive default notifications—reducing cognitive strain for the 85% of business owners lacking digital skills. Implement a process that requires pre-adjudication conciliation for every show-cause notice, extending the response periods to 45 days while providing free legal aid connections through Udyam registration, and establish legal proportionality guidelines that obligate enforcement officers to record capacity evaluations prior to determining penalties.