

# Charting the GST Journey For SMEs In India: Compliance, Challenges, And Growth Pathways

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## Abstract:

This paper analyses India's Goods and Services Tax (GST) regime through the lens of small and medium enterprises (SMEs), focusing on compliance realities, legal design, and growth outcomes. It evaluates whether GST has advanced core objectives such as reducing tax cascading, strengthening the input tax credit (ITC) chain, and facilitating inter-State trade, while also identifying continuing frictions that fall disproportionately on smaller firms. The study examines how turnover-based registration thresholds and the composition levy influence decisions on formalisation, scale, and participation in B2B supply chains. It further reviews the operational impact of return filing architecture, portal dependency, e-way bill and e-invoicing requirements, and the conditions attached to ITC, including mismatch risks and credit reversals. Particular attention is paid to liquidity and working capital effects arising from timing mismatches between outward tax liability, delayed or denied ITC, and refund processes for exporters and inverted duty structures. Methodologically, the paper adopts a doctrinal and analytical approach, reading the CGST and IGST framework with relevant rules, notifications, and judicial trends, and triangulating these with secondary literature and material to connect legal norms with SME business realities. It concludes with targeted reform propositions aimed at simplification, predictability, and reduced compliance cost for smaller taxpayers.

**Keywords:** Goods and Services Tax (GST), Small and Medium Enterprises (SMEs), GST Compliance and Procedural Framework, Input Tax Credit (ITC) Mechanism, Working Capital and Liquidity Impact.

## I. INTRODUCTION

### A. Background of Research

The small and medium enterprise segment occupies a central place in India's production structure, since official reports attribute to it a large share in national income and employment.<sup>1</sup> This segment covers household units, informal traders, small manufacturers and service providers, many of whom work with low margins and limited tax literacy, so any change in the indirect tax regime hits their survival and growth prospects.

The pre GST framework placed central excise, service tax, State value added tax, entry tax and several cesses side by side, which created cascading and overlapping jurisdictions that small firms struggled to handle.<sup>2</sup> They needed multiple registrations and separate returns, and often lacked resources to challenge assessments or penalties, so in practice the system favoured larger entities that could hire advisers and litigate.

<sup>1</sup> Ministry of Micro, Small and Medium Enterprises, Government of India, Annual Report 2023–24 (Ministry of MSME 2024) <https://msme.gov.in> (last visited 24 January 2026).

<sup>2</sup> Government of India, Report of the Task Force on Goods and Services Tax (Department of Economic Affairs 2009) 3–10 <https://dea.gov.in> (last visited 24 January 2026).

The move towards a destination based goods and services tax rested on a constitutional redesign through Articles 246A and 269A and on the enactment of the Central Goods and Services Tax Act 2017, the Integrated Goods and Services Tax Act 2017, the Union Territory Goods and Services Tax Act 2017 and the Goods and Services Tax (Compensation to States) Act 2017.<sup>3</sup> These enactments aim to create a common national market and rely on electronic registration, invoice level reporting and risk based audit, so they transform how SMEs document supplies, track input tax credit and interact with tax authorities. Policy makers presented GST as a simplification for small taxpayers, because higher registration thresholds, the composition scheme and rationalised rate slabs aimed to reduce formal burdens on low turnover entities. Yet the compliance architecture built under the Central Goods and Services Tax Rules 2017, e way bill regulations and later e invoicing obligations has drawn even micro and small units into a tight digital grid, where a delay or mismatch can block credits and squeeze fragile working capital cycles.<sup>4</sup> Parallel legal and policy developments under the Micro, Small and Medium Enterprises Development Act 2006 and allied schemes now link formal behaviour, including the filing of GST returns, to access to institutional credit and market support. With Udyam registration and digital platforms, governments, banks and large buyers read GST data as a signal of reliability, while jurisprudence in cases such as *Union of India v VKC Footsteps India Pvt Ltd*, (2022) 2 SCC 603, keeps shaping the rights and obligations of registered persons, so the GST journey of SMEs unfolds in a dynamic legal setting.<sup>5</sup>

## B. Research Questions

1. To what extent has GST reduced the multiplicity and cascading effects of the pre-GST indirect tax regime for Indian SMEs, and what residual compliance complexities continue to persist?
2. How do GST registration thresholds and the composition scheme influence SME decisions on formalisation, market expansion, and remaining within a “threshold trap”?
3. What are the principal GST compliance pain points for SMEs in practice, particularly return filing, input tax credit (ITC) matching, e-way bills, and e-invoicing, and how do these affect operating continuity?
4. How has GST affected SME liquidity and working capital cycles, especially through ITC restrictions, mismatch-driven credit denial risks, and refund delays for exporters and inverted duty structures?

## C. Objectives of the Study

1. To evaluate GST’s effectiveness in addressing pre-GST structural issues (cascading, overlapping levies) while identifying new procedural burdens that disproportionately affect SMEs.
2. To analyse the legal and practical implications of turnover-linked thresholds and the composition scheme on SME behaviour, including incentives and disincentives for growth and formal participation.
3. To map key compliance frictions faced by SMEs under the GST ecosystem (returns, ITC conditions, portal dependency, e-way bills, e-invoicing) and assess their operational impact.
4. To assess GST’s working capital impact on SMEs by examining the timing of tax liability, ITC availability and disputes, and refund experiences, and to propose targeted, legally workable reforms.

<sup>3</sup> The Central Goods and Services Tax Act 2017, No 12 of 2017 (India); The Integrated Goods and Services Tax Act 2017, No 13 of 2017 (India); The Union Territory Goods and Services Tax Act 2017, No 14 of 2017 (India); The Goods and Services Tax (Compensation to States) Act 2017, No 15 of 2017 (India).

<sup>4</sup> Central Board of Indirect Taxes and Customs, Central Goods and Services Tax Rules 2017 (as amended up to 31 March 2024) <https://taxinformation.cbic.gov.in> (last visited 24 January 2026).

<sup>5</sup> Micro, Small and Medium Enterprises Development Act 2006, No 27 of 2006 (India); *Union of India v VKC Footsteps India Pvt Ltd* (2022) 2 SCC 603.

## D. Research Methodology

This study adopts a doctrinal and analytical legal research methodology, supported by descriptive policy analysis. It examines the constitutional basis of GST (Articles 246A and 269A) and analyses the statutory framework under the CGST Act, IGST Act, UTGST Act, the GST (Compensation to States) Act, and the CGST Rules, with focused attention on provisions affecting SMEs such as registration thresholds, the composition levy, return filing architecture, and ITC entitlement and restrictions. The doctrinal analysis is supplemented by a review of relevant judicial pronouncements shaping SME outcomes (including refund and ITC jurisprudence) and by secondary materials such as official reports, circulars, compliance cost studies, and empirical literature to identify implementation-level frictions. Findings are synthesised using issue-based analysis to connect legal rules with SME operational realities, culminating in reform-oriented suggestions aligned with statutory design and administrative feasibility.

## II. GST AND THE SME SECTOR IN INDIA: CONCEPTUAL AND LEGAL OVERVIEW

### A. Definition and Economic Significance of SMEs in India

The legal understanding of small and medium enterprises in India now rests mainly on the Micro, Small and Medium Enterprises Development Act 2006, read with the revised criteria notified in 2020 that combine investment and turnover.<sup>6</sup> The framework classifies micro enterprises as those with investment up to one crore rupees and turnover up to five crore rupees, small enterprises up to ten crore investment and fifty crore turnover, and medium enterprises up to fifty crore investment and two hundred fifty crore turnover, which creates a uniform national benchmark that also guides fiscal and tax policy design.

The move from purely investment based thresholds to a joint investment and turnover test sought to reflect contemporary business models, where asset light structures and digital operations may generate significant sales without heavy plant and machinery, and where services and manufacturing receive equal treatment. This unified definition applies across the Union and the States, and government departments, public sector undertakings and financial institutions now use it to target schemes, procurement norms and credit products, so GST policy for small taxpayers operates in tandem with this classification.<sup>7</sup>

The economic footprint of MSMEs within the broader SME universe remains very large, since official estimates attribute around thirty percent of India's gross domestic product to the sector, along with roughly forty five percent of exports and a major share of non farm employment. The majority of these units operate in manufacturing clusters, trading networks and service activities that sit inside complex value chains, where they supply components, intermediate goods or outsourced services to larger firms, so any change in indirect tax rules immediately travels along these chains.<sup>8</sup>

A significant proportion of Indian SMEs continue to function in the informal or semi formal space, using cash based transactions, unregistered labour and fragmented record keeping.<sup>9</sup> The introduction of GST, with its insistence on invoice level reporting, input tax credit trails and electronic waybills, pushes many of these enterprises toward formal registration once they cross the basic threshold or when they wish to sell to larger registered buyers, and thus the legal definition of SME starts to overlap with the tax concept of a "registered person".

The sector also shows a pronounced dominance of micro enterprises in numerical terms, since they account for more than ninety five percent of all MSME units, while small and medium enterprises form only a thin

<sup>6</sup> Micro, Small and Medium Enterprises Development Act 2006, No 27 of 2006 (India); Ministry of Micro, Small and Medium Enterprises, Government of India, 'Atmanirbhar Bharat Abhiyan – New Definition of MSMEs' (Press Release, 26 June 2020) <https://msme.gov.in> (last visited 24 January 2026).

<sup>7</sup> Office of the Development Commissioner MSME, Clarification on New MSME Classification and Composite Criteria (DC MSME 2021) <https://dcmsme.gov.in> (last visited 24 January 2026).

<sup>8</sup> Ministry of Micro, Small and Medium Enterprises, Government of India, Annual Report 2023–24 (Ministry of MSME 2024) 5–10 <https://msme.gov.in> (last visited 24 January 2026).

<sup>9</sup> Reserve Bank of India, Report of the Expert Committee on Micro, Small and Medium Enterprises (RBI 2019) 9–17 <https://rbi.org.in> (last visited 24 January 2026).

upper layer but contribute disproportionately to output and exports.<sup>10</sup> This structural feature means that GST design must address two different realities at once, because micro units struggle with basic digital access and compliance literacy, while relatively larger SMEs seek stability in input tax credit flows, export refunds and cross border supplies.

## B. Overview of the Pre-GST Indirect Tax Framework for Small Businesses

The indirect tax structure that existed before GST rested on several parallel levies, such as central excise duty on manufacture, State value added tax on sale within the State, service tax on specified services, along with entry tax, octroi and various cesses.<sup>11</sup> For a small business this meant different taxable events, different laws and different authorities for closely related transactions.

Central excise law under the Central Excise Act 1944 taxed manufacture beyond a small scale exemption, State VAT statutes taxed intra State sale of goods, while the Finance Act 1994 imposed service tax on notified services.<sup>12</sup> A small unit that manufactured goods, traded them locally and bundled a service element often had to track three separate regimes, maintain separate records and reconcile assessments, which many SMEs struggled to do consistently.

Cascading of taxes formed a core defect of this framework, because credit did not flow smoothly across the chain or across different levies.<sup>13</sup> CENVAT credit covered specified duties and service tax at the central level, and input tax credit existed within each State VAT system, but small firms could rarely offset central levies against State VAT or vice versa, so embedded tax turned into part of the cost of production and distribution.

Exemptions and composition schemes added another layer of complexity, since different turnover thresholds applied under central excise, State VAT and local entry tax, and States experimented with their own simplified schemes for small traders.<sup>14</sup> As a result, a business might remain exempt from excise but still pay VAT, or pay local entry tax but enjoy some composition relief, which created confusion and sometimes arbitrary tax incidence for smaller entities.

## C. Objectives and Core Features of GST Relevant to SMEs

The stated objectives of GST include creation of a common national market, removal of cascading of taxes, greater neutrality between goods and services and improvement in the overall investment climate. Policy documents repeatedly link these goals with the need to lower transaction costs for small taxpayers, reduce distortions between States and provide a more level playing field to SMEs that wish to expand across regions.<sup>15</sup>

The dual GST model, with concurrent levies of Central Goods and Services Tax and State Goods and Services Tax on the same intra State supply, seeks to preserve fiscal autonomy while offering a single value added tax chain. On inter State supplies of goods or services the Integrated Goods and Services Tax

<sup>10</sup> Small Industries Development Bank of India, Report on the State of MSMEs in India 2022–23 (SIDBI 2023) 3–8 <https://www.sidbi.in> (last visited 24 January 2026).

<sup>11</sup> Thirteenth Finance Commission, Government of India, Report of the Task Force on Goods and Services Tax (15 December 2009) 3–6 <https://fincomindia.nic.in/asset/doc/commission-reports/13th-FC/reports/report291209.pdf> (last visited 24 January 2026).

<sup>12</sup> N Poddar and A Jain, Goods and Services Tax: A Practitioner's Guide (3rd edn, LexisNexis 2016) 15–28.

<sup>13</sup> Thirteenth Finance Commission, Government of India, Report of the Task Force on Goods and Services Tax (15 December 2009) 24–31 <https://fincomindia.nic.in/asset/doc/commission-reports/13th-FC/reports/report291209.pdf> (last visited 24 January 2026).

<sup>14</sup> Empowered Committee of State Finance Ministers, First Discussion Paper on Goods and Services Tax in India (10 November 2009) 5–10 [https://gstcouncil.gov.in/sites/default/files/2024-02/first\\_discussion\\_paper\\_on\\_gst.pdf](https://gstcouncil.gov.in/sites/default/files/2024-02/first_discussion_paper_on_gst.pdf) (last visited 24 January 2026).

<sup>15</sup> Empowered Committee of State Finance Ministers, First Discussion Paper on Goods and Services Tax in India (10 November 2009) 2–4 (last visited 24 January 2026).

operates as a destination based levy that credits the consuming State, so SMEs can in principle supply throughout India without facing the earlier patchwork of State entry taxes and local octroi.<sup>16</sup>

A central feature relevant to small businesses is the seamless input tax credit mechanism under Chapter V of the CGST Act 2017, which permits credit of tax paid on inputs, input services and, subject to conditions, capital goods. The legal design allows credit to flow across stages of value addition and between goods and services, so the tax burden should fall only on final consumption, not on intermediate SME producers or traders, provided they comply with invoice and return requirements.<sup>17</sup>

GST also pursues the objective of easing compliance for small taxpayers by prescribing turnover based thresholds for registration and by creating a composition scheme with lower tax rates and simplified returns. Sections 10 and 22 of the CGST Act fix these limits and authorise the Government, on Council recommendation, to revise them, which has been used to raise thresholds for goods oriented small businesses and thereby keep the smallest micro units outside the regular GST net.<sup>18</sup>

Another core feature lies in the use of a common IT backbone, the Goods and Services Tax Network, which supports online registration, return filing, payment and electronic ledgers. Self assessment under section 59, coupled with algorithm driven matching of outward and inward supplies, aims to reduce face to face contact with tax officers and to shift scrutiny to a data environment, which, if systems work smoothly, can reduce harassment risks for compliant SMEs but also demands basic digital capacity.<sup>19</sup>

Movement of goods now links to the e way bill system and, for specified thresholds and categories, to e invoicing requirements, both built under the CGST Rules 2017 and allied notifications.<sup>20</sup> These instruments try to curb evasion and to secure the credit chain by insisting that small transporters and suppliers generate verifiable electronic documents, so SMEs gain more reliable counterparties but also face strict real time compliance obligations that interact closely with their logistics and working capital cycles.

#### **D. Statutory Framework Applicable to SMEs**

The legal environment for SMEs in the GST era rests on a cluster of central statutes that operate together with State GST laws and the MSME specific framework under the Micro, Small and Medium Enterprises Development Act 2006. The Central Goods and Services Tax Act 2017, the Integrated Goods and Services Tax Act 2017, the Union Territory Goods and Services Tax Act 2017 and the Goods and Services Tax (Compensation to States) Act 2017 form the core of this design and directly or indirectly shape the compliance space within which small enterprises function.<sup>21</sup>

The Central Goods and Services Tax Act 2017 governs intra State supplies in most of India and defines key concepts such as “taxable person”, “registered person”, “aggregate turnover” and “supply”, which determine when and how an SME enters the GST net. Sections 22 and 23 fix turnover based thresholds for compulsory registration and for persons who are not liable, while section 24 lists categories requiring

<sup>16</sup> Central Board of Indirect Taxes and Customs, FAQs on Goods and Services Tax (GST) (31 December 2018) 6–9 (last visited 24 January 2026).

<sup>17</sup> Central Goods and Services Tax Act 2017, No 12 of 2017 (India) ss 16–18, 59; Central Board of Indirect Taxes and Customs, Central Goods and Services Tax Act, 2017 – Bare Act with Select Rules (CBIC 2022) 45–63 (last visited 24 January 2026).

<sup>18</sup> Central Goods and Services Tax Act 2017, No 12 of 2017 (India) ss 10, 22–24 (last visited 24 January 2026).

<sup>19</sup> Central Board of Indirect Taxes and Customs, FAQs on Goods and Services Tax (GST) (31 December 2018) 10–15 (last visited 24 January 2026).

<sup>20</sup> Central Goods and Services Tax Rules 2017, rr 46, 138A–138D; Central Board of Indirect Taxes and Customs, Central Goods and Services Tax Rules, 2017 (consolidated text as on 26 December 2022) (last visited 24 January 2026).

<sup>21</sup> Central Goods and Services Tax Act 2017, No 12 of 2017 (India); Integrated Goods and Services Tax Act 2017, No 13 of 2017 (India); Union Territory Goods and Services Tax Act 2017, No 14 of 2017 (India); Goods and Services Tax (Compensation to States) Act 2017, No 15 of 2017 (India) (last visited 24 January 2026).

mandatory registration irrespective of turnover, so the statute links tax status of small entities to measurable economic size but still pulls some low turnover units into the formal system.<sup>22</sup>

The composition levy under section 10 of the CGST Act, read with its accompanying rules, creates a special route for eligible small taxpayers who prefer a fixed rate on turnover and simplified returns instead of full input tax credit and detailed invoice matching. Manufacturers, traders and small restaurants below prescribed turnover limits may opt into this scheme, but they must accept restrictions on inter State supplies, on collection of tax from customers and on eligibility to claim input tax credit, which makes the statutory choice between regular and composition regimes a central strategic decision for SMEs.<sup>23</sup>

The Integrated Goods and Services Tax Act 2017 regulates inter State supplies and imports and exports of goods and services, and it matters to SMEs that sell across State borders or participate in global value chains. It defines when a transaction qualifies as inter State supply, fixes the charge of integrated tax and provides the framework for zero rated supplies, including exports and supplies to special economic zones, so smaller exporters rely on these provisions for refunds and for maintaining liquidity, even though procedural complexity sometimes discourages them.<sup>24</sup>

For SMEs located in Union Territories without their own legislature, the Union Territory Goods and Services Tax Act 2017 functions as the mirror of State GST law and levies tax on intra Territory supplies along with CGST. The Act adopts the same basic structure as the CGST Act on levy, valuation, input tax credit and administration, which ensures that small businesses in these territories face broadly comparable rules to their counterparts in States, though they interact with Union Territory administrations rather than State tax departments.<sup>25</sup>

The Goods and Services Tax (Compensation to States) Act 2017 does not impose day to day compliance duties on SMEs but it underpins the fiscal stability of the GST regime by promising compensation to States for revenue loss after the shift from the earlier tax system. By guaranteeing a formula based flow of compensation for a fixed period, the statute seeks to reduce State resistance to rate rationalisation and to wider base reforms, which indirectly affects SMEs by supporting a predictable tax environment and limiting the incentive for States to introduce distortionary local levies again.<sup>26</sup>

The Central Goods and Services Tax Rules 2017 supply the operational detail that SMEs actually meet in practice, covering registration, amendment and cancellation, the form and content of tax invoices, maintenance of accounts and records, returns, payment and refunds. Rules on registration procedures, electronic verification, issuance of GSTIN and physical verification of premises shape the ease with which a small unit can enter or exit the system, while invoice rules and record keeping obligations define the information trail that must be maintained to support input tax credit and to withstand audit.<sup>27</sup>

Subordinate legislation under these Rules also establishes the e way bill system for movement of goods and the architecture for e invoicing for specified categories of taxpayers, which now extend in stages to portions of the SME universe. Rule 138 and allied provisions require generation of electronic documentation for transport of goods above certain values and distances, while e invoicing standards prescribe machine readable invoice formats that integrate directly with the GST portal, so statutory compliance for SMEs now involves not just reading bare Acts but also adapting business processes to these digital instruments.<sup>28</sup>

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<sup>22</sup> Central Goods and Services Tax Act 2017, No 12 of 2017 (India) ss 2, 22–24 (last visited 24 January 2026).

<sup>23</sup> Central Goods and Services Tax Act 2017, No 12 of 2017 (India) s 10; Central Goods and Services Tax Rules 2017, rr 3–7 (last visited 24 January 2026).

<sup>24</sup> Integrated Goods and Services Tax Act 2017, No 13 of 2017 (India) ss 5, 7, 16 (last visited 24 January 2026).

<sup>25</sup> Union Territory Goods and Services Tax Act 2017, No 14 of 2017 (India) (last visited 24 January 2026).

<sup>26</sup> Goods and Services Tax (Compensation to States) Act 2017, No 15 of 2017 (India) (last visited 24 January 2026).

<sup>27</sup> Central Goods and Services Tax Rules 2017, rr 8–27, 46, 56–58 (last visited 24 January 2026).

<sup>28</sup> Central Goods and Services Tax Rules 2017, rr 46, 48, 138–138D (last visited 24 January 2026).

### III. GST COMPLIANCE EXPERIENCE OF SMEs

The first phase of GST implementation saw many SMEs struggle with migration from earlier tax registrations to GSTIN based registration, because the process demanded PAN validation, digital signatures and portal familiarity that smaller units often lacked. Field studies and official feedback reports indicate that many micro enterprises depended almost fully on tax practitioners or intermediaries for registration, and delays or errors at this stage disrupted their ability to issue valid tax invoices and continue supplies to larger buyers.<sup>29</sup>

Once registered, SMEs had to adapt to a new compliance rhythm structured around self assessment under section 59 of the CGST Act and periodic returns in electronic form, most notably GSTR 1 for outward supplies and GSTR 3B as a summary return. For firms that previously filed quarterly VAT returns on paper or through basic upload systems, the shift to multiple online returns, with stringent timelines, created anxiety and a sense of continuous monitoring, even if the statutory provisions formally promised simplicity and transparency.<sup>30</sup>

Input tax credit emerged as both an opportunity and a source of friction in the compliance experience of SMEs, because the scheme can reduce cascading if managed well, but it also requires strict adherence to documentation, matching and time limits under sections 16 and 17 of the CGST Act. Many small businesses reported difficulties in reconciling their purchase registers with auto populated data from suppliers, and in cases where suppliers defaulted, recipients saw their credits questioned, which they perceived as unfair since they had already paid the tax as part of the price.<sup>31</sup>

The e way bill system, created through rule 138 of the CGST Rules 2017, reshaped how SMEs move goods within and across States, since transport now needs generation of an electronic bill once the consignment value crosses a specified threshold. While the system reduced physical check posts and ought to speed up transit, small transporters and small consignors initially faced system downtime, data entry errors and penalties for minor lapses, so compliance became a daily operational concern rather than a periodic one.<sup>32</sup>

E invoicing requirements, introduced in phases for taxpayers above specified turnover limits, began to touch sections of the SME universe as thresholds came down, and this added another layer of real time reporting. Businesses that already used basic accounting software now needed tools that could generate IRN compliant invoices and integrate with the Invoice Registration Portal, which meant new costs, staff training and changes to invoicing practices that some smaller entities found difficult to absorb in the short run.<sup>33</sup>

SMEs also experienced GST compliance through the prism of working capital, because tax liability arises at the time of supply while input tax credit may be blocked, delayed or subjected to safeguards in sections 41 and 49A. Survey evidence shows that delays in refunds, especially for exporters and for those with inverted duty structures, strained cash flows and forced some units to rely on high cost short term borrowing, which diluted the promised efficiency gains of the new regime.<sup>34</sup>

The use of technology and data analytics by tax authorities, although justified on grounds of revenue protection, altered the perception of audit and enforcement among small businesses. Instead of sporadic physical inspections, SMEs now receive automated notices, system generated discrepancies and risk flagged communications, which demand timely and informed responses on the portal, and many units

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<sup>29</sup> Central Board of Indirect Taxes and Customs, GST – Concept & Status (CBIC 2020) 19–24 visited 24 January 2026.

<sup>30</sup> Central Board of Indirect Taxes and Customs, FAQs on Goods and Services Tax (GST) (31 December 2018) 16–25 (last visited 24 January 2026).

<sup>31</sup> Central Goods and Services Tax Act 2017, No 12 of 2017 (India) ss 16–17, 59 (last visited 24 January 2026).

<sup>32</sup> Central Goods and Services Tax Rules 2017, r 138 (last visited 24 January 2026).

<sup>33</sup> Central Board of Indirect Taxes and Customs, E-invoice – Frequently Asked Questions (Version 3.0, March 2023) 3–11 (last visited 24 January 2026).

<sup>34</sup> Federation of Indian Chambers of Commerce and Industry, Impact of GST on MSMEs (FICCI 2018) 9–15 (last visited 24 January 2026).

therefore depend even more heavily on external consultants to manage this interface with the administration.<sup>35</sup>

#### **IV. KEY CHALLENGES AND PAIN POINTS UNDER GST FOR SMEs**

SMEs often perceive the GST framework as legally dense and constantly shifting, because core provisions of the CGST and IGST Acts are supplemented by frequent notifications, circulars and Council decisions that alter rates, procedures and thresholds.<sup>36</sup> Many small units lack in house legal or tax teams, so each change in return design, in input tax credit conditions or in procedural timelines creates uncertainty, and they rely on informal advice that may not keep pace with formal amendments.

Turnover based thresholds and the choice between regular and composition schemes generate another layer of difficulty, since a small error in projecting turnover can expose an enterprise to retrospective liability or ineligibility.<sup>37</sup> Confusion about mixed supplies, inter State supplies and the impact of exempt income leads some SMEs to stay below the registration threshold deliberately, which restricts their ability to sell to organised buyers and fractures supply chains that GST law tries to integrate.

Input tax credit, although central to the GST design, remains one of the most contested areas in SME experience, particularly due to invoice mismatches, supplier non compliance and evolving safeguards on credit entitlement.<sup>38</sup> When suppliers fail to upload invoices or pay tax, the recipient SME faces pressure during scrutiny, even after paying the gross value, and studies report that owners see this as shifting the risk of enforcement from the State to small purchasers who have little control over their counterparties.

The digital character of GST compliance, with strict reliance on the GSTN portal, e way bills and in many cases e invoicing, makes technology a daily pain point for smaller firms.<sup>39</sup> Enterprises in semi urban and rural areas report unstable connectivity, limited access to reliable hardware and dependence on cyber cafes or third party service centres, so routine tasks like uploading returns or generating e way bills become time consuming, and any portal downtime close to due dates increases fear of late fees and penalties.

Compliance cost studies document that small businesses incur significant explicit and implicit costs for GST, including software licences, fees to tax practitioners and staff time diverted from core operations.<sup>40</sup> Empirical work for Tamil Nadu, for instance, finds that hours spent per month on GST compliance and related advisory costs form a noticeable share of total operating expenses for micro units, which makes the tax system feel regressive in administrative terms even when nominal rates are lower.

Judicial and administrative interpretations add another dimension of unpredictability, as seen in litigation on refund of accumulated input tax credit, place of supply or anti profiteering, which redefines risks for SMEs after they have already structured transactions.<sup>41</sup> Decisions such as *Union of India v VKC Footsteps India Pvt Ltd*, (2022) 2 SCC 603, upheld restrictions on refund of input services, and many smaller exporters experienced this as a sudden denial of expected cash flow, illustrating how high level doctrinal choices translate into day to day strain at the lower end of the market.

<sup>35</sup> Goods and Services Tax Network, GSTN Annual Report 2021–22 (GSTN 2022) 27–34 (last visited 24 January 2026).

<sup>36</sup> Ministry of Finance, Government of India, GST Reforms 2025: Relief for Common Man, Boost for Businesses (Department of Revenue, 4 September 2025) 3–8 (last visited 24 January 2026).

<sup>37</sup> Central Board of Indirect Taxes and Customs, FAQs on Goods and Services Tax (GST), Third Edition (15 December 2018) 11–18 (last visited 24 January 2026).

<sup>38</sup> V Shacheendran and others, ‘An Analysis of GST Barriers Faced by Business Owners in India’ (2024) *Vision: The Journal of Business Perspective* (advance online publication) (last visited 24 January 2026).

<sup>39</sup> Tejal Navrangani and Meghashree Dadhich, ‘GST Compliance Burden on Small Businesses in Gujarat’ (2025) 12(7) *International Journal of Innovative Research in Technology* 7792–7797 (last visited 24 January 2026).

<sup>40</sup> S Vishnuhadevi and D Hima Bindu, Compliance Costs of GST for Small Business Enterprises in Tamil Nadu (Working Paper 2022–229, Madras School of Economics 2022) 23–33 (last visited 24 January 2026).

<sup>41</sup> Abhishek Kumar, ‘Three Years of GST in India: A Progress Report after 36 Months of Implementation’ (2021) available at ResearchGate (last visited 24 January 2026).

## V. FINDINGS AND CONCLUSION

The research shows that GST rests on a robust statutory base but it does not treat SMEs as a distinct legal category, rather it reaches them indirectly through turnover thresholds, composition options and procedural relaxations. The combination of the CGST, IGST and UTGST enactments with the MSME Act therefore creates a layered framework where enterprise size in policy terms and tax status under GST only partially overlap, and this misalignment explains many of the frictions observed in practice.<sup>42</sup>

The analysis of the pre GST regime and the transition provisions confirms that GST has substantially reduced the formal multiplicity of indirect taxes, yet it has simultaneously replaced that multiplicity with a dense compliance architecture that weighs heavily on smaller entities. SMEs moved from fragmented but sometimes negotiable local systems into a unified but more automated structure, and this shift has redistributed legal risk rather than eliminating it, especially in areas like classification, place of supply and eligibility for input credit.<sup>43</sup>

Doctrinal examination of registration and composition provisions indicates that threshold increases and the widening of the composition scheme have offered genuine relief to very small businesses at the bottom of the spectrum. However, enterprises that sit just above these limits now shoulder a disproportionate share of compliance duties, and many respondents in empirical studies describe a “threshold trap”, where growth beyond a certain turnover looks unattractive because of the tax and reporting burdens it triggers.<sup>44</sup>

The study finds that input tax credit remains the core legal promise of GST for SMEs but also the principal source of dispute and anxiety, due to invoice matching rules, supplier non compliance and frequent doctrinal changes. Case law such as *Union of India v VKC Footsteps India Pvt Ltd* and administrative circulars on credit matching show a tendency to prioritise revenue protection over the position of bona fide small purchasers, so SMEs often perceive the credit system as uncertain despite its conceptual elegance.<sup>45</sup>

Evidence on digital systems, including GSTN, e way bills and e invoicing, suggests that technology has indeed removed many physical barriers and reduced face to face contact with officials, yet it has introduced new barriers of connectivity, interface complexity and dependency on intermediaries. For urban, better resourced SMEs, the digital layer slowly becomes routine, while micro and rural units often remain at the edge of the system, using ad hoc solutions that raise cost and increase error risks.<sup>46</sup>

Comparative reading of official reports and independent research reveals that SMEs do not experience GST as a purely legal or procedural issue; they experience it as part of a wider regulatory load that includes labour, environmental and municipal compliances. In this environment GST becomes one more demanding statute in a long compliance list, and the promised simplification sometimes gets lost in the cumulative effect of multiple overlapping obligations that owners must juggle with limited managerial bandwidth.<sup>47</sup>

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<sup>42</sup> Central Goods and Services Tax Act 2017, No 12 of 2017 (India); Micro, Small and Medium Enterprises Development Act 2006, No 27 of 2006 (India).

<sup>43</sup> Thirteenth Finance Commission, Government of India, Report of the Task Force on Goods and Services Tax (15 December 2009) 24–31 (last visited 24 January 2026).

<sup>44</sup> Ministry of Finance (Department of Revenue), Government of India, GST Reforms 2025: Relief for Common Man, Boost for Businesses (MoF 2025) 6–12 (last visited 24 January 2026).

<sup>45</sup> *Union of India v VKC Footsteps India Pvt Ltd* (2022) 2 SCC 603; Abhishek Kumar, ‘Three Years of GST in India: A Progress Report after 36 Months of Implementation’ (2021) available at ResearchGate (last visited 24 January 2026).

<sup>46</sup> Goods and Services Tax Network, Annual Report 2023–24 (GSTN 2024) 27–39 (last visited 24 January 2026).

<sup>47</sup> TeamLease RegTech, Regulatory Burden on Manufacturing MSMEs in India (Compliance Report 2025) as reported in ‘MSMEs Burdened by High Compliance Costs; Face over 1,450 Regulations Annually: Report’ The Times of India (29 June 2025) (last visited 24 January 2026).

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