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ICAI MSME ECOSYSTEM

ICAI MSME CLINIC™

Kerala State MSME Policy



Committee on MSME & Startup, ICAI

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Message from Committee Leadership

Dear MSME & Startup Stakeholders,

We are pleased to share details about the ICAI MSME Clinic, an initiative designed to provide valuable guidance, support, and professional assistance to MSMEs and Startups across the country. This weekly walk-in, pro-bono advisory service aims to address key challenges faced by MSMEs, including finance, accounting, technology support, human resources, operations, and marketing—collectively referred to as **FATHOM**.

About ICAI MSME Clinic

The ICAI MSME Clinic will be hosted every Friday by ICAI branches, where MSMEs and Startups can receive expert advice from two dedicated advisory desks:

- **Business Support Desk**: Led by Chartered Accountants specializing in MSME and Startup advisory, financial planning, compliance, and business strategy.
- **Institutional Support Desk**: Led by Bankers and Government Representatives, offering assistance with credit access, grievance redressal, and awareness of government schemes.

Introduction to the State-Specific MSME Policy

We are also excited to present the State-Specific MSME Policy, an essential resource for MSMEs & Startups in the ICAI MSME Clinic initiative. As part of this initiative, the Committee has developed a Resource Handbook and State-Specific MSME Policies, aimed at enhancing the knowledge base of MSMEs and Startups.

These State-Specific Handbooks serve as practical and accessible tools for navigating the unique opportunities, policies, and regulatory frameworks specific to each state. By consolidating available schemes, incentives, and support across states, we aim to provide MSMEs & Startups with the guidance they need to grow at the grassroots level and develop the capacity.

Vision of ICAI MSME Clinic

Through consistent, pro-bono engagement and sustainable operations, each branch becomes a local hub and incubation centre of MSME transformation, bridging professional excellence with grassroots economic development. ICAI aims to empower MSMEs & Startups annually, driving financial literacy, compliance discipline, and business growth.

Acknowledgement

We would like to extend our sincere gratitude to **CA George A. Kurian** for their tireless efforts and contributions in preparing the **State-Specific MSME Policy of Kerala**, which will play a crucial role in this initiative.

Commitment to MSME & Startup Growth

The Committee on MSME & Startup, ICAI, is deeply committed to ensuring the success of the ICAI MSME Clinic and providing continuous support to MSMEs & Startups. Together, we look forward to contributing to the sustainable growth and empowerment of MSMEs & Startups, which are the backbone of the Indian economy.

CA Gyan Chandra Misra
Chairman
Committee on MSME & Startup, ICAI

CA Arpit Kabra
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1. Introduction

Kerala, located on the south-west coast of India, stands as one of the country's most socially progressive and economically resilient states, distinguished by its high literacy levels, skilled workforce, and strong social inclusion framework. With over 580 kms of coastline, major ports at Kochi, Vizhinjam [Trivandrum], and Beypore [Calicut], along with robust road, rail, and air connectivity, the state serves as a strategic gateway for domestic and international trade. Kerala's emphasis on human development, knowledge-driven industries, strong healthcare and education systems, and technology-enabled governance has positioned it as a benchmark for sustainable regional growth. The rapid progress in technology and the rise of startups have further contributed significantly to employment generation and the state's economic development.

This compendium integrates key provisions from:

- *Kerala's Industrial Policy 2023*
- *Kerala Startup Vision 2030 and*
- *Entrepreneur Support Scheme (ESS)*

Ease of Doing Business reforms, and sector-specific schemes, providing a unified reference for enterprises, investors, and startups.

1.a. Policy Rationale: Coherence, Risk Mitigation, and Financial Assurance

A unified compendium is necessary at this stage because various policy documents and schemes currently operate across multiple departments, creating gaps in accessibility, clarity, and ease of navigation for stakeholders. Consolidating them strengthens policy coherence and supports Kerala's economic priorities, such as promoting high-value industries, enhancing investment readiness, and aligning the state's development trajectory with its *Net Zero 2050 target* and national initiatives.

1.b. The Governance Imperative and Risk Mitigation:

Kerala Government's policy to promote MSMEs, is futuristic and should be read in conjunction with Central regulatory and climate risk mandates for hard-to-abate sectors that it seeks to align with. The Policy aims to address *Governance, Climate, and Financial Risks*, that are unique to Kerala's high-density, ecologically fragile environment with a population density of about 859 persons/km^2, and with the 2018 floods inflicting on the state. Other calamities including the more recent Wayanad landslide and the coastal erosion due to capsizing vessels posed challenges in unsettled marine claims despite coastal ecosystem and collateral damages.

The Union MoEFCC approved the new **Coastal Zone Management Plan (CZMP)** for all 10 coastal districts of Kerala in October 2024, aligning with the relaxed norms of the **CRZ Notification, 2019**. This is a significant development as the new rules generally ease construction restrictions. Notably, the No Development Zone **(NDZ)** in densely populated areas (CRZ-III A) can be reduced from 200 meters to just **50 meters** from the High Tide Line (HTL). This change drastically reduces the overall NDZ area in Kerala from **239 sq. km**

(under the old 2011 norms) to an estimated **108 sq. km** under the new plan, impacting future coastal development.

While this plan governs future construction, the numerous existing CRZ violations identified under the stricter old norms will still need to be addressed by the Central Government, state government, the Port Operator, and the vessel owner through legal process, based on the rules that were in place when those structures were built.

This Compendium introduces the necessary *Financial Assurance Mandates* to de-risk the economy.

1.c. Key Highlights:

- **Human Capital:** Highest literacy and skill-ready workforce supporting knowledge-based and high-value industries.
- **Port Infrastructure:** World-class port infrastructure, including India's first deep-water trans-shipment hub at Vizhinjham [Trivandrum]
- **Digital Infrastructure:** Strong IT & digital infrastructure with Technopark (Thiruvananthapuram), Infopark (Kochi), and Cyberpark (Kozhikode) driving innovation.
- **Startup Ecosystem:** Robust ecosystem led by Kerala Startup Mission (KSUM) with 7000+ registered startups (as of 2025).
- **Risk Targeting:** Special emphasis on vital economic sectors (Construction, Shipping, Agriculture) where *Acute Asset Stranding and Maritime Liability Evasion* create systemic financial risk.

2. About the Policy [KERALA INDUSTRIAL, MSME & STARTUP POLICY COMPENDIUM (2025–2030)]

This policy provides a unified framework for promoting industrial growth, MSME competitiveness, and startup innovation in Kerala, with a focus on inclusivity, *mandatory assurance*, sustainability, and ease of doing business. The policy embeds stringent ESG principles across all stages of enterprise development and incentive delivery.

Policy and Risk Overrides:

The policy's Interest Subsidy and credit-linked schemes are designed to align with the *Reserve Bank of India (RBI) Banking Rules* (Reserve Bank of India, 2025**),** which encourage commercial banks to improve MSME credit behaviour. However, this compendium stipulates that such credit is conditional on verifying the underlying asset's resilience to climate and regulatory risk.

Enterprises operating in geographically and environmentally sensitive zones are essential to the state's economy, but they exhibit a high degree of operational and financial vulnerability. Central Government legislation concerning the management and allocation of natural resources introduces new environmental hazards and may reduce operational stability for these businesses. The Central government's new *Offshore Areas Mineral Amendment Act, 2023* poses a direct threat

to Kerala's MSME sector, specifically traditional fisheries and coastal tourism, and constrains the state MSMEs from contributing to UN sustainable development goals. The *Green Kerala Movement* officially opposes recent Central Government moves to auction offshore mineral blocks, viewing such activities as a direct threat to existing coastal economies and environmental stability.

A. Definitions:

i. MSME: Micro, Small and Medium Enterprises defined as per the MSMED Act.

ii. Start-ups: Entities registered with Kerala Startup Mission (KSUM) fulfilling government norms on innovation, age and turnover.

iii. Service Enterprises: Businesses offering services (not manufacturing), subject to eligibility criteria specified below.

iv. High-Risk Enterprises: Enterprises operating in the 10 coastal districts or designated ecologically sensitive zones (e.g., Western Ghats), for whom the Mandatory Climate and CRZ Risk Assurance Certificate (MCRAC) is required.

v. Rare minerals: Rare Minerals are those classified as Critical and Strategic Minerals and Atomic Minerals, they are essential for national security, economic development, and the clean energy transition, encompassing elements like Rare Earth Elements (REEs), Lithium, Cobalt, Nickel, Titanium, Niobium, Uranium, and Thorium.

B. Policy Period: 2025–2030

C. Applicability: All new and existing enterprises registered as MSMEs, startups, or industrial units operating in Kerala. Existing enterprises registered under Udyam will be auto migrated into the Compendium's system but must re-certify for new incentives.

D. Terms & Conditions for Extending Incentives and Concessions:

- Incentives apply only to units registered on the Single Window Clearance Portal, Udyam, or Startup Mission platform.
- Beneficiaries must maintain operations for 3–5 years from commencement to retain eligibility, PPP contracts allow extensions under forcemajeure, tied to the disruption's duration, not a fixed grace period. (e.g., natural disasters or supply chain shocks).
- Compliance with the Central Environment Audit Rules, 2025 is a prerequisite for retaining the Capital Investment Subsidy (CIS).
- **CRITICAL POLICY OVERRIDE:** While 'Red' category industries are excluded, *all enterprises operating in coastal districts or ecologically sensitive zones* (e.g., Western Ghats) are subject to mandatory **Financial Assurance Requirements**.
- **Misrepresentation or non-compliance,** *including failure to disclose material environmental/regulatory risks***,** will result in suspension or recovery of benefits**.**

Table 1.

List of Eligible Service Enterprises for Incentives

Eligible Service Enterprises	***Target Beneficiary Group***
IT / ITES & software development firms	All eligible; priority for women, SC/ST, minorities, differently abled, NRKs, nano/rural MSMEs
Logistics & warehousing operations	All eligible; Conditional on MCRAC compliance} (4.a) for assets in coastal or port-influenced areas.
Food processing and value-added service units	All eligible; special incentives for women, SC/ST, minorities, nano/rural enterprises.
Technical testing, design & R&D labs	All eligible.
Skill development, training and incubation centres	All eligible; priority for training in **Green Jobs** and carbon accounting expertise.
Export-oriented, creative and media service units	All eligible; prioritized for those seeking **CBAM** compliance certification.

Non-eligible Service Enterprises for Incentives:

- Trading and retail outlets (Excluded due to not contributing to high-value, sustainable job creation).
- Real Estate and Speculative activities.
- Alcohol-based industries (except pharma).
- Road-metal, quarrying and stone crushing units (excluded due to high environmental impact/Acute risk).
- Enterprises using > 25 % second-hand machinery.
- Brick manufacturing and ordinary earth excavation (excluded due to high environmental impact).

3. Policy Features & Incentives:

The policy introduces a comprehensive support system combining subsidies, innovation grants, ESG incentives, and digital facilitation.

A. Financial Incentives (Detailed Breakdown):

Type of Incentive	Details	Eligibility / Specific Criteria
Capital Investment Subsidy (CIS)	25–45% of Fixed Capital Investment (FCI) subject to a maximum of ₹40 Lakh (Micro), ₹100 Lakh (Small), and ₹200 Lakh (Medium).	All MSMEs. Additional 10% support for priority sectors or units in backward districts.

Type of Incentive	Details	Eligibility / Specific Criteria
Interest Subsidy	6–8% subsidy for 3 years on term loans. Max ₹10 Lakh per unit for nano/household enterprises.	Startups & MSMEs, designed to align with the RBI's **Priority Sector Lending (PSL)** targets (Ref 5)
Technology Upgradation Support	40% subsidy (₹50L–₹2Cr) for modernization, automation, and digital adoption.	**Priority for MSMEs transitioning away from Methane-emitting fuels** (LPG/LNG) and those in CBAM-affected sectors to manage **BRSR Scope 3** compliance risk.
Incentive for Sustainability & Responsible Industrialization	25% reimbursement of expenses incurred for setting up ETPs, installations for renewable power substitution, and Zero Discharge technologies. Maximum limit is up to ₹25 Lakh per unit.	All Category Units. This encourages self-regulation and mitigation in high-emission sectors.
SGST Reimbursement	100% SGST (State Goods and Services Tax) reimbursement on intra-state supply for 5 years or until full recovery of FCI.	Manufacturing Units.
Stamp Duty & Registration Fee Exemption	100% exemption on land purchases/leases.	All MSMEs. 100% exemption is available to Women, SC/ST, and Transgender entrepreneurs.
Energy Subsidy	₹1 – ₹1.25 per unit for 5 years. 25% capital subsidy up to 1 Cr, for installation of renewable energy systems/waste recycling facilities.	Manufacturing Enterprises. **Crucially, no subsidy is extended for new fossil fuel/ LNG bunkering infrastructure, as this increases methane risk.**
Export Incentive	1% support on annual export turnover for 3 years.	Export-Oriented Units.
Access to Finance via IPO Route	50% expense reimbursement (max ₹1 Cr) for MSMEs listing on the SME platform of NSE/BSE.	MSMEs seeking to scale and increase transparency.
Venture Capital Support (KSUM)	KSUM acts as a Limited Partner (up to 25%) in Kerala-focused venture capital funds, encouraging private capital flow.	KSUM-registered Startups and associated funds.

B. Non-Financial Support:

- **Incubation & Mentoring:** Over 60 incubators and 10 sectoral Centres of Excellence (CoEs) under KSUM in health tech, Agritech, Fintech, AI/Robotics, Marine tech, and more.

- **Skill Development & Training:** 40 ITIs and 19 polytechnics focusing on *Green Jobs* (solar maintenance, waste management), financial literacy, industrial safety, and *Carbon Accounting*.
- **Progressive Labour Reform:** Policy support for the proposed *Kerala Right to Disconnect Bill, 2025* [Ref. 9], aimed at protecting the well-being and productivity of private sector employees.
- **Support for Low-Digital-***Capacity MSMEs: Digital literacy programs, helpdesks at DICs, and the option of physical* **submission** of applications to ensure equitable access to incentives.
- **Cluster Development:** 200+ industrial clusters emphasizing *value-chain-focused modernization* for traditional sectors (coir, handloom, rubber) to enhance competitiveness and meet global ESG sourcing standards.

4. Financial Assurance and Climate Liability Policy (The Mandate Overrides)

This section mandates the integration of *ESG Governance and Financial Assurance* into regulatory and lending practices, directly addressing the core risks that have historically compromised the "True and Fair View" of Kerala's economy.

4.a. Mandatory Climate and CRZ Risk Assurance Certificate (MCRAC)

- **Rationale:** Unchecked coastal structures and the *Maradu Implosion* Supreme Court precedent, confirm that *CRZ violations and physical climate risk* lead to the instant and complete stranding of assets (Ref 10). This risk requires a dedicated assurance mechanism to protect the financial sector from catastrophic *Credit Risk* and unquantified *Loss Given Default (LGD).*
- Approval by MOEFCC's relaxation from October 2024, that **No Development Zone (NDZ)** in densely populated areas (CRZ-III A) to 50 mts from HTL.
- **Mandate:** All enterprises operating in the 10 coastal districts or designated ecologically sensitive zones must obtain an annual MCRAC.
- **Assurance Requirement:** The MCRAC must be issued by an independent professional CA/CPA) and must certify that the *Estimated Useful Life (EUL) and Written Down Value (WDV)* of the Plant, Property, and Equipment (PPE) are *not materially overstated*. This certification requires explicit verification of:
    - **Regulatory Status:** Full compliance with the Coastal Regulation Zone (CRZ) rules.
    - **Physical Risk:** Assessment of chronic (erosion, sea-level rise) and acute (storm surge) physical risks.
- **Accounting Implication:** Non-compliant assets must be treated as Impaired (Ind AS 36), thus forcing the balance sheet to reflect the true economic reality and protecting banks from unquantified collateral risk.

4.b. Maritime Environmental Liability Guarantee

- **Rationale:** To stop the systemic evasion of liability and the use of *Flags of Convenience (FoC)* by international shipping (e.g., *MSC Elsa 3* disaster), which subjects fisherfolk MSMEs to delayed, inadequate compensation and chronic food chain contamination.
- **Mandate:** Vessels operating under FoC or carrying hazardous cargo must deposit a *Non-Refundable Environmental Liability Bond* with the State before entering port limits.
- **Purpose:** This Bond is immediately callable by the State to fund cleanup, *ecosystem restoration,* and **prompt livelihood compensation** for affected coastal communities and MSMEs, bypassing lengthy international P&I litigation. This ensures the *Social (S)* pillar of ESG is protected.

4.c. State Environmental Veto Audit

- **Rationale:** To safeguard Kerala's environmental sovereignty and mitigate the risk of irreversible ecological damage from external policies, such as the *MoEFCC's administrative order* on mining especially rare minerals or the *Offshore Areas Mineral Amendment Act, 2023*.
- **Mandate:** Any Central directive for mining or high-impact infrastructure in coastal or ecologically sensitive zones is subject to a binding *State Environmental Veto Audit* and a mandatory public consultation process. The State reserves the right to deny incentives, power connections, and local clearances if the project's risk of escalating landslides (Idukki/Wayanad) or coastal erosion is deemed unacceptable to long-term sustainable development.

4.d. Contact & Support (MSME-Specific Contacts):

- **Official Website:** www.keralaindustry.org
- **Toll-Free Number:** 1800 890 1030
- **Local Assistance:** The General Manager of the respective District Industries Centre (DIC) is the key local contact for MSMEs.
- Kerala Financial Corporation **[KFC]** and
- Kerala State Industrial Development Corporation **[KSIDC]**

5. Focused Areas for the policies:

5.a. Procedure for Availing the Incentives for MSME:

I. Register on the Single Window Clearance Portal (KSWIFT) or the Startup Mission Portal.

II. Submit enterprise details, DPR, and financial statements.

III. For high-risk enterprises, obtain and submit the MCRAC (Section **4.a**).

IV. Obtain verification from the respective District Industries Centre.

V. KSIDC processes financial approvals.

VI. Incentive disbursement takes place after verification and approval through Government Orders (G.O.s).

VII. Maintain operational compliance and assurance certification for 3 – 5 years to retain benefits.

Industry Benefits and Risk-Adjusted Policy (Summary)

The Kerala policy framework shifts government incentives from simple subsidies to **Risk-Adjusted Grants**, mandating environmental and climate compliance (ESG) as a precondition for financial support. This approach mitigates "hard-to-abate risks" for both the State and the MSME, ensuring the sustainability of investment.

Sector	Policy Adjustment (Incentive Conditionality)	Risk Mitigation Focus
Construction & Infrastructure	Incentives (e.g., SGST deferral) are conditional on **MCRAC compliance**, validating asset collateral against CRZ violations.	Protects assets and investment value from **CRZ risk** (e.g., Demolition orders).
Oil & Gas	Incentives restricted primarily to **Green Hydrogen/Zero-emission projects**.	Mitigates **Stranded Asset Risk** and **Methane liability** associated with fossil fuels.
Mining & Mineral Processing	Subsidies strictly conditional on adherence to the **State Environmental Veto Audit**.	Addresses and counters the ecological impact of potential rare earth PPP mining (MOEFCC relaxations).
Agritech & Food Processing	Incentives tied to **Methane and Nitrous Oxide mitigation** (e.g., precision farming).	Safeguards exports from new global tariffs (like the EU's **CBAM**).
Marine & Fisheries Processing	Incentives linked to verifiable **carbon emission certifications** and protected by the Environmental Liability Bond.	Ensures global market access and accountability against major pollution events (like the **ELSA-3 capsizing**).

Export Promotion and Target Beneficiaries

Export measures are strategically aligned with global ESG standards. Financial support, including export turnover **reimbursements** and grants for participating in global expos, is prioritized for units with CBAM (Carbon Border Adjustment Mechanism) compliance certifications. New Export Infrastructure, including coastal economic zones, must incorporate climate-resilient design certified by the Department of Environment and Climate Change. The policy targets a broad group of entrepreneurs, specifically prioritizing Women Entrepreneurs, SC/ST/Minority, Differently-abled Entrepreneurs, and NRK investors across 22 Priority Sectors to foster inclusive growth.

6. MSME Climatic and other ESG Risks in Kerala

MSME Extrinsic Risks in Kerala

Kerala's MSME sector faces significant extrinsic governance risks that deter sophisticated investment despite the state's high human development. These barriers include:

- **Financial & Regulatory:** Banks impose stringent KYC/AML and Cyber Risk controls, largely due to the high global exposure of IT/ITES MSMEs and the unreliability of informal financial data.
- **Land & Infrastructure: Exorbitant land prices** act as the largest barrier to capital investment. This is severely compounded by Local Self-Government Corruption (LSGD) leading to CRZ enforcement failure (the "Maradu risk"), causing banks to **refuse coastal land as collateral**. Operational risks are worsened by major infrastructure failures (e.g., NH-64/66 collapses).

Global ESG Misalignment and Compliance Gaps

Global ESG reporting standards remain fragmented, creating mandatory compliance risks for Indian MSMEs:

- **Global vs. National Standards:** While major jurisdictions pursue mandatory IFRS S1/S2 adoption, India prioritizes the **Business Responsibility and Sustainability Report (BRSR)**. This misalignment necessitates complex reconciliation and prevents full alignment with investor-focused standards like SASB. The "Social" pillar of ESG (Human Capital/Rights) remains severely underdeveloped globally.
- **Scope 3 Compliance Duality:** Global supply chains see 75–95% of emissions in **Scope 3**. While the EU's Omnibus provisions excluded many MSMEs to ease compliance, India's BRSR mandates that the top 1,000 listed entities begin disclosing sustainability metrics for their material partners (cumulatively approx. 75% of the value chain) starting **FY 2025-26**. This duality amplifies the compliance and audit burden on Indian MSMEs, exposing export hubs to trade retaliation (e.g., **CBAM** tariffs).

Policy Correction: Mandatory Assurance (The MCRAC Solution)

To counteract these failures and de-risk investment, the Kerala policy must install independent safeguards:

- **MCRAC (CRZ Check):** The Mandatory Climate and CRZ Risk Assurance Certificate **(MCRAC)** forces an external, independent third-party opinion on asset legality, de-risking collateral, and correcting systemic corruption failures of the LSGD.
- **Liability Enforcement:** The **Environmental Liability Bond** guarantees prompt compensation for vulnerable communities (e.g., fisherfolk after spills), bypassing the slow national court system.
- **Land & Support:** The policy must commit to a **Dedicated Land Bank** and provide Tamil Nadu-style capital subsidies to overcome prohibitive land costs, alongside subsidies for cyber security to meet stringent RBI/bank requirements.

- **Independent Audit:** Implement the **State Environmental Veto Audit** (Section 4.c) to demand independent oversight on central infrastructure projects, protecting local environment and MSME logistics.

10. Conclusion:

Kerala's Industrial, MSME & Startup Policy (2025–2030) is transformed into a *Mandate for De-Risked Governance.* The policy formally recognizes the acute and chronic financial risks posed by systemic policy non-alignment: **Asset Stranding** (CRZ non-compliance), *Maritime Liability Evasion, and Erosion of State Environmental Sovereignty (*Offshore Mining).

By embedding mandatory financial assurance mechanisms—the *Mandatory Climate and CRZ Risk Assurance Certificate (MCRAC) and the Environmental Liability Bond*—the policy compels the financial ecosystem (MSMEs, Banks, Insurers) to internalize climate and governance liabilities. This framework sets a national standard for *Responsible Industrialisation*, protecting the State's social capital and the financial integrity of its MSMEs.

Professional Advisory: Navigating Policy and Risk for MSMEs in Kerala

Kerala presents an exceptional market opportunity for MSMEs, defined by its high Human Development Index (HDI), top-tier literacy rates, and substantial consumer spending power, significantly boosted by remittance inflows. This market offers a sophisticated base for technology, services, and high-quality goods. However, a responsible and sustainable business approach requires a clear-eyed recognition of the complex governance, fiscal, and environmental risks inherent to the state's political economy. Prospective ventures must prioritize meticulous due diligence over dependency on short-term incentives.

a. Investment Opportunities: Dominant High-Growth Sectors

While many sectors offer potential, MSMEs should capitalize on Kerala's established strengths, particularly in high-value, knowledge-based industries:

- **Healthcare:** Kerala boasts one of the best public and private healthcare infrastructures in India, with high patient awareness. The sector is attracting significant private equity investment (over $700 million in recent years) due to high demand for specialty care, low capital expenditure (CapEx) costs relative to other major South Indian cities, and a large, skilled nursing workforce. Opportunities exist in medical devices, health-tech, diagnostics, and specialized hospital services.
- **Information Technology (IT) and Tech Startups:** The state has fostered a strong startup ecosystem (over 6,900 startups) and is home to a growing number of IT professionals (estimated at 2.5 lakh in 2023). Focus areas include Deep Tech, AI-driven solutions, Fintech, and G-Governance, supported by the Kerala Startup Mission (**KSUM**).

b. Fiscal and Regulatory Environment: Navigating Federal Disputes

MSMEs must navigate the dynamic landscape of fiscal federalism in India. The state faces an ongoing financial strain, marked by internal deficits and disputes with the Union

Government over the timely release of mandated funds (often citing figures over ₹10,000 crore) in news reports and restrictions on state borrowing limits.

This conflict introduces two key risks, irrespective of political alignment:

- **Project Unpredictability:** Infrastructure or public service contracts reliant on large, Centrally Sponsored Schemes may face **delays or temporary freezes** due to policy non-compliance issues (e.g., adherence to scheme branding or implementation of the National Education Policy/PM SHRI).
- **Data Reliability:** Discrepancies persist between state (KSUM) and central (DPIIT) reporting methodologies for startup and MSME recognition. Ventures must independently verify market data and rely on objective, non-partisan sources.

c. Critical Ground-Level and Environmental Risk Factors

Projects near the coast or water bodies are exposed to specific, high-consequence risks where the common man and environment bear the brunt of legal and policy ambiguity:

- **Maritime Disaster Liability (ELSA-3 Incident):** The capsizing of the vessel MSC ELSA-3 off the Thottappally coast in 2025 serves as a crucial warning. This resulted in significant oil spills, plastic pellet contamination, and loss of livelihood for fishing communities. The legal battle highlights that while the Kerala High Court has robustly pursued compensation (initially demanding ₹9,531 crore for environmental and economic damage), the shipping company has invoked international maritime conventions to **limit its liability** to a fraction of the cost.
- **Caveat for Investors:** This incident underscores the weakness in global liability frameworks when powerful international operators evade full environmental responsibility, leaving local communities and the state to manage the long-term impact. MSMEs should assume liability risk is high when operating in coastal supply chains or port-adjacent services, particularly when availing bank credit facilities and insuring of assets.
- **Erosion of Coastal Buffer (CRZ Relaxation):** The 2024 approval of the relaxed CRZ Notification (reducing the No Development Zone to 50 meters in specific dense areas) is highly contentious. While politically driven to facilitate development, this policy is fundamentally at odds with Kerala's documented **climate risks** (floods, sea-level rise, and erosion). Ventures must integrate climate resilience and environmental ethics into their CapEx planning, as reliance on the relaxed rules exposes assets and operations to high natural hazard risk.
- **Mineral Mining Conflict:** Projects involving rare mineral mining remain politically and environmentally charged. MSMEs should approach any form of PPP in this sector with extreme caution, as such activities have historically led to environmental degradation, severe health issues for locals (e.g., in Kollam), and strong local resistance that can halt operations indefinitely.

Conclusion for Sustainable Enterprises

For MSMEs aiming to thrive with integrity, the path in Kerala requires a focus on ***sustainability and genuine community integration***. Do not rely solely on government incentives; instead, commit to:

a. **Meticulous Compliance:** Adhere strictly to the spirit and letter of CRZ, environmental, and labor laws, anticipating the possibility of future judicial reversals that may tighten current relaxations.

b. **Climate Proofing:** Integrate climate resilience into all planning, especially for projects near water bodies or the coastline, independent of the relaxed NDZ rules. Red flagging eco-sensitive zones like Idukki and Wayanad districts which are prone to landslides and flooding due to dams and rivers at spate, and farming in the fringes of forest areas, leading to animal-human encounters.

c. **Local Engagement:** Seek out business models that genuinely benefit and integrate vulnerable local communities (e.g., fisherfolk, marginalized groups) rather than displacing them.

d. **Global ESG compliance duality:** Indian MSMEs, operating in Kerala as Scope 3 value chain partners, must comply with national rules (BRSR, EPA 1986) as well as fragmented global mandates (GRI, SASB, CSDP, GHG Protocol) required by MNC clients. Global standards like IFRS S1 and S2 (including TCFD**)** should be considered for futureproofing. While the EU relaxed provisions for some small partners, India's BRSR mandates that the top 1,000 listed entities disclose approx. 75% of their value chain's data starting **FY 2025-26**. This duality amplifies the MSME compliance burden and exposes export hubs to trade retaliation **(CBAM)** due to non-alignment.

By navigating these complex ground realities with transparency and ethical rigor, MSMEs can build a strong, sustainable foundation in one of India's most economically advanced but environmentally sensitive regions. Invest Kerala [https://invest.kerala.gov.in/kerala-unveiled/kerala-insights/esg/] for further information.

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