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FISME's Proposals for consideration for Union Budget 2018 – 19

Federation of Indian Micro and Small & Medium Enterprises (FISME)- a national body of MSMEs comprising of over 740 associations, hereby submits its memorandum of proposals for the consideration of Union Budget 2018-19. The Memorandum comprising of the following five parts:

1. Direct Taxes
2. Indirect Taxes
3. Issues concerning Banking and Finance
4. Other important issues

1. Direct Taxes

i. Investment allowance on Capex

Section 80-I, investment allowance on capex was earlier allowed without any lower threshold. As tax benefit will accrue to the claimants only after each claim undergoes the scrutiny of the assessing officers, there should be no problem in administering the facility even in case of smaller capex. There is an urgent need to introduce tax breaks to promote employment generation on the same lines as depreciation encourages capital investment.

Suggestions:

Section 80-I, investment allowance on capex should be without any lower threshold.

ii. **Incentive for employment**

There can be no doubt that for a country teeming with Human Resources (looking for gainful employment), it is the bounden duty of the Government to encourage enterprises that encourage more employment for the same capital. Capital intensive large manufacturing Companies are able to claim large tax wite-offs due to depreciation provisions. MSMEs being employment intensive but not capital intensive, cannot derive such benefits and at the end left with little surplus after paying hefty taxes.

Suggestion:

To encourage Increase in internal accruals in MSMEs, which will further enhance their employment capacity through expansion etc. they should be allowed deemed depreciation on the basis of the employment created in a particular F.Y. Taking that the large sector provide employment to one worker per 1 crore investment on capital, the number of new workers employed in a year should be capitalised as deemed capital investment and should be made eligible for tax exemption.

iii. **Income Tax on Companies**

Less than 3% of MSMEs are body corporates under Companies Act. Almost the entire MSME sector is composed of Proprietorship and Partnership firms. One of the major reasons of this peculiar phenomenon is absence of Income Tax slabs at lower rates for lower income Companies as is the case for individuals.

Suggestion:

Income / Corporate Tax for enterprises operating in the much desired (by the government) company format may be levied in slabs as available to individual tax payers.

3. Indirect Tax

i. Leveraging GSTN to curb theft of Excise/ VAT in supplies made to public service providers/ utilities

GSTN is the key to success of GST- the ambitious tax reform in works for last 10 years. The reason is apparent. GSTN has the infrastructure and the capacity to accept millions of transaction of sales and purchases. The self-check is built into the system in all transactions taking place between two traders because tax paid on a purchase is valuable money for the buyer who uses it to meet his liability of tax on his sale of the goods/services – whether in as it is condition or new in which the purchased goods/services were used. This unbroken chain is what makes the system work and provides it the integrity.

In case the goods or services reach the ultimate/end consumer who has no use of the tax paid on its purchase, the string of transactions with respect to goods/service comes to a logical end. There is however a peculiar situation where the buyer of goods/services may be in business of selling or providing free some goods/services, using the purchased inputs on which he is not required to charge GST. In all such cases the chain of transactions comes to an abrupt end leaving a wide gaping hole in the whole scheme of GST.

The share of this business in the overall economy is quite significant if we recognize that all power cos. – Generators, Transcos & Discoms, other utilities like municipalities, local bodies, water works & almost all government departments like PWD, irrigation, police department, education, defence etc. fall into this category. As a result, huge quantum of purchases they make and the GST they pay has the possibility of going untraced and out of the monitoring system. Unscrupulous elements have ample opportunity to siphon off government revenues as they are reported to be doing in the present system.

Suggestion:

Our suggestion is that in all such cases where the goods, services or public goods are concerned, it should be mandatory for above buyers to enter their purchase transactions in GSTN irrespective of the fact that they have no use of GST paid by them/claiming refund, while making purchases. Ideally, in maximum number of such cases and wherever possible- for example in case of power companies, GST may be made applicable on electricity so that a self-checking chain is built by itself.

ii. 'Un-make in India' : Protective Measures for large manufacturers like Safeguard duties and Minimum Import Price (MIP) make MSMEs uncompetitive

Commodity prices in India are governed by global trends in prices. The domestic producers have the protection through import tariffs, falling exchange rates and logistics advantages. For the last one year Government is imposing different protective measures like Anti- Dumping Duty, Safeguard Duty on import of base metals e.g. Steel to protect the market of domestic manufacturers' from 'cheap' imports. While the intention of the Government may be to support the domestic industry to be viable, these measures are causing enormous damage to the user industries viz., engineering sector, by making their products uncompetitive in both domestic and export market due to high cost of the basic metals. EEPC has also raised these issues repeatedly to the Government without much avail. On the other hand more and more steel products are being brought to the purview of such protectionist measures.

The tariffs were raised by 50% in the last budget. It did not satiate the producers' greed so Minimum Import Price (MIP) was brought in the picture - something inherently absurd ! Once an innovation like MIP is accepted in one item the others cannot be left behind. So aluminium industry is now demanding further duty protection + MIP It is said the production cost for aluminium metal is around $1300; the bench mark LME is trading at $ 1770+75 but the producers are unhappy and the government is keen to meet their demand on a quid pro quo basis.

What is shocking is the adversely affected user industry is being advised not to plead its case before the quasi-judicial forum (meant to hear petitions of aluminium producers for slapping safe guard duties) to avoid unnecessary delays in slapping the duty!

If imposed, these measures will cause irreparable damage to the domestic, down the line, manufacturers. This will also seriously affect the export performance of the MSME sector who export nearly half of the commodity export from India. Needless to mention, such a situation will further aggravate the drop in exports. The fact is the ultimate sufferer is the government, the user of downstream electrical products for T&D infrastructure.

Suggestions:

For the sake of the growth and competitiveness of the value adding, down the line industries, protective measures for all basic metals and chemicals should be taken judiciously, keeping in view their effects on the entire value chain. In any case Safeguard Duties should be immediately done away with from Steel imports. And Government should constitute a consultative machinery including the MSME sector, to capture the concerns of all stakeholders before imposing such protective measures.

iii. 'Make in India': Leveraging customs duties in right way

Every country that has industrialized used differential rates of duties to encourage domestic value addition. Instead of having just two slabs, the duties could be intelligently tweaked within the framework of multi-lateral and regional commitments to create a pull for "Make in India" and encourage manufacture of value added products

Suggestion:

Rates of Custom Duties on various stages of production - from raw material to finished products may be finely differentiated allowing small breathing space to each of the value adder. A study could be commissioned to identify potential sectors and slabs to encourage such. value addition activities.

4. Issues concerning Banking and Finance

i. Functionalising Trade Receivables e-Discounting System (TReDS) for Micro, Small and Medium Enterprises –

a) Deemed Acceptance of Trade Receivables:

TReDS has the potential to be a very powerful tool not only for providing liquidity to MSME at reasonable cost but also at bringing financial discipline among the corporate. But the platform can be purposeful only if legislative backing is extended to it particularly through a provision for Deemed Acceptance of Trade Receivables. In the current business practice, there is no question of a corporate accepting a supply invoice of an MSME. In fact some NBFCs are agreeable to accommodate a seller against a NOA from the corporate in favor of the NBFC to the effect that payment of the invoice will be made to the NBFC at the seller's request. The reasons for refusal to issue a simple NOA or a confirmation that an amount is due on a certain date are the asymmetry in power of the MSME supplier and the Corporate buyer.

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Besides the buyers are in an unassailable position to refuse to deal with the small supplier or place next order.

Suggestion:

To make TReDS purposeful, it is necessary that the invoices are uploaded mandatorily and status of deemed acceptance is granted after 45 days of non - payment to convert them into negotiable financial instruments. This will not only provide much needed liquidity to MSMEs but will also discipline in corporate and PSUs which is equally important for the country's financial usher in financial system.

b) Developing Market makers in the TReDS platform:

For successful operation of the TReDS there should be enough Bill Discounting entities of the platform. Today only a few Banks are operating as discounting agencies and this is affecting market based valuation of the Bills offered. Also there is every chance of monopolising the market by a few players, who earn a super profit by offering very high discount rates for the MSME Bills.

Suggestion:

For a healthy growth of the TReDS platform, availability of more market makers is essential. And to induce more discounting agencies on the platform Government should provide financial support may be re- discounting facilities at repo rate or similar instruments. This will help to get the discounted Bills a fair price in the market.

ii. Revitalizing Trade credit channels by strengthening Sec-138 of the NI Act; making cheques as good as cash

World over Trade Credit (TC) has been more important than Bank Credit (BC). India with history of several millennia has been well versed in flow of credit between traders based on trust - societal modes and peer pressures. It is easy to understood that TC increases velocity of money transmission in the market manifold. It is for such reasons that TC has been considered by some as life blood of the economy. Even though BC has percolated enormously in the last few decades, there are limitations to it as very large no. of small traders and self-employed find it difficult to establish their eligibility as per banking norms. The proliferation of TC in such a situation can help even BC reach those who cannot obtain it directly.

TC unfortunately has been seen to be shrinking and going down as a proportion of trade. The reasons cited are lack of mutual trust among businesses and easing of peer pressure on defaulters in society. We believe in FISME that a habit of financial discipline can be induced by a simple Act which has become almost junk for all practical purposes by strengthening Sec-138 of the Negotiable Instrument Act.

Once trade starts treating it as enough security to extend credit (against a cheque) the volume of business will go up substantially. The biggest beneficiaries of this step will be small businesses - who do not have the wherewithal to arrange LC to avail credit – may be able to obtain the facility on the strength of their cheque. This simple step can have few reaching consequences as it will grease the wheels of trade effectively. In course of time it will also inculcate financial discipline amongst the concerned which in itself will be a very desirable fall out.

Suggestion:

The Sec 138 which is vitalized to an extent that a cheque becomes a negotiable financial instrument, payment of which can be enforced without going to a court. It could be done through RBI/IBA route by instructing banks to freeze the amount equivalent to the sum of cheque bounced in the account of the issuer of the cheque whenever such amount is available.

It would also give a huge fillip to the current initiative of the Government making businesses move from cash based transactions to using banks for commercial transactions.

iii. Project funding for the MSME manufacturing sector

MSME finance is treated by the banks and often by the Government as a homogenous issue. However, within the sector the challenges in finance for the MSME manufacturing sector are way different from other sub sectors like services or trade. There is general reluctance among bankers for financing manufacturing units, particularly term loan, because they find manufacturing processes more risky in comparison to consumer finance say of Car or Housing. So, it is not astonishing that the credit flow to the manufacturing MSMEs are stagnating for last four quarters.

***Suggestion*:**

For success of make in India, MSME manufacturing sector Government should encourage Banks and RBI to provide term loan, beyond the normal prudential norm and for this purpose special re-finance window should be opened for Banks.

5. Other important issues

i. 'Unease of Doing Business': forcing the compliance requirements of Listed Companies on privately held companies including medium enterprises

Ease of Doing Business is one of the focal initiatives of the present Government and towards this end Government is doing is best to simplify procedures. However, the Ministry of Corporate Affairs introduced a plethora of regulatory filings under the Companies Act, 2013 which make 'Doing Business' difficult for MSMEs. Requirements like compulsory cost audits on all Companies, may be essential to take care of monopolistic pricing by power discoms and other private monopolies, but imposing them on privately held enterprises will only add further burden of compliance costs.

Suggestion:

a. Cost accounting and Cost Audit is already applicable on all Utilities/ natural monopolies like Discoms, Airports, Railways etc. but needs to be enforced

b. Private companies competing in open economy should be excluded from compulsory Cost Audit

ii. **Towards 'Making in India': availability of affordable workplace for MSMEs**

Make in India is a timely initiative by the Government to boost the stagnant manufacturing sector. For manufacturing industry need workplace which is in real short supply today besides being formidably costly. If Government is really motivated towards upscaling manufacturing in India, it has to develop a work plan to make industrial sheds and modular factories available at affordable price. While the large sector can extract big plot of lands from the State Governments at zero or minimal costs, the MSMEs need to make market prices, which make the project unviable from the day one.

Suggestion:

Government provides funding support to state governments under various schemes of different ministries for upscaling infrastructure. There should be caveats under such schemes to utilise a reasonable share of the grant to develop affordable work-sheds and modular / flatted factories for MSMEs. Government also should consider utilising idle land banks of Defence Railways etc. to develop Industrial estates and modular factories on PPP mode.

iii. Minimising burden for conformity to labour laws for MSMEs - Bunching all employers' contributions for future security of a worker to 10% of wage

In his Budget speech (2015-2016),Finance Minister himself remarked that both EPF and ESI have hostages, rather than clients. The Finance Minister also talked about alternate schemes to the above.

However, even today, much has not changed at the ground level. While the Government is seized to the fact that a large number of people employed in the informal sector are not covered by social security net, the bureaucracy possibly overlook the sheer unviability of the existing EPF and ESI framework for MSMEs. A pragmatic labour policy will encourage more enterprises in the unorganised sector to declare their actual number of workers and also provide them social security. The potent barriers in the way, namely, the high cost of compliance and low quality of benefits, drive away both the employers from adopting the schemes and in turn forces the MSMEs to employ less people in the formal sector.

Suggestion:

FISME has written to the Prime Minister's Office to bunch all employers' contributions for future security of a worker to 10% of his wage and subsume EPF, ESI etc. FISME has also asked for a single return to be filed by the MSMEs against all social security Acts. While the demand may look to be a tall order, according to experts on the subject, the spin offs are huge. Firstly it will encourage the 4 crore plus enterprises in the unorganised sector, who so far largely remained 'invisible' to the *authorities*, to come under the legal regime, thus paying taxes and other contributions. The more important spin off, from welfare angle, will be access to social security measures like pension by the workers of these enterprises who may count to be nearly 10% of the India's population.

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