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Impact of GST on Micro, Small and Medium Enterprises (MSMEs)

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ABSTRACT

Goods and Services Tax (GST) is an indirect tax which was introduced in India on 1 July 2017 and was applicable throughout India which replaced multiple cascading taxes levied by the central and state governments. It's true that GST means 'Great Step towards Transformation', 'Great Step towards Transparency' in India and it is also true that someone gives 'birth' while someone else 'nurtures it'. It has been long pending problem to streamline all the specific types of oblique taxes and put into effect a "single taxation" system. Because the name indicates, the GST could be levied each on items and offerings. GST is a tax that needs to pay on supply of products & offerings. Any person, who is presenting or offering goods and services, is liable to fee GST. Now we are witnessing, how this tax reform reshapes our economy and business dynamics for Micro, Small and Medium Enterprises. Flourishing amidst a challenging environment, the Small and Medium Enterprises *(*SMEs) of India experienced several highs and lows in the past few years. With the Indian economy expected to emerge as one of the leading economies in the world and likely to become a $5 trillion economy by 2025, major impetus is being given to strengthen the back bone of our economy-the SME sector. This paper highlights to know the GST and MSMEs and Impact of GST and MSMEs.

Key words-- GST, MSMEs and GSTN

I. INTRODUCTION

Goods and Services Tax (GST) is an indirect tax which was introduced in India on 1 July 2017 and was applicable throughout India which replaced multiple cascading taxes levied by the central and state governments. It was introduced as The Constitution (One Hundred and First Amendment) Act 2017, following the passage of Constitution 122nd Amendment Act Bill. The GST is governed by a GST Council and its Chairman is the Finance Minister of India. Under GST, goods and services are taxed at the following rates, 0%, 5%, 12% ,18% and 28%. There is a special rate of 0.25% on rough precious and semi-precious stones and 3% on gold. In addition a cess of 22% or other rates on top of 28% GST applies on few items like aerated drinks, luxury cars and tobacco products.GST replaced a slew of indirect taxes with a unified tax and is therefore set to dramatically reshape the country's 2 trillion dollar economy.

The single GST(goods and service taxes) replaced several former taxes and levies which included: central excise duty, services tax, additional customs duty, surcharges, state-level value added tax and Octroi. Other levies which were applicable on inter-state transportation of goods have also been done away with in GST regime.GST is levied on all transactions such as sale, transfer, purchase, barter, lease, or import of goods and/or services. India adopted a dual GST model, meaning that taxation is administered by both the Union and State Governments. Transactions made within a single state are levied with Central GST (CGST) by the Central Government and State GST (SGST) by the State governments. For inter-state transactions and imported goods or services, an Integrated GST (IGST) is levied by the Central Government. GST is a consumption-based tax/destination-based tax, therefore, taxes are paid to the state where the goods or services are consumed not the state in which they were produced. IGST complicates tax collection for State Governments by disabling them from collecting the tax owed to them directly from the Central Government. Under the previous system, a state would only have to deal with a single government in order to collect tax revenue.

As per the government website on GST, "Goods and Services Tax" Network (GSTN) is a nonprofit organization proposed to be formed for creating a website / platform for all the concerned parties related to the GST, namely stakeholders, government and taxpayers to collaborate on a single portal. When up and running, the portal is supposed to be accessible to the central government which allows it to track down every transaction on its end while taxpayers are advertised to have the ability of connecting this to their tax returns. However its efficacy and efficiency is yet to be tested. The known authorized capital of GSTN is 10 crore (US$1.6 million) in which Central Government holds 24.5 percent of shares while the state government holds 24.5 percent and rest with private banking firms for smooth running of the transactions.

II. MICRO, SMALL AND MEDIUM ENTERPRISES DEVELOPMENT

(MSMED) Act 2006

The Micro, Small and Medium Enterprises Development (MSMED) Act was notified in 2006 to address policy issues affecting MSMEs as well as the coverage and investment ceiling of the sector. The Act seeks to facilitate the development of these enterprises as also enhance their competitiveness. It provides the first-ever legal framework for recognition of the concept of “enterprise” which comprises both manufacturing and service entities.

It defines medium enterprises for the first time and seeks to integrate the three tiers of these enterprises, namely, micro, small and medium. The Act also provides for a statutory consultative mechanism at the national level with balanced representation of all sections of stakeholders, particularly the three classes of enterprises and with a wide range of advisory functions. Establishment of specific funds for the promotion, development and enhancing competitiveness of these enterprises, notification of schemes/programs for this purpose, progressive credit policies and practices, preference in Government procurements to products and services of the micro and small enterprises, more effective mechanisms for mitigating the problems of delayed payments to micro and small enterprises and assurance of a scheme for easing the closure of business by these enterprises, are some of the other features of the Act.

Objectives

1. **To Know the GST and MSMEs**
2. **To Study the Impact of GST on MSMEs**

III. RESEARCH METHODOLOGY

The present study is depending on secondary data. The secondary data was collected from Government of India Ministry of Micro, small and Medium Enterprises and also search edited books and websites.

IV. GST AND MSMEs

The increasing formalization of the Indian economy, especially through digitization, is an inexorable advance that will upend the business model based on the twin arbitrage of labor and cash transactions of micro, small and medium enterprises (MSMEs).India’s paradigm shift to the Goods and Services Tax (GST) regime in July will increase their compliance costs and snare a majority of them into the indirect tax net for the first time.

Sharp practices

So far, unorganised MSMEs have grown faster than organised peers because of lower cost structures stemming from tax avoidance, and not having to pay social security benefits to employees (such as provident fund and gratuity), and excise duty (if turnover is less than Rs.1.5 crore).Some MSMEs also understate employee base or set up multiple ventures to avoid breaching tax thresholds. Such sharp practices helped them price products and services competitively over the past few decades and also maintain operating margins at organised player levels.

The vicissitudes resulting from the impact of GST are many. To wit, for manufacturers, the reduction in the threshold for GST exemption to 20 lakh from 1.5 crore means tens of thousands of unorganised MSMEs will soon be cast into the tax net. And digital transaction trails created by dual authentication of invoices under GST will strengthen tax compliance. Additionally, a lower tax burden under GST will reduce the cost of raw materials and logistics.

Different for services

For the services sector, though, the tax burden will increase. Hence, organised players with the ability to hold their price-lines, or pass on any increase in cost to customers, will be able to maintain or improve profit margins. We believe a simplified tax structure and a unified market will improve operational efficiencies, especially of MSMEs with a wider reach. Then again, there was demonetisation. Last fiscal, MSMEs were expected to record on-year top line growth of 14 to 16 per cent.

However, the impact of demonetisation has been severe in the second half and they would have closed the year with an increase of just 6 to 8 per cent. But as the effects of demonetisation fade, growth will pick up in the current fiscal.

A peep into outlook: Positive for light engineering: Light engineering MSMEs rated by Crisil saw 15 per cent compound annual growth rate in topline between fiscals 2014 and 2016, with demonetisation causing just a blip.GST is expected to provide a boost to this segment because of lower tax incidence. The Government’s thrust on ‘Make in India’ will also lead to continued investments, helping the sector maintain growth momentum.

Positive for electrical equipment: Sales in companies rated by Crisil grew way faster at about 23 per cent in fiscal 2016 compared with 16 per cent in 2015. The sector will benefit from lower freight costs and tax rates. Though growth is expected to be strong this fiscal, cheaper imports, especially from China, remain a challenge.

Neutral for pharmaceuticals: Sales in companies rated by Crisil grew 11 per cent in fiscal 2016 compared with 15 per cent in 2015.Demonetisation had a limited impact as the Government had allowed extended use of the banned Rs.500 and Rs.1, 000 currency notes for purchasing medicines. We do not foresee any significant difference in tax rates under GST. This fiscal, too, we expect similar growth.

Neutral for auto components: Between fiscals 2014 and 2016, sales by unorganised auto component makers rated by Crisil grew at 14 per cent annually compared with 7 per cent for their organised peers. However, demonetisation led to a short-term drop in sales to original equipment manufacturers (OEMs), or vehicle makers. This fiscal, OEM sales are expected to normalise. Organised players will benefit and record moderate growth given the thrust on digitisation and lower tax rates under GST. Unorganised players catering mostly to the non-OEM replacement market will be forced to move into the organised domain.

Marginally negative for textiles: Sales growth in the textiles-related MSME segment had already declined from 15 per cent in fiscal 2015 to 8 per cent in 2016.GST will have a marginally negative impact because of higher tax rates expected. During Crisis's interactions with clients, some of them raised concerns that a unified market would create more competition in an already crowded and price-sensitive arena with a large number of unorganised players. Organised players dealing in branded apparel are expected to fare well, though. The sector is expected to record below-par growth of 5 per cent or lower.

Marginally negative for leather and footwear sectors: Companies Crisil rates in this segment have seen muted growth and have borne the brunt of demonetisation. With competition, including from Chinese players being strong, the operating margin has fallen to as low as 6 per cent for organised players.We do not expect GST rates to vary much from the current indirect tax rates. Crisil expects overall growth and margins of players to remain subdued this fiscal.

The present ceilings on investment for enterprises to be classified as micro, small and medium enterprises are as follows:

Classification	Manufacturing Enterprises*. (Investment limit in Plant & Machinery)	Service Enterprises** (Investment limit in equipment)
Micro	Rs. 2.5 million / Rs. 25 lakh	Rs. 1 million / Rs. 10 lakh
Small	Rs.50 million / Rs. 5 crore	Rs. 20 million / Rs 2 crore
Medium	Rs 100 million / Rs 10 crore	Rs. 50 million / Rs 5 crore

Monthly and financial performance of development commission, MSME

Under various Promotional and development activities taken up as part of plan schemes, the number of MSMEs reported to be benefitted during the month of November 2017 was 4,985 as compared to 3,139 during the same period of last year. 20,114 persons were trained in November,2017 as compared to 9,351 persons in November, 2016.Thenumbers of cases of credit proposals approved are 15,920 during Nov.'17 as against 25,971during the month of November, 2016. The detail of MSMEs and other beneficiaries under the various schemes is noted in statement below:

No. of MSMEs and Other Beneficiaries under various schemes

SI. No.	Name of Scheme	Performance			
		Nov.'17	Upto Nov.'17	Nov.'16	Upto Nov.'16
1	**Design Clinics Scheme for MSME Sector**				
	No. of MSME benefited	9	331	240	240
2	**Credit Linked Capital Subsidy Scheme**				
	No. of MSME benefited	0	4,027	0	3,391
3	**Technology Upgradation and Quality Certification Support to MSMEs**				
	No. of MSME benefited	0	0	9	122
4	**Intellectual Property Right (IPR) No. of Participants Benefied**				
	No. of Participants Benefied	232	1,262	80	1,322

5	**MDA Scheme Bar Code**				
	No. of Units Benefited	36	490	97	539
6	**Credit Guarantee Scheme**				
	No. of credit proposals approved	15,920	1,78,044	25,971	3,40,472
7	**Export Promotion**				
	No. of Participants Benefited	61	315	698	1437
8	**Vendor Development Programme for Ancillarisation**				
	No. of Units Participated	1,717	6,440	0	5,305
9	**MDP/EDP/Skill Development**				
	No. of Trainee Benefited	10,330	39,240	2,166	27,699
10	**Tool Rooms & Tech. Institutions**				
i	No. of Trainee	9,491	93,549	6,407	1,07,324
ii	No. of Unit Assisted	3,223	21,212	2,209	21,779
11	**MSME TCs/MSMETSs***				
i	No. of Tests Performed		1,26,630	20,687	1,24,903
ii	No. of MSME benefited		1,170	584	1,960
A.	Total (MSMEsBenefitted) (1+2+3+5+8+10(ii)+11(ii))	4,985	33.67	3,139	33,336
B.	Total (Persons Benefitted) (4+7+9+10(i)	20,114	1,34,366	9,351	1,37,782
C.	Total (Tests Performed) (11(i))		1,26,630	20,687	1,24,903

Souces: www.dcmsme.gov.in

V. IMPACT OF GST ON MSME

At present, the total tax collection in India is around 14.5 Lakh Crore, of which 34% is indirect tax. Indirect taxes include service tax, stump duty, customs duty, VAT, etc. It refers to the collection of tax indirectly by the Government of India. In most of the developing countries, the share of indirect tax is higher than the direct tax. However, in the developed countries the share of indirect tax is much lower. Therefore, the new GST implementation will allow the government to have a better grip on the taxpayers. This should be capable of evolving the entire tax system.

Small and Medium Enterprises (SMEs) have been considered as the primary growth driver of the Indian economy for decades. It is further evident from the fact that today we have around 3 million SMEs in India contributing almost 50% of the industrial output and 42% of India's total export. For a developing country like India and its demographic diversity, SMEs have emerged as the leading employment-generating sector and has provided balanced development across sectors. Let's examine what would be the impact of GST on Small & Medium Enterprises.

All the compliance procedures under GST — Registration, Payments, Refunds and Returns will now be carried out through online portals only and thus SMEs need not worry about interacting with department officers for carrying out these compliances, which are considered as a headache in the current tax regime.

Below we have provided a high level impact analysis of GST on small and medium businesses in India.

Compliance Procedure	Positives	Negatives
Registration	Online registration will ensure timely receipt of certificate of registration and minimal bureaucracy interface	Not all the SMEs have technical expertise to deal with online systems, thus most of them will need intermediaries to obtain registration for them. This will add to their registration cost.
Payment	Electronic compliance will bring transparency and will also reduce the compliance cost.	Since funds are required to be maintained in the form of electronic credit ledger with the tax department, it may result in liquidity crunch.
Refund	Electronic refund procedures will fast track the process and enhance liquidity for SMEs	Refunds can be claimed only after filing of relevant returns. Also it depends on the compliances done by the supplier and his rating.
Returns	All returns are required to be filed electronically and input tax credit and tax liability adjustment will happen automatically on the basis of these returns	Minimum of thirty-seven returns are required to be filed by every registered taxpayer during a financial year. Thus SMEs will have to deploy additional resources and eventual cost of compliance will increase

Direct impact of GST on small and medium enterprises

GST will help and ease the process of starting a business in India. Earlier, every business in India was required to obtain VAT registration, which differs in every state, and the rules and regulations are different. Thus it was a very confusing procedure. However, under GST, the businesses have to only register for GST which will have a centralized process, similar to service tax.

Currently, for any business, it is mandatory to make a VAT payment if the annual turnover is more than 5 lakh in few states and 10 lakhs in few other states. This difference in various states creates confusion. Under GST a business does not have to register or collect GST if the annual turnover is 10 lakh. This is applicable to every state. This will allow many small businesses which have a turnover between 5 lakh – 10 lakh to avoid applying for the GST return.

GST allows small and medium business to do business with ease in India, due to the less complexity. The distinction between the services and goods will be gone, and this will make compliance easier.

VI. CONCLUSION

Several policy interventions along with technology and innovation will continue to play vital role in creating a business-friendly atmosphere for the SMEs. No doubt that GST is aimed to increase the taxpayer base, majorly SMEs into its scope and will put a burden of compliance and associated costs to them. But in the long run, GST will turn these SMEs more competitive with a level playing field between large enterprises and them. In fact, recently government has also formed a special committee to look after the issues faced by MSME sector in GST. It is urged to the industry that they proactively highlight the above issues and obtain the relief prior to advent of GST as once GST is implemented; the chances of respite would be very minimal for the sector. Furthermore, these Indian SMEs would be able to compete with foreign competition coming from cheap cost centers such as China, Philippines and Bangladesh.

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