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FISME's Memorandum for Budget 2019-20
Concerns and Suggestions

Context

The MSME sector by and large has been undergoing a prolonged period of stress. The reasons can be attributed to two main factors.

Firstly, stress is because of **contraction in their staple markets** due to stress in agriculture sector, corporate sector (IBC resolution process of over 1500 large corporates) and reduced investment in infrastructure sector.

Secondly, a crisis like situation is experienced by MSMEs because of **reduced liquidity** arising from corporate stress and NBFC led squeeze in money markets.

To address some of these constraints FISME proposes a set of interventions that could be done through Budget:

1. **A transformative idea to de-clog Trade credit markets benefitting MSMEs**

   Like other transformative ideas of NDA-II, IT has been at heart of one major initiative of TReDS- an online mechanism for facilitating the financing of trade receivables of MSMEs through multiple financiers.

   There is similar but even a bigger opportunity to positively impact working capital needs of MSMEs by de-clogging massive trade credit markets leveraging IT and GST.

   Trade credit is one of the most important forms of financing. It is greater in volume than short-term bank credit in nearly all developing and industrialised countries. However, in India trade credit has steadily declining due to host of reasons the most prominent being the loss of trust on negotiable instruments especially cheques. The informal trade credit has also been hit due to series of disruptions off late. The net result is that MSMEs- majority being in informal segment, are facing acute shortage of funds. Not only has the shortage arrested expansion of economic activities as a normal course in a growing economy but forced businesses to scale down, leading to pressure on even existing employment.

Suggestion:

i. We propose that Government to create a multi-stake holder Agency on the lines of Credit Bureau (under Govt. control). The Agency may be provided access to big data of GST, bank transactions and ROC filings based on which it would automatically create credibility report of companies. The Agency will allow access to these reports to those who are willing to subscribe and on reciprocal basis ready to share the data– similar to CIBIL. It may create a scoring model based on the data analysis. (Details of fee and terms could be thrashed later).

ii. Advantages:
   - Data analysis of delays in payments through the setup could work as an early warning system for potential defaulters and likely NPAs which could be extremely useful for Banks also.
   - This will have a salutary impact on instilling payment discipline as well.
   - It is a market based mechanism to address the delayed payment problems experienced by MSMEs.
   - No new legislation is needed and it could be started with executive orders.

It can be a really transformative initiative.

iii. TReDS- let all listed companies be on it:

TReDS is proving a successful initiative. Three TReDS platforms: M1xchange, RXIL, and A.TReDS, are already in operation. In November 2018, Prime Minister Narendra Modi announced that companies whose turnover exceeds Rs 500 crore will have to be registered on TReDS in order to smoothen cash flows for MSMEs. TReDS platforms have recorded explosive growth: from Rs. 800 crore in (2017-18), the business of all three exchanges put together touched approximately about Rs. 7,000 crore (31st March 19). It is expected to touch Rs. 30,000 crore in FY 2019-20.

To make it more effective and broad-based, all listed companies may be asked to upload their bills.

2. Direct Taxes:

a. 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 investment in capital goods on the same lines as depreciation and thereby generate employment. The current dispensation excludes most MSMEs from taking advantage of investment allowance.

Suggestion:
Under Section 80-I, investment allowance on capex should be given without any lower threshold; even at a higher rate/ MSMEs not excluded.

b. Capital gain tax on sale of industrial assets

For expansion, many a times there is a need to sell the existing industrial/ commercial property to buy another one. Although individuals are exempt from paying the Capital Gains Tax if the another dwelling is bought within a specified time, no such provisions are available for industrial/commercial properties. It makes access to land more expansive and contributes to un-competitiveness of Indian industry.

Suggestion:

To encourage expansion and enhanced economic activity, the exemption from Capital gain tax could be extended to industrial/ commercial properties also.

3. Indirect taxes: GST

a. IGST refund for exporters

Exporters secure business in tough competition. Timely refund of Tax paid and consumed in export goods is critical to be competitive and to survive for an exporting enterprise. During the initial phase of implementation GST, when neither exporters nor the officials were fully aware how the system would function, there have been many errors of commission and omission committed from both sides. Such cases include pending refund of IGST paid on goods exported during the transitional period (i.e. 01.07.2017-30.09.2017) in cases where higher rate of Duty Drawback was claimed under column A. And cases where Duty Drawback rates were identical in Column A and Column B, but drawback was claimed under Column A instead of B.

Suggestion:
One time opportunity could be given to all exporters who have a grievance with regards to refund of IGST. Exporters must be allowed to revise their returns/ choices and their refunds processed accordingly.

b. **GST on electricity** (Utilities purchase GST paid goods. With no GST on electricity, loop is not completed. Result: evasion and unscrupulous suppliers)

Most States impose electricity duty on electricity in percentage terms and the rest at fixed amount/unit. If the utilities are covered under GST and start charging GST on electricity supply (duty subsumed in GST), the GST paid by them on their purchases will become a source of revenue as it could be used as ITC and set off against their own liability of depositing GST on electricity sold enlarging the scope of GST in the process – a progressive step in the chain. It is often learnt that certain recalcitrant suppliers to power utilities do not deposit the GST amount collected from the utilities on sale of their goods/services. Chances of this evasion are strong because Utility buyers have no use for GST paid on its purchases. There is as such no occasion to reconcile GST accounts at the sellers and buyers level. Naturally once the circle is completed, such leakage will also get plugged. Funds starved Utilities will also be able to save large sums on their purchases of equipment etc.

Suggestion: levy GST on Electricity forthwith.

4. **Securing dues of MSMEs during Corporate Insolvency Resolution Process**

The Insolvency and Bankruptcy Code 2016 is giant step in redeploying stressed assets in economy. But during Corporate Insolvency Resolution Process

(CIRP)/Liquidation procedure MSME suppliers are categorized as "Operational Creditors" which all but leaves them out of participation in the entire process under IBC. There is no statutory protection of their payments under the resolution plan and / or liquidation which is guaranteed to the MSME under MSMED Act. The unfortunate fall out of this anomaly is that corporate NPAs will in turn lead to generation of plethora of MSME NPAs.

Suggestion:
The Ministry of Corporate Affairs in consultation with Ministry of Law and Justice should pass appropriate clarifications / changes to ensure the creation of a separate sub-category of MSME within the Operational Creditors and accord the MSMEs with special rights of recovering full payments due against the companies facing CIRP or Liquidation under MSMED Act. MSME be given the status of Financial Creditors under Insolvency & Bankruptcy Code, 2016 and accorded special rights of recovering full payments due against the companies facing CIRP or Liquidation under MSMED Act

5. **Land reforms**

Inability to access land has become the biggest bottleneck for industries. Without improving access to affordable industrial land there is little hope for new industries to come up. Today setting up an MSME after purchasing land and building has become unviable at in most cities. The following steps could bring effectively down the cost of land for industries:

Suggestions:
- i. Allow Stamp duty paid to be treated as ITC in future
- ii. Ease of transferability and change of use of land
- iii. Pass the Land Titling Bill pending in Parliament
- iv. Create large scale 'Plug and Play' infrastructure/ ready to move industrial sheds offered to MSMEs on affordable rent.

6. **Unilateral increase in claim period of BGs by Banks**

While issuing a fresh Bank Guarantee (BG) or extending any existing one, Banks have increased 'claim period' of minimum one year from the date of expiry of validity period of the BG and charge accordingly. Generally BGs are issued with no claim period or maximum 3 months claim period. Now even if one requires a BG for six months, Banks would charge for 18 months. MSMEs already suffer from high cost of BGs as Banks demand upfront margin money, then charges for period the BG is in use and more than 100% collateral against BGs. It will have very adverse impact both on exports and large number of MSMEs supplying through tenders both to the Government as well as private agencies. Firstly, the liability is increased for the customers, which is not even required as per contract, due to increase in claim period by 12 months. Secondly, they have to bear the burden of additional bank charges for that unwarranted extended period. Thirdly, their BG limit will get consumed totally unnecessarily due to this additional requirement.

Suggestion:

Firstly, there is a need to thoroughly review the Banking practices for issuing the BGs and issue guidelines on price band too. Secondly, the claim period should be restricted to the period of validity of BG. Thirdly, the BGs being non-fund based financial product used to cover future risk, they should be allowed to be offered by Insurance companies as is the case in other countries such United States. This will increase competition and reduce cost.

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