The Medium, Small and Micro Enterprises Development (Amendment) Bill, 2018

I. Introduction

The Micro, Small and Medium Enterprises Development (Amendment) Bill, 2018 aims to amend **section 7** of The Micro, Small and Medium Enterprises Development Act, 2006. It was introduced in Lok Sabha by the Minister of State for Micro, Small and Medium Enterprises, Mr. Giriraj Singh on July 23, 2018. The bill re-classifies micro, small and medium enterprises as given within the original act.

This change was felt necessary due to the changing business ecosystem, and the trends that were being observed due to the previous method of classification. It was seen that the existing classification based on investment led to the stagnation of several industries, and did not provide enough incentive for them to grow. In this situation, it was felt necessary to propose a re-classification, due to the changing times. The aim of the new bill is to align companies towards growth, promote ease of doing business, and to make it easier to adjust to the new tax regime of GST (Goods and Services Tax).

II. The Medium, Small and Micro Enterprises Development (Amendment) Bill, 2018

The bill is primarily aims to restructure the way these industries are categorized by introducing a uniform classification, in an effort to encourage them, and to remove certain practical lacunae that existed in the the earlier framework.

Salient Features of the Bill[1]

- **Classification on turnover:** During their consultation with various stakeholders, the Ministry found that the existing classification based on investment in plant and machinery or equipment, was leading to industries keeping their industries at a small size. This is due to the fact that the classification requires physical verification of the transaction costs of these investments. This encourages industries classified

[1] The Medium, Small and Micro Enterprises Development (Amendment) Bill, 2018

as micro or small enterprises to keep their business size small to retain the benefits associated with this, and does not foster a spirit of growth, thus defeating the objective of the Act.

In such a situation, the ministry has proposed an alternative classification structure based on annual turnover of the enterprise. This is proposed to be done using the information that is currently available with the GST network, or other sources, in order to re-classify the industries.

- **Uniformity of Classification:** Presently, the industries under the MSME Act, 2006 are categorized as per their investment in (i) plant and machinery, for enterprises engaged in the manufacturing or production of goods, and (ii) equipment, for enterprises providing services. Given that the proposed bill now classifies industries as per annual turnover, this distinction between industries providing goods and services will be done away with.

  The new limits are as follows:

Change in Classification of MSMEs			
Type of Enterprise	**MSME Act, 2006**		**MSME Bill, 2018**
	Investment in Plant and Machinery	Investment in Equipment	New Classification: Annual Turnover
Micro	25 lakh	10 lakh	5 crore
Small	25 lakh to 5 crore	10 lakh to 2 crore	5 to 75 crore
Medium	5 to 10 crore	2 to 5 crore	75 to 250 crore

- **Power of the government to change limits:** The new bill gives the power to the central government to change the annual turnover limits for MSMEs through the passage of a notification. This has been done to provide for changing circumstances and industry standards. However, there is a limitation to this power, with the change limit being a maximum of three times the turnover limit specified in the Bill.

Benefits of the Bill

- **Expansion of the MSME Definition:** Now that turnover is proposed as a metric for classification, industries are now incentivized grow, as increased investments will no longer remove them from the MSME category. Thus, they can continue receiving benefits such as tax incentives. Presently, many industries faced disadvantages, as their high investment rate kept them out of the MSME definition.

- **Boost to Modernisation:** The ease of industries to freely invest, without being removed from the MSME category, will be a boost to modernization of many small enterprises. This, in turn, will spur the mechanization industry. It will specifically benefit technology-intensive sectors, such as food processing and pharmaceuticals.

- **Ease in Classification:** Instead of the previous system of physical verification of transaction costs, in the new classification annual turnover of companies can be obtained from the data present with the GST network. This puts an end to physical inspections necessitated by the investment-based regime, and increases the transparency and accountability in the classification process.

- **Long-term Planning:** The amendment takes into account the changing business ecosystem, inflation, high rate of growth of MSMEs, and the shifting market trends. This is shown in the fact that the bill has a built in mechanism for increasing the limits for annual turnover, thereby allowing the government to allow more industries to be included within the scope of the Act, without the need for a long-drawn amendment process. This is a well thought-out clause as it also includes a limitation on how much the limit can be raised, and thereby ensures a check on government power.

Shortcomings of the Bill

- **Exclusion from Public Procurement Policies:** The bill may affect industries and enterprises falling within specific brackets i.e. those who has a relatively smaller investment rate, but high turnover. In such a situation, they may now be categorized from small to medium enterprises, or even lie outside the MSME bracket.

  This affects their access to crucial benefits, including reservation under the Public Procurement Policy, as per which all central government purchases reserve **20 percent** of tenders for Micro and Small Units. The Public Procurement Policy for MSMEs would now no longer apply to those with an annual turnover of more than 75 crores. Under the new bill, several industries currently categorized as micro or small, may now be shifted to the medium category, and are no longer eligible for reservation for such tenders. This will affect both the enterprises, as well as the government, who may have a dearth of bids under the reserved category. A move can be made to include medium industries in the reserved pool, in cases where there too few bids.

- **Employment-based classification not considered:** An alternative metric for classification is the number of persons employed by an enterprise. This metric is globally considered reliable, and should have been considered when deciding on how to categorise MSMEs under the new bill. However, it is possible that this was not taken up due to the impracticality of verifying this information. There is no proper system in place to cross-check employment transparently, and the practice of underreporting numbers is rampant across small industries. A lack of labour reforms has made the situation even worse.

III. Conclusion

Overall, the new definition is a vast improvement over the earlier definition and should help MSMEs to face new challenges with the help of a better framework. However, a few issues need to be addressed, to ensure that certain enterprises do not suffer due to the re-classification.