REPORT NO.

294

PARLIAMENT OF INDIA

TWO HUNDRED NINETY FOURTH REPORT

ON

MICRO, SMALL AND MEDIUM ENTERPRISES DEVELOPMENT (AMENDMENT) BILL, 2018

Pertaining to

The Ministry of Micro, Small and Medium Enterprises

(Presented to the Rajya Sabha on 28th December, 2018)

(Laid on the table of Lok Sabha on 28th December, 2018)

RAJYA SABHA

DEPARTMENT-RELATED PARLIAMENTARY STANDING COMMITTEE ON INDUSTRY

Rajya Sabha Secretariat, New Delhi
December, 2018/Pausa, 1940 (Saka)

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C O N T E N T S

* To be appended at printing stage

COMPOSITION OF THE COMMITTEE
(2018-19)

RAJYA SABHA

1. **Shri Ram Chandra Prasad Singh** — ***Chairman***
2. Shri G.C. Chandrashekhar
3. Shri Ram Narain Dudi
4. Shri Md. Nadimul Haque
5. Shri Shwait Malik
6. Shri Sanjay Seth
7. Shri Amar Singh
8. Shri Tiruchi Siva
9. Shri T. G. Venkatesh
10. Dr. Amee Yajnik

LOK SABHA

11. Shrimati Ranjanben Dhananjay Bhatt
12. Shri Birendra Kumar Chaudhary
13. Shri Feroze Varun Gandhi
14. Shri S. P. Muddahanume Gowda
15. Shri G. Hari
16. Shrimati Darshana Vikram Jardosh
17. Shri Rabindra Kumar Jena
18. Shrimati Poonamben Hematbhai Maadam
19. Shri Bidyut Baran Mahato
20. Shri Mutthamsetti Srinivasa Rao (Avanthi)
21. Shri Ramsinh Pataliyabhai Rathwa
22. Shri Konda Vishweshwar Reddy
23. Shri Raj Kumar Saini
24. Shri Rajveer (Raju Bhaiya) Singh
25. Shri Rameswar Teli
26. Shrimati Savitri Thakur
27. Shrimati Dev (Moon Moon Sen) Varma
28. Shri Rajan Baburao Vichare
29. Vacant*
30. Vacant
31. Vacant

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* Vacancy caused due to demise of Shri Asrarul Haque Mohammed

SECRETARIAT

Shri Jagdish Kumar, Joint Secretary

Smt. Sasilekha Nair, Director

Shri J.K. Mallick, Additional Director

Smt.Sreeja.V, Deputy Secretary

Shri Anil Kumar Saini, Deputy Secretary

Shri Ajin J.R., Under Secretary

Smt. Renu Sreekanth, Committee Officer

Shri Devinder Singh Bisht, Committee Officer

Shri Anuj Verma, Assistant Research Officer

INTRODUCTION

I, the Chairman of the Department-related Parliamentary Standing Committee on Industry, having been authorized by the Committee, hereby present this Two Hundred Ninety Fourth Report on Micro, Small and Medium Enterprises Development (Amendment) Bill, 2018 pertaining to the Ministry of Micro, Small and Medium Enterprises.

2. In pursuance of Rule 270 of the Rules of Procedure and Conduct of Business in the Council of States relating to the Department-related Parliamentary Standing Committees, the Chairman, Rajya Sabha referred the MSMED (Amendment) Bill, 2018 (Annexure-I) on the 01st October, 2018 as introduced in the Lok Sabha on the 23rd July, 2018 for examination and Report within 3 months.

3. The Committee in its meeting held on the 09th October, 2018 decided to invite the Experts on the subject and the Stakeholders/Associations concerned to hear their opinion/views/suggestions on the proposed Amendment.

4. The Committee heard the views of Ministry of Micro, Small and Medium Enterprises and the Ministry of Law & Justice (Legislative Department) on the Amendment Bill.

5. The Committee held four sittings during the course of examination of the Bill i.e., on 01st, 09th & 16th November and 27th December, 2018. The list of witnesses heard by the Committee is at Annexure-II.

6. The Committee has relied on the following documents in finalizing the Report:

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

(ii) Presentation, clarification and oral evidence of Secretary, M/o MSME;

(iii) Oral evidence and written submissions by various Stakeholders/Experts on the Bill;

(iv) Replies received from the M/o MSME to the Questions/Queries raised by the Members during the course of the meetings on the Bill; and

(v) Clarifications received from Legislative Department, (M/o Law & Justice).

7. The Committee considered the draft Report and adopted the same on 27th December, 2018.

8. On behalf of the Committee, I would like to acknowledge with thanks the contributions made by those who deposed before the Committee and also those who gave their suggestions to the Committee through their written submissions.

9. For facility of reference and convenience, the recommendations of the Committee have been printed in bold letters in the Contents of the Reports.

RAM CHANDRA PRASAD SINGH
Chairman
Department -related Parliamentary
Standing Committee on Industry
Rajya Sabha

New Delhi,
December, 2018/
Pausha, 1940 (Saka)

Report

BACKGROUND

1.1 The MSMED Act, 2006 provides the regulatory framework for MSMEs. Prior to coming into effect of the Act, the sector was known as Small Scale Industries Sector. With the advent of the Act, the concept of 'Enterprises' as against 'Industries' was brought in. It thus added 'Services' into the framework in addition to 'Manufacturing'.

1.2 In the Micro, Small and Medium Enterprises Development Act, 2006 (the MSMED Act), there is a provision for classifying micro, small and medium enterprises. Over a period of time, it was felt necessary to change the definition/ classification criteria to align them with needs of the current times and the changing business ecosystem.

1.3 The Section 7 of the MSMED Act classifies the Micro, Small and Medium Enterprises (MSMEs) on the basis of investment in plant and machinery for manufacturing units, and investment in equipment for service enterprises. The relevant provision of Section 7 (1) of the MSMED Act is reproduced below:

> **"7. Classification of Enterprises** – *(1)* Notwithstanding anything contained in section 11B of the Industries (Development and Regulation) Act, 1951, (65 of 1951) the Central Government may, for the purposes of this Act, by notification and having regard to the provisions of sub-sections *(4)* and *(5)*, classify any class or classes of enterprises, whether proprietorship, Hindu undivided family, association of persons, co-operative society, partnership firm, company or undertaking, by whatever name called,
>
> *(a)* in the case of the enterprises engaged in the manufacture or production of goods pertaining to any industry specified in the First Schedule to the Industries (Development and Regulation) Act, 1951 (65 of 1951), as-
>
> *(i)* a micro enterprise, where the investment in plant and machinery does not exceed twenty-five lakh rupees;
>
> *(ii)* a small enterprise, where the investment in plant and machinery is more than twenty-five lakh rupees but does not exceed five crore rupees; or
>
> (*iii)* a medium enterprise, where the investment in plant and machinery is more than five crore rupees but does not exceed ten crore rupees;
>
> *(b)* in the case of the enterprises engaged in providing or rendering of services, as-
>
> *(i)* a micro enterprise, where the investment in equipment does not exceed ten lakh rupees;
>
> *(ii)* a small enterprise, where the investment in equipment is more than ten lakh rupees but does not exceed two crore rupees; or
>
> *(iii)* a medium enterprise, where the investment in equipment is more than two crore rupees but does not exceed five crore rupees.

.4 A Group of Secretaries examined the issues relating to Commerce and Industry and in their Report, recommended that the Ministry of MSME may examine and work out suitable criteria involving additional parameters such as turnover and employment which could be used in combination for classification of firms as MSMEs.

1.5 As per the submission of the Ministry of MSME, they had consulted various stakeholders and the predominant view that emerged was that the criterion of investment in plant and machinery stipulates self declaration, which entails verification, if deemed necessary, and associated transaction costs. Similarly, employment as a criterion has problems associated with factors such as seasonality and informal nature of engagement. This may also entail verification/inspection with avoidable transactions costs for MSMEs. Taking annual turnover as a criterion overcomes all these shortcomings as it can be pegged with reliable figures available in GST Network and other important methods of ascertaining.

1.6 The Ministry has stated that the following are the other important observations that came forth during the course of their consultations with the stakeholders:

(i) There is a need to put in place a non-discretionary, transparent and objective definition of the MSMEs to further promote the ease of doing business.

(ii) There is a need to put in place a classification framework which incentivizes the enterprises to grow continuously.

(iii) There is a need to align the classification of MSMEs to annual turnover pegged with reliable figures available e.g. in GST Network and other methods of ascertaining which will result in an automatic and unambiguous classification of enterprises.

(iv) There is a need to provide certain flexibility to the Government to modify the definition criteria specified under the MSMED Act to cater to the need of aligning them with the changing business ecosystem.

1.7 Accordingly, the Ministry of MSME, therefore proposes to amend sub-section (1) of Section 7 of the MSMED Act, 2006 to read as under:

> "*(1)* Notwithstanding anything contained in section 11B of the Industries (Development and Regulation) Act, 1951, (65 of 1951) the Central Government may, for the purposes of this Act, by notification and having regard to the provisions of sub-sections *(4)* and *(5)*, classify any class or classes of enterprises, whether proprietorship, Hindu undivided family, association of persons, co-operative society, partnership firm, company or undertaking, by whatever name called, engaged in the manufacture or production of goods pertaining to any industry specified in the First Schedule to the Industries (Development and Regulation) Act, 1951, or engaged in providing or rendering of services, as-
>
> *(i)* a micro enterprise, where the annual turnover does not exceed five crore rupees;

(ii) a small enterprise, where the annual turnover is more than five crore rupees but does not exceed Seventy -five crore rupees;

(iii) a medium enterprise, where the annual turnover is more than seventy-five crore rupees but does not exceed two hundred and fifty crore rupees";

(1A) The Central Government may, by notification, vary turnover limits, which shall not exceed thrice the limits specified in sub-Section *(1)* for the purposes of development of micro, small and medium enterprises."

THE MICRO, SMALL AND MEDIUM ENTERPRISES DEVELOPMENT (AMENDMENT) BILL, 2018- AN INTRODUCTION

2.1 The Micro, Small and Medium Enterprises Development (Amendment) Bill, 2018 was introduced in Lok Sabha on 23rd July, 2018 (Annexure-I), (hereinafter referred to as the Bill) and referred to the Department-related Parliamentary Standing Committee on Industry by the Hon'ble Chairman, Rajya Sabha in consultation with the Hon'ble Speaker, Lok Sabha on 01st October, 2018 for examination and report thereon within 3 months.

2.2 The Bill seeks to amend Sections 7 (1), (9) and 14 (2) of the Principal Act. The Bill also proposes to introduce a new clause as Section 7(1A) in the Principal Act which empowers the Government to vary the turnover limits not to exceed thrice the limits for the purpose of development of Micro, Small and Medium Enterprises.

The Statement of Objects and Reasons to the Bill

3.1 The Micro, Small and Medium Enterprises Development Act, 2006 was enacted to provide for facilitating the promotion and development and enhancing the competitiveness of micro, small and medium enterprises. The said Act, *inter alia*, provides for classification of the enterprises as micro, small or medium based on their investment in plant and machinery or equipment for manufacturing and service sectors respectively. Over a period of time, it has been felt necessary to change the criteria for the classification in order to align it with the need of current times and changing business ecosystem.

3.2 In the course of consultation with various stakeholders, it has been noted that the criterion of investment in plant and machinery or equipment entails physical verification having associated transaction costs. It also incentivises the tendency in the promoters of the enterprises to keep the investment size restricted in a particular business entity in order to retain the benefits associated with micro or small enterprises category. While evaluating various alternatives, it has been considered appropriate that if the annual turnover is taken as a criterion for classification, the information available with goods and services tax network and other sources can be used for determination and classification of the category of the enterprises. Overall, the turnover based clasification will promote the ease of doing business and will put in place a non-discretionary, transparent and objective classification system. Besides, it will bring an end to the physical verification system and Inspector Raj.

3.3 In view of the above, it is proposed to amend section 7 of the Micro, Small and Medium Enterprises Development Act, 2006 and to achieve the following objectives:

(*a*) provide for change in the criterion of classification of micro, small and medium enterprises from the existing criterion of investment in plant and machinery or equipment to a new criterion based on annual turnover of the enterprises; and

(*b*) confer power upon the Central Government to vary, the turnover limits, by notification which shall not exceed thrice the limits specified in sub-section (*1*) of section 7 for the purpose of development of micro, small and medium enterprises.

4.1 As per the information provided by the Ministry of MSME, the objectives of the Bill are

(i) To have a non-discretionary, transparent and objective criteria of classification and to eliminate the need for inspections and avoidable associated transaction cost;

(ii) To make the classification system progressive, dynamic and adaptable to prevailing business ecosystem;

(iii) To overcome the uncertainties associated with the classification based on investment in plant & machinery/equipment and employment;

(iv) To improve the ease of doing business; and

(v) To provide flexibility to the Government to fine-tune the classification of MSMEs in response to changing economic scenario without resorting to the amendment of MSMED (Micro, Small & Medium Enterprises Development) Act.

4.2 The facts narrated above laid the justifiable ground for bringing an amendment in the criterion of classification.

EXAMINATION OF THE BILL BY THE COMMITTEE

5.1 Considering the implications involved in the proposed amendment and its impact on the entrepreneurs at large, the Committee decided to hear the views and suggestions of Experts on the subject, stakeholders, concerned associations and the Ministry of MSME. The Committee invited the representatives of various organisations/associations and renowned experts and held extensive interactions with them. These included Dr. Prabhat Kumar, Ex-Cabinet Secretary & Ex-Governor Jharkhand who was also the Chairman of the One-Man Committee appointed by the Ministry of MSME to study MSME Policy; Dr. H.P.Kumar, Ex CMD, NSIC & Advisor PHD Chamber of Commerce & Industry and the representatives from (i) Laghu Udyog Bharati (LUB); (ii) The Coimbatore District Small Industries Association (CODISSIA); (iii) Confederation of Women Entrepreneurs(COWE); and (iv) Chamber of Indian Micro, Small and Medium Enterprises (CIMSME).

6.1 The Secretary, M/o MSME in his presentation before the Committee stated that India has improved its global ranking in Ease of Doing Business in the last four years from the rank of 142 to the rank of 77. Earlier MSMEs used to be in the informal economy. Now after demonetisation and GST, they are gradually coming to the formal economic framework. More than one crore MSME units, approximately 1.16 crore units have registered under the GSTN, which is a paradigm shift. Therefore, there is a requirement to make the classification criterion transparent, objective and non-discretionary. Today, MSME being an aspirational sector, it needs to be encouraged and nurtured carefully for its proper growth and development. He stated that, accordingly, many rounds of discussions were held with various stakeholders and Industry Associations before proposing the MSMED (Amendment) Bill.

6.2 In their presentation, M/o MSME apprised that the MSMED Act came into force in the year 2006. As per the existing provisions, service providing & manufacturing sectors were categorized as two different sectors and accordingly the enterprises in the Manufacturing Sector as well as Service Sector were classified in three categories *viz.* Micro, Small and Medium based on their investment in plant, machinery and equipment. However, as per the new proposed MSMED (Amendment) Bill, 2018, both Services and Manufacturing Sectors have been integrated as one common sector.

6.3 The Secretary, M/o MSME further added that in the present investment criterion, the land and buildings are not included in both manufacturing and service sector.

6.4 The Secretary, M/o MSME further stated that the purpose and benefit of classification of MSMEs is that the Ministry runs various schemes/programmes like Credit, Technology, Infrastructure, Marketing and Skill Development and the classification enables the micro and small enterprises to enjoy the major share of benefits of such schemes/programmes. It also helps to achieve the long-term objective of large-scale employment generation. However, the problem with the present classification criterion is, there is lack of a transparent and online system of verification of MSMEs. The present system involves physical inspection leading to increase in transaction costs and it inhibits investment, scale-up, modernization and growth of enterprises. Moreover, there has been significant price rise since the adoption of MSMED Act, 2006, which has made the current threshold level irrelevant.

6.5 Further, it was stated that globally the classification of enterprises is done on the basis of number of employees in the countries like UK, USA, Republic of Korea, China *etc*. In South Africa classification is done in combination of turnover and employment criteria. But the problem with employment criteria in Indian context is non-availability of reliable/verifiable sectoral data and the seasonal variance in labour engagement. The employment system, if taken into consideration, will increase the need for inspection, which will involve huge transaction cost and could place a question mark on the veracity of the figures given by the Enterprises in different Sectors. Moreover, it will also lead to large number of litigations. The Ministry has therefore, opted for turnover criterion and proposed amendment through MSMED (Amendment) Bill, 2018. The turnover criterion will bring an unambiguous, transparent, non-discretionary, objective and online framework for classification. The data can be easily verified from the reliable information available with the GST network. Provision of 'Notarized Statement' is also made available to enterprises that are not registered in GST Network. Further, turnover criterion will encourage investment in modernization and scaling up and will also simplify the procedure and promote the ease of doing business. Necessary safeguards shall also be put in place by adopting suitable policy measures to counter the possibility of MNCs cornering the incentives meant for MSMEs *etc*. Besides, the turnover as on 1st April of a particular financial year will be taken as the turnover of a particular entity in that Financial Year. Regarding regulation of the investment of MNCs, it was informed that it is a matter of Foreign Direct Investment and has to be dealt with the concerned authorities such as Foreign Investment Promotion Board and that change of classification criteria has no role in this.

6.6 The Secretary stated that in the present scenario, the turnover criterion is the best formula. As regards the determination of limits of each slab, there is flexibility for change, which could be deliberated upon, however the main objective is to change the classification criteria from investment to turnover.

7. The Committee while examining the Amendment Bill had made certain observations, which were forwarded to the M/o MSME for their response.

7.1 The Committee was given to understand that an amendment was proposed regarding upward revision of investment in plant and machinery and equipment in the MSMED (Amendment) Bill, 2015. However, the Ministry informed that the amendment did not come into force and the MSMED Amendment Bill, 2015 was withdrawn and, in its place, the MSMED Amendment Bill, 2018 has been introduced in the Parliament regarding change in the criteria of classification of MSMEs from investment in plant & machinery to annual turnover. The Ministry of MSME also had consultations with various MSME Associations and other Stakeholders in the National Board for MSME and this necessitated the withdrawal of the previous Amendment Bill of 2015.

7.2 The Committee inquired about the impediments that are stalling the growth of MSMEs in the present criterion of classification based on investment in plant and machinery/equipment to which the Ministry of MSME stated that they consulted various stakeholders and the predominant view appeared to be that the criterion of investment in plant and machinery stipulates self declaration which entails verification and associated transaction costs. There is no online and transparent system to verify the data/figures regarding such investment. Moreover, it hinders investment as the MSMEs like to stay under the ceiling for remaining eligible to access benefits under various Government Programmes and priority sector lending. Thus, it inhibits growth and modernization. Similarly, employment as a criterion has problems associated with factors such as seasonality and informal nature of engagement/employment for which no data/records exist and also entails verification/inspection with avoidable transactions costs for MSMEs. On the other hand, the annual turnover criterion overcomes these shortcomings as it can be pegged with reliable data available in GST Network and other methods of ascertaining. This would be rather transparent, non-discretionary and verifiable method for ascertaining.

7.3 The Committee also took note of the provisions of Section 7 (4) of the MSME Development Act, 2006, which stipulates that the Central Government shall obtain the recommendation of the Advisory Committee prior to classifying any class or classes of enterprises. The Committee, therefore, desired to know about the details of reports/recommendations of the Advisory Committee constituted for the purpose. In response, the Ministry of MSME stated that recommendations of the Advisory Committee were not obtained, as the classification for change in criteria was referred directly to the National Board for MSME in its meeting held on 26.02.2018. None of the Members opposed in particular to the change in criteria to turnover basis. Besides, the matter was also placed before an informal Group of Ministers and the Group recommended to adopt the criterion of annual turnover.

7.4 The Committee further desired to know the rationale and underlying principle based on which the proposed turnover limits have been arrived at in the MSMED (Amendment) Bill, 2018. It was stated by the Ministry of MSME that the limit of Rs 5 crore has been arrived at by multiplying the earlier limit with a factor of 20. As this sector is growing and needs large-scale investment, higher limits of annual turnover, have been suggested for Small and Medium Enterprises, so that they can grow without worrying about the limits.

7.5 The Committee noted that as per the existing provisions, separate classification or investment limit is earmarked for manufacturing enterprises and service rendering enterprises. However, no justification has been given by the Ministry of MSME for the proposed amendment setting the common annual turnover limit for both manufacturing and service enterprises. The Ministry of MSME submitted before the Committee that the extant MSMED Act, 2006, encompasses in its scope both manufacturing and services. The proposed amendment doesn't differentiate between manufacturing and services sector since turnover is supposed to be an activity-neutral criterion unlike investments in plant & machinery or equipments in which manufacturing and services enterprises differ greatly from each other. There is a need to keep the criterion very simple which will have no scope for interpretation (whether manufacturing or service unit) or inspection.

7.6 The Committee also noted that the One-Man Committee on the MSME Policy had viewed that a change in the criteria of defining MSMEs would not add any value to the development, sustenance and growth of the enterprises. Even, no entrepreneur, federation of associations of MSMEs has demanded change in the criterion. In response, the M/o MSME informed that GST had not been launched when the One Man Committee considered the matter. This digital platform would help immensely in having a transparent, online, non-discretionary system. The Ministry of MSME is of the view that change in the criteria of defining MSMEs will add value to the existing system. There are Associations/units who have supported and requested the Ministry of MSME to expedite issuing the notification of change in the criteria on turnover basis. Some of them are: The Associated Chambers of Commerce and Industry, Delhi; Chamber of Indian Trade & Industry, Delhi; Calcutta Chamber of Commerce, Kolkata; Apex Chamber of Commerce & Industry, Punjab; Focal Point Industries Association (Regd), Amritsar, *etc.*

7.7 The Committee observed that the Laghu Udyog Bharati, New Delhi and Jharkhand Small and Tiny Industries Association have objected to the proposed classification on the turnover basis on the plea that turnover may change on year to year basis but after the clarification given by the M/o MSME on cut off date i.e. 1st April of a particular financial year, for arriving at turnover and inclusion of Scheme-Specific safeguards, their objections seem to be mitigated.

7.8 The Committee also inquired about the yardstick for registration under different categories for new entrepreneurs since the turnover of an MSME can be ascertained with GST Network and other sources only after completion of more than one year in operation to which the Ministry replied that the enterprise can estimate its turnover at the initial stage of setting up of an enterprise and the selling price of the product and accordingly register itself.

7.9 To a query about the introduction of the employment criterion along with turnover for classification purpose of MSMEs entailing further associated transaction cost, the Ministry stated that if the employment criterion is also included in the definition for MSMEs, the enterprise would start taking all precautions to restrict/limit their numbers to ensure that various laws/regulations are not applicable and such a situation would act as a barrier in their growth and would encourage Inspector Raj.

7.10 The Committee took note of the observation made by the Department of Expenditure that no financial implication is involved. Further, the Committee desired to know what necessitated to change the criteria of MSMEs from investment in plant and machinery to annual turnover. The Ministry of MSME clarified that the turnover criteria for Micro, Small and Medium Enterprises have been suggested keeping in view the need to ensure continued inclusion of the maximum number of Micro and Small Enterprises in the respective categories even in the changed classification framework. Simultaneously, the scope for encouraging transition of Micro Enterprises to Small and Medium Enterprises and eventually as large enterprises has also been factored in while making the proposed change in the criterion.

7.11 The Committee considered the apprehensions existing in the MSME Sector that if the upper/limit of annual turnover for micro enterprises is earmarked as Rs. 5 crores, particularly the manufacturing entities on the lower end with annual turnover of a few lakhs would get totally crowded out by the larger firms. The Ministry of MSME submitted before the Committee that the proposed classification shall not only increase number of enterprises in the MSE sector but there will be shifting of enterprises also from small and medium sectors and hence the budget allocation for MSME Sector by the Government has to be increased. Moreover, due safeguards would be taken in various schemes by the Ministry of MSME to provide help to the micro enterprises on the lower end.

7.12 The Committee has taken note of the observations made by the Department of Economic Affairs to consider creating separate sub-categories for manufacturing and services sectors as both the sectors follow different business models. On the issue of sub-categories, it was stated by the M/o MSME that the separate sub categories for manufacturing and services sectors in the existing arrangement, were based on the criterion of investment in plant and machinery/equipment. As the scale of investments in the manufacturing and services sectors varied significantly hence separate limits were prescribed. As it is proposed now to move on to annual turnover as the sole criterion, the aforesaid sub-categories have been done away with.

7.13 The Committee noted that the proposed amendment has been opposed by some associations on the ground that it will ruin the small entrepreneurs who are surviving on the little incentives they gain under the umbrella of MSMEs. However, with this change in definition, they stand to lose even that advantage. The Ministry of MSME informed that even though some associations have represented against the change in the classification of MSMEs but at the same time large number of associations have also supported the new definition. The necessary adjustments can be made in due course in the policy and schemes for incentives to the Micro and Small enterprises so that no segment gets adversely affected.

7.14 The Committee is given to understand that Karnataka State Small Scale Industries Association (KASSIA) has protested against the proposed amendment to change the definition of MSME claiming that amendment based on turnover is allegedly designed to help large entrepreneurs and would negatively impact the small enterprises. Explaining the situation, the Ministry stated that KASSIA has protested against the proposed amendment to change the definition of MSMEs by their representation dated 01/08/2018, addressed to Hon'ble PM. In the same representation the Association has also appreciated the need for adopting a scientific definition of SMEs keeping in view the global trends. Further, in a joint representation dated 22/02/2018 by TANSTIA, KASSIA, KSSIA, FSME-INDIA, FETSIA, FAPSIA addressed to Hon'ble MoS (IC) for MSME, these Associations had demanded to reduce the turnover limit.

7.15 The Committee observes that some associations had apprehensions that the amendment would affect MSME entrepreneurs negatively, as they will lose government benefits that they are getting and big entrepreneurs will grab all the benefits thus affecting the Make in India Programme, manufacturing sector and creation of jobs. The Ministry informed that its every scheme benefiting the MSMEs would have adequate safeguards against big enterprises grabbing benefits. Due safeguards would be put in place in various scheme guidelines to ensure that even within the category of the MSMEs, the maximum benefits of such schemes accrue to the smaller segments within the Micro and Small Sectors. The Committee was given to understand by the M/o MSME that while considering the issue of extending the benefits of Government schemes and programmes to those MSME units providing employment to more and more people, the absence of reliable data in this count is major impediment as significant section of people are not in the ambit of ESIC/EPPO who could be relied upon for such data maintenance.

7.16 The Committee queried about the enhancement of employment, reducing poverty and rural-urban migration in view of the new classification and the Ministry stated that the proposed classification of MSMEs is progressive, which would add to the growth of MSMEs and shall pave the way for increased investment, employment generation and reducing poverty and rural-urban migration. The proposed systems of classification is based on consultation with stakeholders and other relevant Ministries, Department/Agencies of the Government.

7.17 The Committee sought clarification if the new definition/classification could see a paradigm shift towards trading and will ignore manufacturing sector. The Ministry of MSME stated that the new definition/classification will not ignore manufacturing sector as the Government is focusing on manufacturing sector. Programmes such as Make in India, Startup India, Standup India, Schemes of NMCP *etc*. are focused to increase the manufacturing sector.

8.1 The Ministry stated that the basic objective of keeping a provision of varying- the turnover limit upto 3 times is to keep the criteria current and effective in the context of changing economic and other factors influencing the enterprise ecosystem.

8.2 The Ministry of MSME on the issue of classification and differentiation for composite/aggregator units in Small and Medium Sector, stated that turnover as a criteria is independent of nature and characteristics of enterprises, be it aggregator or supplier or supporting unit or product sectors like textiles, diamond or jewellery industries. On the contrary, it would classify them only on consideration of turnover.

VIEWS OF THE STAKEHOLDERS

9. The Committee had invited various stakeholders to present their views and suggestions regarding the MSMED (Amendment) Bill, 2018 before the Committee. Few of the stakeholders could not appear in person and preferred to send their written views for consideration of the Committee.

9.1 FEDERATION OF INDIAN MICRO, SMALL & MEDIUM ENTERPRISES (FISME) in their written submission stated that the Micro, Small & Medium Enterprises (MSMEs) are defined under the MSMED Act, 2006 on the basis of capital investment made in plant and machinery. The proposed turnover based criterion resolves many of the ills of earlier regime. It is transparent, as authorities could always cross check the turnover through platforms such as GSTN. No CA certificate would be required to justify the turnover criteria. The new criterion would open level playing field for new and old enterprises as the comparison is not between historical investments and current investments but between current turnovers. Besides being realistic, there is a flip side too. There are few sectors where investment is low but turnover is high. For example gems and jewellery units, units producing Aluminium conductor steel-reinforced cable (ACSR) among others. Many of the units have been under small category owing to investment criteria but having high turnover ranging from Rs. 100 to 300 crore. They enjoy benefits under Public Procurement Policy for MSEs, which mandates 20% set-aside for Micro and Small Units in all central government purchases. Suddenly, the reserved pie of the cake is out of their reach. The Public Procurement Policy would not be available for MSE Units having more than Rs. 75 crore annual turnover. Keeping in view that in the proposed thresholds, there would be hardly any Micro and Small unit that could participate in high volume government tenders, it has been proposed by FISME that where smaller units have not bid, the reserved category benefits could be passed on to Medium enterprises.

9.2 The Indian Banks' Association **(IBA)** also submitted its written views to the Committee. In their written submission, they concurred with the views of doing away with the criterion of investment in plant and machinery, and supported the annual turnover criterion for classification of MSMEs. In its opinion turnover limit for micro enterprise may be enhanced from five crore rupees to twenty crore rupees. This is in view of the fact that the banks have been given target to achieve under Priority Sector Lending (PSL) for Micro Enterprises up to 7.5 percent of ANBC or Credit Equivalent Amount of Off-Balance Sheet Exposure, whichever is higher, as per RBI guidelines. In order to augment the lending and increasing importance of service sector, RBI vide circular no. FIDD.CO.Plan.BC.18/04.09.01/2017-18 dated March 01, 2018 removed the applicable loan limits of Rs. 5 crore and Rs. 10 crore per borrower to Micro/ Small and Medium Enterprises (Services) respectively, for classification under priority sector. Accordingly, all bank loans to MSMEs, engaged in providing or rendering of services as defined in terms of investment in equipment under MSMED Act, 2006, shall qualify under priority sector without any credit cap. It also feels that, implementing change in the definition of classification from asset based to annual turnover based could temporarily disrupt the MSME units. Finally, IBA opined that implementing the turnover-based definition in a phased manner say one, two or three years could give big relief to banks as well as MSME units.

9.3 All India Manufacturers Organisation (AIMO) an apex body for MSME in its written submission stated that it feels if the Government implements the proposed turnover criteria, it will really help MSMEs to survive in the market. AIMO also requested to reconsider the monthly payment of GST as most of the Small Scale Units are struggling to pay GST owing to the prevailing payment cycle in the market which is 90 – 120 days. Even large industries and Government agencies practice this payment cycle. Whereas the Government policy of GST payable in the following month terribly affects the cash flow and the MSME find it tough to cope with this situation and are unable to survive in the market.

9.4 In their submission, the Self Employed Women Association (SEWA) stated that SEWA, registered as a central trade union is organising women workers of the informal economy since 1972 with the twin goals of Full Employment and Self-Reliance. Currently, SEWA has organised 1.5 million workers in the 18 states of India. It favored the criteria for applicability of the Act to the economic enterprises of the informal economy workers like cooperatives, associations, for / not for profit companies etc. should be different than the proposed criteria as their investment is quite low and their annual turnover also is uncertain in the growing stages. The provisions of Act should provide to protect this informal worker economic enterprise and support them in their growth and achieving their development by making changes in the current tax structure and eliminating them from GST. Exemption OR separate limits should be set for the enterprises of informal workers. Furthermore, the clarification is required on the time period for considering the limit of calculating turnover and there is a need for the clarification on the newly incorporated enterprises and for which financial year, the turnover will be calculated. The exclusion from the turnover needs to be specified clearly. Further, SEWA stated that it is difficult for the economic enterprises of the poor workers of the informal sector to survive in this competitive world as they lack capital, technology, marketable skills to survive. Moreover, the current structures/framework are framed keeping in mind the formal sector enterprises. The informal sector enterprises find it difficult to comply with and fit in the structures of the formal sector and are not able to develop due to these. But at the same time such enterprises in informal economy are very important to benefit from economies at scale, standardization, reach market and compete with the main stream and brand building *etc*. In the formal sector enterprises the profit gets concentrated in the hands of few, whereas in the economic enterprises of the informal sector like cooperatives, for / not for profit companies, associations *etc*. the profit gets distributed in all the worker members. Thus, the economic enterprises in informal economy are the surest way to empower them and to make them economically independent. The economic enterprises need long-term investment in the sense of capital, technology and skills to thrive. SEWA made the following suggestions:

(a) Financial Support as loan or invest at affordable rate with Bank guarantee by MSME.

(b) Long term capacity building on Marketing, Business/Institutional Management, to sustain their business.

(c) Increase the annual sales slab up to Rs. 2 crores from the current slab of Rs. 20 lakhs, on GST exemptions for the small and micro enterprises owned by the informal economy workers as well as for those making procurement from the SHGs and Producers Group in order to benefit themselves and groups from the economies at scale.

(d) The informal economy enterprise should not limit to enterprise employing less than 10 workers but should also consider the constitution of the enterprises e.g. ownership and management with the informal economy workers, shareholding among the workers, procurement / services taken from the informal economy workers etc. The registration of such enterprises could be done in consultation with the national level CBOs working in the said area.

9.5 Chamber of Indian Micro, Small And Medium Enterprises (CIMSME) in their written submission have stated that the existing method of classification of MSMEs based on investment in Plant & Machinery disincentivises entrepreneurs to invest in modern, upgraded machinery in order to remain classified as an MSME unit affecting quality and competitiveness of the product. With the turnover based classification, the disincentive against modernization/upgradation of plant & machinery would be removed as it also incentivises splitting up the manufacturing/service unit into more units to retain the MSME character which would be more difficult under the turnover based classification which can be verified from the GST Returns. These loopholes in classification based on investment in plant & machinery allow entities, not otherwise a MSME, to be classified as MSME and enables them wrongly to claim the benefit of self-bidding under section 240-A of the Insolvency & Bankruptcy Code, which is prohibited for non-MSMEs under section 29A of the Insolvency & Bankruptcy Code. The new method of classification would put a stop to this misuse also. Units with turnover of upto Rs.250 crores generally fall under the Small Scale category or the lower end of the Medium Scale category. Under the present system, such units which may have an investment of more than Rs.10 crores in plant & machinery, are unable to get unrelated parties as bidders for their companies under the Insolvency & Bankruptcy Code. The turnover based classification would enable such units to self bid for their assets under the Insolvency & Bankruptcy Code, thereby helping in mitigating the banks' NPAs to that extent. CIMSME favoring the turnover-based classification clarified that turnover-based sanction of credit limits by banks & other financial institutions would be more transparent as these can be verified with the GST returns of the borrowing entity and this classification would encourage units to get GST registered and thereby help in a more extensive formalization of the economy.

9.6 Many of the micro enterprises may not be GST registered today. However, assessment of credit requirements of micro enterprises by banks primarily based on turnover method. So, identifying & classifying micro enterprises on turnover basis would not therefore involve any more cumbersome processes. Finally, in case there is no agreement on the changes, the Act could provide the entrepreneur the option to have his unit classified under the old or the new method. CIMSME was of the view that the classification method chosen by a particular unit should be allowed to be changed only in the 6th financial year from the financial year in which the particular mode of classification was chosen. After a few years, based on the experience gained, the option of the Plant & Machinery method could be dropped altogether as it would ensure minimum dislocation & dissatisfaction.

9.7 The Chamber of Indian Micro, Small & Medium Enterprises (CIMSME) in its deposition broadly agreed with the suggestion of shifting from plant and machinery investment criteria to turnover criterion . So far as the limits are concerned talks could be held for reducing and increasing turnover limits, though it is felt, by and large, that the limits or the ceilings, are fine for micro, small and medium industries in line with the insolvency and bankruptcy code.

9.8 During their deposition before the Committee the Coimbatore District Small Industries Association (CODISSIA) welcomed the proposal of changing the criterion for classification of Micro, Small and Medium Enterprises from the existing criterion of investment in plant and machinery or equipment to a new criterion based on annual turnover of the enterprises. However, CODISSIA suggested that people engaged in manufacturing or production of goods pertaining to any industry and/or engaged in providing and rendering of services should be placed in the category of Micro and Small Industries. They also suggested that special attention should be paid and there should be a separate package and provision for the development of Micro and Small Industries. It further stated that most of the Job Working Industries fall under Micro & Small Industries category. The Micro & Small Industries are already burdened with requirement of additional working capital due to higher slab of 18% GST, since most of the large industries have credit period, ranging from 90 to 120 days. Therefore, it was further suggested that the rate of GST for Job Order be brought down from 18% to 5% as it is done for textile industries with ITC. If this is not done, then the Job Order Industries would be very badly hit due to working capital shortage.

9.9 In their deposition before the Committee, Laghu Udyog Bharati (LUB) acknowledged & appreciated the importance of Micro & Small Industry as the same has become more significant in the present scenario with the increasing population & unmatched opportunities of employment. Further LUB added that the proposal for change in classification was considered by a One Man Committee constituted by the then Government to give recommendation for national policy for MSME. After having wide consultation with stakeholders, it recommended that the redefining of MSMEs will not add any value to the development, sustenance and growth of the enterprise or anything worthwhile over the present system. The One-Man Committee was also of the view that the criterion in vogue may be continued. The representative of the LUB also apprised the

Committee about the turnover on an average in MSME Sector in all three categories for the registered units vis-à-vis unregistered units. It also raised apprehensions about the crowding away of benefits and incentives by large and medium units after the reclassification. This apprehension had been highlighted by the One-Man Committee as stated by LUB that:

(i) The moment the upper limit is raised for small manufacturing to say 15 crores, a small group of medium enterprise will henceforth become Small and will corner all the benefits meant for MSEs in the credit and procurement;

(ii) At the end of FY 2011-12, the total credit supply was meeting only 38% of the total credit leaving 62% credit gap; and

(iii) In terms of percentage, the share of finance gap in the three sub groups of MSMEs worked out to: Micro 77%, Small 19% and Medium 4%.

9.10 Further, LUB stated that most of the countries in the world use a combination of investment in plant and machinery along with number of persons employed by respective unit. According to LUB, the new criterion does not take into account the type of activity whether manufacturing or trading and if trading is registered as industrial enterprise then it will encourage trading only and manufacturing will be disrupted**.** This will be against the objective of making India a manufacturing hub and Make in India scheme. Since there is no limit on plant and machinery investment, the units will tend to procure costly automatic machines thereby reducing job opportunities further. There are chances that once registered as Micro or Small Enterprise, any MNC can produce product worth thousands of rupees and then market it through various subsidiaries all registered as Micro/Small under GSTN. The criterion is dynamic in nature and may change from one quarter to another quarter and this will create more confusion. The basic objective of creating a separate Ministry for MSMEs to promote, support and protect them will be defeated. MSEs not only provide maximum job opportunities but also ensure equitable and inclusive growth. The future of India Micro & Small Industry, which is 2nd largest contributor to National GDP & employment is at stake if the Definition Criterion is changed as proposed.

9.11 LUB urged for careful and judicious consideration and suggested that:

(a) The definition criterion of Micro & Small Industry should be based on threshold limits of less than Rs. 50 lakhs for Micro and more than Rs. 50 lakh & less than Rs. 500 lakh for Small.

(b) It supported formulating a separate policy for Micro and Small Industries and exclude the Medium sector from the purview of current MSMED Act, 2006 and make it as " Micro & Small Industry Act.

(c) It also favored the applicability of MSI status "Indian Ownership and Management" Industries only.

9.12 The Representatives from the Confederation of Women Entrepreneurs (COWE) stated before the Committee that the Confederation of Women Entrepreneurs was formed in 2004 with the idea of upliftment of women and promoting women entrepreneurs and now there are about one thousand women who are strongly growing and helping each other in their different businesses and entrepreneurship. The first suggestion from COWE is not to consider the machinery as the part of criterion of turnover, since a person with minimum investment could build up a turnover in crores. The procurement cost of raw materials *etc.* of an enterprise of 250 crore turnover and 5 crore turnover would be extremely different. The procurement cost of raw material for a firm with 5 crore turnover goes very high, Therefore, when the raw material is bought at a higher cost, it is not possible to sell the product at a cost which is lower than the bigger corporate or even the medium enterprise. It was pointed out that the turnover gap is very huge and the small scale sector can never match with it and the biggest challenge faced by Micro and Small units is to match the rates of bigger corporate. The second important point put forth before the Committee was about skill development and industry wise knowledge as every industry has its own specific problems. In tea industry the specifications would be different, in NGO it would be different. The industries in their opinion today lacked the right knowledge and approach to the right department where one can go and take their business to the next level.

10.1 Besides Dr. Prabhat Kumar, Ex-Cabinet Secretary and Ex-Governor, Jharkhand also appeared before the Committee. The Committee invited him to hear the views as he headed the One-Man Committee appointed by the Government to report on the problems that prevailed in MSME Sector. He stated that being Chairman of the One-Man Committee on MSME, he interacted with a large number of associations of Small, Medium and Micro Enterprises but did not find any consolidated or reasoned demand for such a change in classification. Surprised on the proposed Amendment Bill, he stated that as in this age when the small scale sector, the MSME sector is struggling with a number of problems – there is a stressed economy, shrinking employment, liquidity crunch, marketing problems, depressed markets, depressed exports, the government would bring a more comprehensive package for the whole sector. But only an Amendment Bill have been preferred, which mainly deals with the method of classification of Micro, Small and Medium enterprises. He feels that the method of classification may apparently appear to be simple and innocent but it has wide implications and further added that there was no major reasoned demand for such a change in classification. Moving on the discussion further, he also stated that there were various suggestions and recommendation in his report, which could have been considered by the government and brought in the form of different bills. Clarifying his statement, he also quoted few examples *viz.* delayed payments, which should be dealt with urgently, problem of liquidity in the banking sector for lending to the MSMEs, nurturing the Micro & Small Industries etc. He moved on to state that objects and reasons say that the Amendment Bill, 2018 is to promote and develop the sector but he feels that there is no value in this amendment which will develop or promote the sector. In fact it might create some more difficulties, not major difficulties, because hundreds of thousands of small and micro units will have to undergo this process of redetermination of their classification. Commenting on the amendment proposed in the Bill before the Committee, he expressed his apprehension over the transition that may take place in MSME Sector and added that it is not clear how the classification will be done from year to year because if the turnover fluctuates due to market conditions, then the classification would also change accordingly. The major concern which came up before the Committee from him was on account of employment as MSME Sector has the greatest strength in providing the bulk of employment outside the agriculture sector, at lesser investment than the organised sector. Therefore, he views the new proposal of turnover criterion as an anti-employment measure. Therefore, his suggestion is that in a country like India where the capital is scarce, it should continue to be with investment criterion.

10.2 Dr. H. P. Kumar, Ex-CMD, NSIC & Advisor appeared before the Committee and complimented the Ministry of MSME for bringing out these amendments/changes in the definition of MSME. He further stated that over the last decade, he has been associated with the MSME sector and it was observed that there are great difficulties in certifying and identifying the Micro, Small & Medium enterprises based on the definition which exist today *i.e.* investment in plant & machinery. He further stated that sometimes the branch head or the implementing officers are not able to certify themselves as to whether it is a micro, small or medium enterprises based on the investment criterion, in which case, they ask for certificate by the Chartered Accountant or Audited Accounts or

Audit Report inviting additional expenditure on the part of the enterprise. Internationally, some countries classify on the basis of turnover, some classify on the basis of employment, while some on the basis of the size of balance sheet and some combine two or three criterion. However it is felt combining two or three criterion again becomes a challenge for the dispensing authority to identify the accurate nature of the enterprise. Regarding the employment criterion it has been a general observation that the moment the employment is restricted to 10 for micro or 20 for small enterprises, people may stop recruiting more people and they may try to keep the number below 10 or 20 so that they do not start losing the advantages of a micro or small enterprise. The other problem with the employment criterion as stated is seasonal nature of Industries. Quoting the example of food processing industry, he added that during peak season, the employment goes up and during lean season, employment may decrease. Additionally, the question of contractual employment also comes up. So the uniformity in employment figures throughout the year becomes a difficulty. Therefore, in his opinion, it is felt that the best way to classify is the turnover criterion and especially with the introduction of GST. It is easy to understand and link it with the turnover, which has been filed in the GST returns. In their written submission also PHD Chamber of Commerce and Industry supported the proposed changes in the criteria of classification of MSMEs and complement the Ministry of MSME, for bringing in a simple criteria which is easy to understand and apply and which will not require any certification of Chartered Accountants or experts to identify the MSMEs. It was also stated that the new criteria will promote ease of doing business as the process of identification and dealings with MSMEs will become simpler and faster.

CLAUSE BY CLAUSE EXAMINATION OF THE BILL

11.1 During the course of the examination of the bill, the Committee took note of the concerns, suggestions, views and opinions expressed by various experts and stakeholders and considered the amendments proposed in the bill clause by clause, which is detailed in the succeeding paragraphs:

Clause 2 (a)

Clause 2(a) reads as under:

In the Micro, Small and Medium Enterprises Development Act, 2006 (hereinafter referred to as the principal Act), in section 7,-

(a) For sub-section (1), the following sub-sections shall be substituted, namely –

"(1) Notwithstanding anything contained in section 11B of the Industries (Development and Regulation) Act, 1951, (65 of 1951) the Central Government may, for the purposes of this Act, by notification and having regard to the provisions of sub-sections (4) and (5), classify any class or classes of enterprises, whether proprietorship, Hindu undivided family, association of persons, co-operative society, partnership firm, company or undertaking, by whatever name called, engaged in the manufacture or production of goods pertaining to any industry specified in the First Schedule to the Industries (Development and Regulation) Act, 1951, or engaged in providing or rendering of services, as-

(i) a micro enterprise, where the annual turnover does not exceed five crore rupees;
(ii) a small enterprise, where the annual turnover is more than five crore rupees but does not exceed Seventy -five crore rupees ;

(iii) a medium enterprise, where the annual turnover is more than seventy-five crore rupees but does not exceed two hundred and fifty crore rupees";

(1A) The Central Government may, by notification, vary turnover limits, which shall not exceed thrice the limits specified in sub-Section (1) for the purposes of development of micro, small and medium enterprises."

11.2 The Committee while taking oral evidence heard the views of the experts on the subject and stakeholders and got the mixed views, while some were for change in the present investment criterion to turnover criterion while some others wanted to continue with the present investment in plant and machinery criterion with a change in the investment limits prescribed for Micro, Small & Medium Enterprises. Few of them also preferred to include the employment criteria in combination with turnover criteria for classification of the MSMEs. Their assertion is that MSMEs being the largest employer next to the agriculture with highest potential of generating large-scale employment in future, the MSME should be classified on the basis of number of employees.

11.3 The M/o MSME while clarifying the query raised by the Members of the Committee as well as stakeholders stated that post GST, there is a need to put in place a non-discretionary, transparent and objective definition of the MSMEs to further promote the ease of doing business. Therefore, turnover criterion would result in an automotive and unambiguous classification of enterprises. There was a need to provide certain flexibility to the Government to modify the definition criteria specified under the MSMED Act to cater to the need of aligning them with the changing business ecosystem. The problems with employment criteria in Indian context is non-availability of reliable/verifiable sectoral data and the seasonal variance in labour engagement. The employment system will also increase the need for inspection as in the case of investment criterion, which will involve huge transaction cost. He apprised the Committee that the turnover criterion will encourage investment in modernization.

11.4 Further, the Committee got the feedback from various stakeholders that due to the ceiling of investments in the definition of Micro, Small and Medium Enterprises, such enterprises have the tendency to keep the investment in plant and machinery restricted, so as to ensure that they continue to get the benefits that accrue to their respective categories. This, in turn, hampers the process of their modernization and also competitiveness, by keeping capital formation industries at a low level. Hence, the turnover-based classification will encourage MSME to reap benefit by moving to a higher category, which is an automotive process linked to the GST Network. As a matter of fact, higher limits of turnover would incentivise the MSMEs, to invest and grow, without worrying about inspections etc.

11.5 During the examination of MSMED (Amendment) Bill, 2018, the Committee has come across different views of experts and stakeholders with regard to re-classification of MSMEs based on their annual turnover instead of the existing investment in plant and machinery/equipment, as well as consideration of employment along with the annual turnover for re-classification of MSMEs.

11.6 The Committee was given to understand by the views expressed by the Ministry of MSME that in case employment is factored along with turnover to make a composite criterion for classification, the major impediment will be the absence of a reliable/verifiable and updated data on employment. Moreover, in India, the manpower engaged in MSMEs has a significant seasonal variance and there is always a possibility of continuous inter-sectoral mobility *i.e.* from agriculture to manufacturing or service sector and *vice-versa* depending on the demands and supply of registered manpower. Inspection and certification of employees engaged would be required as in the case of investment criteria, which will also involve huge transaction cost.

11.7 The Committee notes that the present classification of MSMEs based on investment in plant and machinery is effective since the adoption of the MSMED Act, 2006. Therefore, the extant financial limits fixed in 2006 for MSMEs are no longer relevant given the impact of inflation. Most of the Industry Associations and stakeholders have, therefore, expressed the need for changing the present criteria of investment in plant and machinery to annual turnover as criterion for classification of MSMEs.

11.8 The Committee notes that the present classification based on investment in plant and machinery also has a number of disadvantages as it prevents MSMEs to become competitive in the market, inhibits investment to modernize, upscale, improve productivity and technology upgradation due to rigor of investment thresholds. On the other hand, taking turnover as a criteria shall overcome the said shortcomings as it can be pegged with reliable data available in GST Network and other methods of ascertaining, which will

- **(i) help in having a non discretionary, transparent and objective criteria and will eliminate the need for inspections;**
- **(ii) make the classification system progressive and evolutionary;**
- **(iii) help in overcoming the uncertainties associated with the classification based on investment in plant & machinery/equipment and employment**
- **(iv) improve the ease of doing business; and**
- **(v) provide flexibility to the Government to fine-tune the classification of MSMEs in response to changing economic scenario without resorting to the amendment of MSMED Act.**

11.9 The Committee, however, feels that wide gap in turnover limits i.e. upto Rs. 5 crore for a Micro unit and between Rs. 5 crores and 75 crores for a Small unit is exorbitantly high because a unit with a turnover of Rs. 6 crores and a unit with a turnover of Rs. 75 crores would both be categorized as 'Small' which seems to be incongruous. The Committee accordingly desires that the Ministry may consider this aspect while finalizing the Amendment Bill.

The Committee accordingly adopted the above Clause 2(a) of the Bill, subject to the aforesaid recommendation.

<u>Clause 2 (b)</u>

Clause 2(b) reads as under:

(b)in sub-section (9), -

(i) for the words "criterion of investment", the words "criterion of annual turnover" shall be substituted;

(ii) for the words "as part of small enterprises", the words "as part of small and medium enterprises" shall be substituted.

<u>Clause 3</u>

Clause 3 reads as under:

4. *In section 14 of the principal Act, in sub-section (2), the words, brackets and figure "sub-section (1)of " shall be omitted.*

11.10 As the amendments proposed in clause 2 (b) and clause 3 are only consequential changes in the provisions of the Principal Act, the said clauses does not call for any examination or comments and hence the same are adopted by the Committee.

Section 2 (Definitions) of the MSMED Act, 2006.

11.11 The Committee while examining the Bill observed that the proposed amendment in Section 7 (1) also entails consequent amendment in clause (g), (h) & (m) of Section 2 (definitions) of the MSMED Act, 2006. However, there was no mention in the Amendment Bill for subsequent amendments in the definition under Section 2.

11.12 The Ministry of MSME clarified that the basic objective of changing the Act is in Section 7(1). The changes in definitions under clause (g), (h) & (m) of Section 2 of the MSMED Act, 2006 will be taken up consequently. The Committee further sought clarification on this issue from Legislative Department (M/o Law & Justice) and the Legislative Department was in agreement with the observation made by the Committee and proposed draft Amendment as under:-

In the Micro, Small and Medium Enterprises Development Act, 2006, (hereinafter referred to as the principal Act), in Section 2,-

(i) In clause *(g)*, for the words, brackets, letters and figures "sub-clause *(iii)* of clause *(a)* or sub-clause *(iii)* of clause (b) of sub-section *(1)*", the words, brackets and figures "clause *(iii)* of sub-section *(1)*" shall be substituted;

(ii) In clause *(h)*, for the words, brackets, letters and figures "sub-clause *(i)* of clause *(a)* or sub-clause *(i)* of clause *(b)* of sub-section *(1)*", the words, brackets and figures "clause *(i)* of sub-section *(1)*" shall be substituted;

(iii) In clause *(m)*, for the words, brackets, letters and figures "sub-clause *(ii)* of clause *(a)* or sub-clause *(ii)* of clause *(b)* of sub-section *(1)*", the words, brackets and figures "clause *(ii)* of sub-section *(1)*" shall be substituted.'

11.13 The Committee recommends that as agreed to by both Ministry of MSME and Ministry of Law and Justice, the amendments in clause *(g)*, *(h)* & *(m)* of Section 2 (definition) of the MSMED Act, 2006 be carried out simultaneously to ensure complete consequential amendment.

11.14 Taking into consideration the views of majority of the stakeholders and the arguments put forth by the M/o MSME, the Committee feels that instead of the current classification based on investment in plant & machinery/equipment, the MSMEs could be classified based on their annual turnover as proposed in the Bill.

<u>General Observations/Recommendations</u>

12.1 With the proposed change in the classification of MSMEs, it is more likely that large number of Enterprises would come under the Ministry of MSME. The Committee, therefore, desires that the Ministry may make all-out efforts to obtain increased Budget Allocation for the MSME Sector. It accordingly desires that the Ministry may take up the issue with Ministry of Finance in right earnestness.

12.2 To allay the apprehensions of some of the stakeholders, in view of the proposed change in definition of MSMEs, the Ministry has stated that necessary adjustment to safeguard the interests of MSEs would be done. The Committee notes the flexibility adduced by the Ministry to make necessary course corrections in the policy and schemes for incentives to the MSEs, so that they do not get adversely affected.

12.3 The Committee is of the opinion that there is some weightage in the apprehensions expressed by the stakeholders as the Committee too feels that possibilities do exist for the large corporates or the MNCs to corner the incentives meant for the MSMEs, which has in fact, been explicitly exhibited in the Research Study conducted by the One-Man Committee, wherein the share of finance gap amongst the three sub-groups of MSMEs in itself is exorbitant. The Committee, therefore, desires that the Ministry may put in place suitable policy interventions to avert such situations, which may prove to be catastrophic to the Indian Industry and Economy as a whole. The Committee hopes that scheme-specific measure to safeguard the MSME Sector wherever necessary will be taken up soon after provisions of the Bill are made operational.

12.4 The Committee acknowledges the fact that Micro, Small & Medium Enterprises (MSME) Sector plays a significant role in the growth of Indian Economy. It also provides the 2nd largest employment next to Agriculture Sector. MSME also contribute enormously to the socio-economic well-being and progress of our country. It is therefore, imperative to groom and nurture the MSME sector.

12.5 The Committee is unable to fathom the argument adduced by the Ministry that in the case of employment criteria in the Indian context, there is non-availability of reliable data and that there is problem of seasonal variance in labour engagement. The Committee feels that in a labour-intensive country like India, appropriate focus is required to be concentrated on employment generation and the best and most accurate platform for this is the MSME Sector, which provides the greatest employment opportunities, next only to the Agricultural Sector. Therefore, the Committee recommends that the Government should take up the exercise to assess the number of persons employed in MSME Sector and consider employment too as a criteria while classifying MSMEs.

12.6 The Committee notes that the turnover as on 01st April of a particular financial year will be taken as the turnover of that enterprise for the whole financial year. The turnover of some enterprises may fluctuate depending on their business, which may result in the change of the classification of the enterprise. The Committee recommends that in order to address the issue, scheme-specific safeguards should be adopted by the Ministry so that large enterprises do not grab the benefits meant for MSEs.

12.7 The Committee feels that with the adoption of new criteria, large number of Micro Enterprises will benefit from various Government schemes. Moreover, complicated calculations for paperwork and requirement of certification by CAs or experts would be settled once for all.

12.8 During the examination of MSMED (Amendment) Bill, 2018, the Committee has come across different views of experts and stakeholders with regard to re-classification of MSMEs based on their annual turnover instead of the existing investment in plant and machinery/equipment, as well as consideration of employment along with the annual turnover for re-classification of MSMEs.

12.9 However, the Committee feels that the definition/classification based on employment criteria may not help MSMEs to generate more employment as it appears only an enabling provision and not an instrument in itself to create more employment. The proposed new criterion based on Turnover will encompass all enterprises with turn over upto Rs. 250 crore.

RECOMMENDATIONS/OBSERVATIONS AT A GLANCE

1. The Committee notes that the present classification of MSMEs based on investment in plant and machinery is effective since the adoption of the MSMED Act, 2006. Therefore, the extant financial limits fixed in 2006 for MSMEs are no longer relevant given the impact of inflation. Most of the Industry Associations and stakeholders have, therefore, expressed the need for changing the present criteria of investment in plant and machinery to annual turnover as criterion for classification of MSMEs.

(Para 11.7)

2. The Committee notes that the present classification based on investment in plant and machinery also has a number of disadvantages as it prevents MSMEs to become competitive in the market, inhibits investment to modernize, upscale, improve productivity and technology upgradation due to rigor of investment thresholds. On the other hand, taking turnover as a criteria shall overcome the said shortcomings as it can be pegged with reliable data available in GST Network and other methods of ascertaining, which will

(i) help in having a non discretionary, transparent and objective criteria and will eliminate the need for inspections;

(ii) make the classification system progressive and evolutionary;

(iii) help in overcoming the uncertainties associated with the classification based on investment in plant & machinery/equipment and employment

(iv) improve the ease of doing business; and

(v) provide flexibility to the Government to fine-tune the classification of MSMEs in response to changing economic scenario without resorting to the amendment of MSMED Act.

(Para 11.8)

3. The Committee, however, feels that wide gap in turnover limits i.e. upto Rs. 5 crore for a Micro unit and between Rs. 5 crores and 75 crores for a Small unit is exorbitantly high because a unit with a turnover of Rs. 6 crores and a unit with a turnover of Rs. 75 crores would both be categorized as 'Small' which seems to be incongruous. The Committee accordingly desires that the Ministry may consider this aspect while finalizing the Amendment Bill. The Committee accordingly adopted the above Clause 2(a) of the Bill, subject to the aforesaid recommendation.

(Para 11.9)

4. As the amendments proposed in clause 2 (b) and clause 3 are only consequential changes in the provisions of the Principal Act, the said clauses does not call for any examination or comments and hence the same are adopted by the Committee.

(Para 11.10)

5. The Committee recommends that as agreed to by both Ministry of MSME and Ministry of Law and Justice, the amendments in clause *(g)*, *(h)* & *(m)* of section 2 (definition) of the MSMED Act, 2006 be carried out simultaneously to ensure complete consequential amendment.

(Para 11.13)

6. Taking into consideration the views of majority of the stakeholders and the arguments put forth by the M/o MSME, the Committee feels that instead of the current classification based on investment in plant & machinery/equipment, the MSMEs could be classified based on their annual turnover as proposed in the Bill.

(Para 11.14)

7. With the proposed change in the classification of MSMEs, it is more likely that large number of Enterprises would come under the Ministry of MSME. The Committee, therefore, desires that the Ministry may make all-out efforts to obtain increased Budget Allocation for the MSME Sector. It accordingly desires that the Ministry may take up the issue with Ministry of Finance in right earnestness.

(Para 12.1)

8. To allay the apprehensions of some of the stakeholders, in view of the proposed change in definition of MSMEs, the Ministry has stated that necessary adjustment to safeguard the interests of MSEs would be done. The Committee notes the flexibility adduced by the Ministry to make necessary course corrections in the policy and schemes for incentives to the MSEs, so that they do not get adversely affected.

(Para 12.2)

9. The Committee is of the opinion that there is some weightage in the apprehensions expressed by the stakeholders as the Committee too feels that possibilities do exist for the large corporates or the MNCs to corner the incentives meant for the MSMEs, which has in fact, been explicitly exhibited in the Research Study conducted by the One-Man Committee, wherein the share of finance gap amongst the three sub-groups of MSMEs in itself is exorbitant. The Committee, therefore, desires that the Ministry may put in place suitable policy interventions to avert such situations, which may prove to be catastrophic to the Indian Industry and Economy as a whole. The Committee hopes that scheme-specific measure to safeguard the MSME Sector wherever necessary will be taken up soon after provisions of the Bill are made operational.

(Para 12.3)

10. The Committee acknowledges the fact that Micro, Small & Medium Enterprises (MSME) Sector plays a significant role in the growth of Indian Economy. It also provides the 2nd largest employment next to Agriculture Sector. MSME also contribute enormously to the socio-economic well-being and progress of our country. It is therefore, imperative to groom and nurture the MSME sector.

(Para 12.4)

11. The Committee is unable to fathom the argument adduced by the Ministry that in the case of employment criteria in the Indian context, there is non-availability of reliable data and that there is problem of seasonal variance in labour engagement. The Committee feels that in a labour-intensive country like India, appropriate focus is required to be concentrated on employment generation and the best and most accurate platform for this is the MSME Sector, which provides the greatest employment opportunities, next only to the Agricultural Sector. Therefore, the Committee recommends that the Government should take up the exercise to assess the number of persons employed in MSME Sector and consider employment too as a criteria while classifying MSMEs

(Para 12.5)

12. The Committee notes that the turnover as on 01st April of a particular financial year will be taken as the turnover of that enterprise for the whole financial year. The turnover of some enterprises may fluctuate depending on their business, which may result in the change of the classification of the enterprise. The Committee, therefore, recommends that in order to address the issue, scheme-specific safeguards should be adopted by the Ministry so that large enterprises do not grab the benefits meant for MSEs.

(Para 12.6)

13. The Committee feels that with the adoption of new criteria, large number of Micro Enterprises will benefit from various Government schemes. Moreover, complicated calculations for paperwork and requirement of certification by CAs or experts would be settled once for all.

(Para 12.7)

14. During the examination of MSMED (Amendment) Bill, 2018, the Committee has come across different views of experts and stakeholders with regard to re-classification of MSMEs based on their annual turnover instead of the existing investment in plant and machinery/equipment, as well as consideration of employment along with the annual turnover for re-classification of MSMEs.

(Para 12.8)

15. However, the Committee feels that the definition/classification based on employment criteria may not help MSMEs to generate more employment as it appears only an enabling provision and not an instrument in itself to create more employment. The proposed new criteria based on Turnover will encompass all enterprises with turn over upto Rs. 250 crore.

(Para 12.9)

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ANNEXURE-I

AS INTRODUCED IN LOK SABHA

Bill No. 102 of 2018

THE MICRO, SMALL AND MEDIUM ENTERPRISES DEVELOPMENT (AMENDMENT) BILL, 2018

A

BILL

to amend the Micro, Small and Medium Enterprises Development Act, 2006.

BE it enacted by Parliament in the Sixty-ninth Year of the Republic of India as follows:—

Short title and commencement.

1. (*1*) This Act may be called the Micro, Small and Medium Enterprises Development (Amendment) Act, 2018.

(*2*) It shall come into force on such date as the Central Government may by notification in the Official Gazette, appoint.

Amendment of section 7.

27 of 2006.

2. In the Micro, Small and Medium Enterprises Development Act, 2006 (hereinafter referred to as the principal Act), in section 7,—

(a) for sub-section (*1*), the following sub-sections shall be substituted, namely:—

65 of 1951.

"(*1*) Notwithstanding anything contained in section 11B of the Industries (Development and Regulation) Act, 1951, the Central Government may, for the purposes of this Act, by notification and having regard to the provisions of sub-sections (*4*) and (*5*), classify any class or classes of enterprises, whether proprietorship, Hindu undivided family, association of persons, co-operative society, partnership firm, company or undertaking, by whatever name called, engaged in the manufacture or production of goods pertaining to any industry specified in the First Schedule to the Industries (Development and Regulation) Act, 1951, or engaged in providing or rendering of services, as—

(i) a micro enterprise, where the annual turnover does not exceed five crore rupees;

(ii) a small enterprise, where the annual turnover is more than five crore rupees but does not exceed seventy-five crore rupees;

(iii) a medium enterprise, where the annual turnover is more than seventy-five crore rupees but does not exceed two hundred and fifty crore rupees.

(*1A*) The Central Government may, by notification, vary the turnover limits, which shall not exceed thrice the limits, specified in sub-section (*1*) for the purposes of development of micro, small and medium enterprises.";

(b) in sub-section (*9*),—

(i) for the words "criterion of investment", the words "criterion of annual turnover" shall be substituted;

(ii) for the words "as part of small enterprises", the words "as part of small and medium enterprises" shall be substituted.

Amendment of section 14.

3. In section 14 of the principal Act, in sub-section *(2)*, the words, brackets and figure "sub-section (*1*) of " shall be omitted.

STATEMENT OF OBJECTS AND REASONS

The Micro, Small and Medium Enterprises Development Act, 2006 (the said Act) was enacted to provide for facilitating the promotion and development and enhancing the competitiveness of micro, small and medium enterprises. The said Act, *inter alia*, provides for classification of the enterprises as micro, small or medium based on their investment in plant and machinery or equipment. Over a period of time, it has been felt necessary to change the criteria for the classification in order to align it with the need of current times and changing business ecosystem.

2. In the course of consultation with various stakeholders, it has been noted that the criterion of investment in plant and machinery or equipment entails physical verification having associated transaction costs. It also incentivises the tendency in the promoters of the enterprises to keep the investment size small in a particular business entity in order to retain the benefits associated with micro or small enterprises category. While evaluating various alternatives, it has been considered appropriate that if the annual turnover is taken as a criterion for classification, the information available with goods and services tax network and other sources can be used for determination of the category of the enterprises. Overall, the turnover based clasification will promote the ease of doing business and will put in place a non-discretionary, transparent and objective classification system.

3. In view of the above, it is proposed to amend section 7 of the Micro, Small and Medium Enterprises Development Act, 2006 to—

(a) provide for change in the criterion of classification of micro, small and medium enterprises from the existing criterion of investment in plant and machinery or equipment to a new criterion based on annual turnover of the enterprises; and

(b) confer power upon the Central Government to vary, the turnover limits, by notification which shall not exceed thrice the limits specified in sub-section (*1*) of section 7 for the purpose of development of micro, small and medium enterprises.

4. The Bill seeks to achieve the above objects.

NEW DELHI;
The 22*nd* *March*, 2018.

GIRIRAJ SINGH

MEMORANDUM REGARDING DELEGATED LEGISLATION

Sub-clause (*a*) of clause 2 of the Bill seeks to insert sub-section (*1A*) in section 7 of the Micro, Small and Medium Enterprises Development Act, 2006, so as to confer power upon the Central Government to vary the turnover limits relating to the classification of micro, small and medium enterprises by way of notification.

2. The matters in respect of which the notification may be issued under the proposed legislation are matters of procedure or administrative details and it is not practicable to provide for them in the Bill itself. The delegation of legislative power is, therefore, of a normal character.

ANNEXURE

EXTRACTS FROM THE MICRO, SMALL AND MEDIUM ENTERPRISES DEVELOPMENT ACT, 2006 (27 OF 2006)

*   *   *   *   *

CHAPTER III

CLASSIFICATION OF ENTERPRISES, ADVISORY COMMITTEE AND MEMORANDUM OF MICRO, SMALL AND MEDIUM ENTERPRISES

Classification of enterprises.

65 of 1951.

7. (*1*) Notwithstanding anything contained in section 11B of the Industries (Development and Regulation) Act, 1951, the Central Government may, for the purposes of this Act, by notification and having regard to the provisions of sub-sections (*4*) and (*5*), classify any class or classes of enterprises, whether proprietorship, Hindu undivided family, association of persons, co-operative society, partnership firm, company or undertaking, by whatever name called,—

65 of 1951.

(a) in the case of the enterprises engaged in the manufacture or production of goods pertaining to any industry specified in the First Schedule to the Industries (Development and Regulation) Act, 1951, as—

(i) a micro enterprise, where the investment in plant and machinery does not exceed twenty-five lakh rupees;

(ii) a small enterprise, where the investment in plant and machinery is more than twenty-five lakh rupees but does not exceed five crore rupees; or

(iii) a medium enterprise, where the investment in plant and machinery is more than five crore rupees but does not exceed ten crore rupees;

(b) in the case of the enterprises engaged in providing or rendering of services, as—

(i) a micro enterprise, where the investment in equipment does not exceed ten lakh rupees;

(ii) a small enterprise, where the investment in equipment is more than ten lakh rupees but does not exceed two crore rupees; or

(iii) a medium enterprise, where the investment in equipment is more than two crore rupees but does not exceed five crore rupees.

Explanation 1.—For the removal of doubts, it is hereby clarified that in calculating the investment in plant and machinery, the cost of pollution control, research and development, industrial safety devices and such other items as may be specified, by notification, shall be excluded.

65 of 1951.

Explanation 2.—It is clarified that the provisions of section 29B of the Industries (Development and Regulation) Act, 1951, shall be applicable to the enterprises specified in sub-clauses (*i*) and (*ii*) of clause (*a*) of sub-section (*1*) of this section.

*   *   *   *   *

65 of 1951.
61 of 1956.

(*9*) Notwithstanding anything contained in section 11B of the Industries (Development and Regulation) Act, 1951 and clause (*h*) of section 2 of the Khadi and Village Industries Commission Act, 1956, the Central Government may, while classifying any class or classes of enterprises under sub-section (*1*), vary, from time to time, the criterion of investment and also consider criteria or standards in respect of employment or turnover of the enterprises and include in such classification the micro or tiny enterprises or the village enterprises, as part of small enterprises.

* * * * *

Administration and utilisation of Fund or Funds.

14. (*1*) * * * * *

(*2*) The Fund or Funds shall be utilised exclusively for the measures specified in sub-section (*1*) of section 9.

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Bill No. 36 of 2018

36

LOK SABHA

———

A

BILL

to amend the Micro, Small and Medium Enterprises Development Act, 2006.

———

(*Shri Giriraj Singh, Minister of State for Micro, Small and Medium Enterprises*)

MGIPMRND—5190LS(S3)—28.03.2018.

Annexure-II

LIST OF WITNESSES

1. EXPERTS

(i) Dr. H.P. Kumar, Ex-CMD, NSIC & Advisor from PHD Chamber of Commerce & Industry

(ii) Dr. Prabhat Kumar, Ex-Cabinet Secretary & Ex-Governor Jharkhand.

2. STAKEHOLDERS/REPRESENTATIVES

Chamber of Indian Micro, Small and Medium Enterprises (CIMSME)

(i) Shri S. K. Gagroo from

Laghu Udyog Bharati

(ii) Shri Jitendra Gupta, National President

(iii) Shri Govind Lele, National General Secretary

Coimbatore District Small Industries Association (CODISSIA)

(iv) Shri Ramamurthy Ranganathan, President

(v) Shri Ramesh Babu MV, Vice-President

Confederation of Women Entrepreneurs (COWE)

(vi) Ms. Meenu Maggon

(vii) Ms. Payal Agarwal

(viii) Ms. Ruchi Rastogi