IMPACT OF GST ON MICRO, SMALL AND MEDIUM ENTERPRISES

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ABSTRACT: For a developing country like India and its demographic diversity, SMEs have emerged as the leading employment-generating sector and has provided balanced development across sectors. Let’s examine what would be the impact of GST on Small & Medium Enterprises. The true extent of the ‘One Market’ benefit of GST will be realized most by SMEs. Under the current tax regime, the ability of SMEs to reach potential consumers across India is limited.

With the passage of the uniform Goods and Services Tax in the Rajya Sabha, the Small and Medium Enterprises (SME) in the country are caught in a state of flux. The general perception is that GST may negatively impact SMEs as aspects like excise exemption will disappear when GST rolls out. The Government's intention behind GST is to expand the taxpayers’ base and not to enhance tax burden on business/individual tax payers. This study is relating to positive and negative impact of GST on MSME Sector.

Introduction:
Small and Medium Enterprises (SMEs) have been considered as the primary growth driver of the Indian economy for decades. It is further evident from the fact that today we have around 3 million SMEs in India contributing almost 50% of the industrial output and 42% of India’s total export. For a developing country like India and its demographic diversity, SMEs have emerged as the leading employment-generating sector and has provided balanced development across sectors. Let’s examine what would be the impact of GST on Small & Medium Enterprises. After the passage of the Goods and Services Tax (GST) Bill, the Industry is hailing the government for bringing up this reform which has been long pending because of political deadlocks.

But before we analyze the impact of GST on Small & Medium Enterprises, we should understand how GST is going to widen the taxpayer base. Earlier, any manufacturer with a turnover of Rs 1.5 crore or less was not required to comply to the rules of excise duty. However, with the merging of all State and Central level taxes into the ambit of GST, any manufacturer with a turnover of Rs 20 lakh (others) /10Lakh (Special category states) or more will have to comply with GST and its procedures.

All the compliance procedures under GST — Registration, Payments, Refunds and Returns will now be carried out through online portals only and thus SMEs need not worry about interacting with department officers for carrying out these compliances, which are considered as a headache in the current tax regime.
Every major reform is faced with certain hurdles, and arguments from various stakeholders. However, from an SME perspective, GST will bring in many positives compared to the current systems such as easy process of availing input credit, single point tax, elimination of cascading tax system, and simpler taxation. These pros offset the negatives. While hopes rest with GST to boost the GDP growth and reduce the fiscal deficit. The extent of such impact will depend on a favorable consensus on GST rates for all business segments and integrated implementation of the same.

**Positive Impact of GST:**

**Starting business becomes easier:** Currently, the Sales Tax department has various turnover slabs which require VAT registration. A business with multi-state operation in this case has to follow varied tax rules applicable to different states. This not only creates excess complication but also adds to procedural fees, due to which the price sensitive MSMEs will be burdened. Uniform GST will standardize the process.

**Improved MSME market expansion:**

In the current system, big corporations procured goods based on MSME’s locality in order to reduce overheads. Thus MSMEs limit their customers within state as they wi” bear the ultimate burden of tax on interstate sales, reducing their customer base. With implementation of GST, this will be nullified as tax credit will transfer irrespective of location of buyer and seller. This allows MSME segment to expand their reach across borders.

**Lower logistical overheads:**

As GST is tax neutral it will eliminate time consuming border tax procedures and toll check posts and encourage supply of goods across borders. Accordingly the logistical cost for companies manufacturing bulk good will be reduced. Such costs can be crucial for the survival of MSMEs.

**Aids MSMEs dealing in sales and services:**

GST will not distinguish between sales and services. This is good news for the MSMEs that deal with sales and services model of business, for them the taxation is simplified and will be calculated on total.

**Unified market:**

GST will allow flexibility in transfer of goods across states and reduce the cost of doing business, as the reform will cut down multiple taxes imposed by state and central government.

**Purchase of Capital Goods:**

In the current system, only 50% of the input tax credit against purchase of Capital Goods is available in the year of purchase and the balance amount in subsequent years. Under GST regime, entire amount of input tax credit can be availed in the year of purchase itself. This will support "Make in India" campaign.

**Reduction of tax burden on new business:**

As per the current tax structure, businesses with a turnover of more than rupees 5 lakh need to pay a VAT registration fee. The government mulls the exemption limit under GST to twenty five lakh giving relief to over 60% of small dealers and traders.

**Improved logistics and faster delivery of services:**

Under the GST bill, no entry tax will be charged for goods manufactured or sold in any part of India. As a result, delivery of goods at interstate points and toll check posts will be expedited. According to an estimate by CRISIL, the logistics cost for manufacturers of
bulk goods will get reduced significantly—by about 20%. This is expected to boost ecommerce across the nation.

**Elimination of distinction between goods and services:**

GST ensures that there is no ambiguity between goods and services. This will simplify various legal proceedings related to the packaged products. As a result, there will no longer be a distinction between the material and the service component, which will greatly reduce tax evasion.

**Negative Impact of GST**

**The burden of lower threshold:**

The GST bill proposes a reduction in threshold to be Rs. 9 lakh to increase the tax net, Rs. 41 lakh for North Eastern states. (However, GST council has increased the threshold limit from 10 lakh to 20 lakh and from 41 lakh to 10 lakh for North eastern states) Under the reform, any service provider or retailer will be subject to tax levy. In the current central excise law threshold is Rs. 1.5 crore. This reduction will significantly impact the MSMEs’ working capital. For example, a manufacturer who trades today at Rs. 25 lakhs without any tax levy will be expected to pay GST post implementation. As the threshold is low, most MSMEs are now exempted and will have to pay a chunk of their capital towards tax in future.

**No tax differentiation for luxury items and services:**

The tax neutrality will not differentiate luxury goods and normal goods. Currently the state and central government levy higher taxes on luxury goods and services. Under GST implementation, all goods and services will have to pay the same tax which will lead to rich becoming richer and poor becoming poorer. It is not an ideal situation for MSMEs competing against large businesses.

**Selective tax levying:**

GST will not be applicable to Alcoholic liquor for human consumption and Petroleum based businesses, which creates further gap and does not support the unified market ideology of GST.

**The burden of higher tax rate for Service Provider:**

Presently Service Tax rate is 15%. GST rate will be around 18%. The scenario in the service sector will further be impacted as the concept of Centralised Registration has been done away with and each unit in different states will have to take separate registration. Thus even if services are supplied by company’s one Unit in State A to another Unit in State B, then also taxes will be payable.

**Excess Working Capital Requirement** –

Taxation of stock transfer will primarily impact the working capital requirements. The quantum of impact will vary depending on stock turnaround time at warehouse, credit cycle to customer, quantum of stock transfer, etc. Higher amount of Capital Requirement Jill increase interest cost which ultimately will increase the price of Finished Goods.

**Realignment of Purchase and Supply Chain** –

Under GST credit will be not be available to a compliant company if the vendor from whom MSME is purchasing goods does not show the same in his return. Thus sourcing strategies will change on account of GST credit mechanism. Also there will be re-consideration of Supply Chain on account of taxation of Stock Transfers.

**Challenges for SMEs**
A size able portion of SMEs are of the opinion that GST is not all good for the sector and their fears may not be totally vacuous. The tax neutrality that the SMEs enjoy may be one of the prominent benefits. However, reduction in duty threshold is one of the key concerns that has led them to be wary of the GST bill. Under the existing excise tax, no duty is paid by a manufacturer having a turnover of less than rupees 1.50 crores. But, post GST implementation, the exemption limit will get significantly lowered. During a speech at a news conference, Finance Minister, Arun Jaitley estimate said, the limit can be as low as rupees 25 lakh. As a result, a large number of SMEs and startups will be mandated to come under the tax net and will have to pay a large chunk of their earnings towards tax. Furthermore, there are other flip-sides to the proposed tax neutrality. GST regime won’t differentiate between luxury goods and normal goods; these will it hard for the SMEs to compete against large enterprises. GST that is ultimately levied on supply will not be available for input credit. This will lead to an increase in the cost of the products for businesses that supply directly to end users.

Conclusion:
Goods and Service Tax (GST) likely to be beneficial for auto cement and organised retail sectors, but will have a negative impact on oil and gas, and SME sectors. However, the impact would be broadly neutral for property, electricity, telecom, pharmaceutical and fertilizer sectors.

SMEs will have to opt for electronic compliance system, starting from registering to filing online returns. This will primarily cause teething problems and will also increase the cost of compliance. GST would improve demand and competitiveness of ‘Made in India’ products. It is most likely that the burden of indirect tax will reduce both for the producer of goods and the ultimate end user except in some cases, as the producer or manufacturer of goods will get the advantage of input tax credits (ITC) and the consumer will have to bear only the indirect tax charged by the last retailer or dealer in the supply chain. Under the Goods and Service Tax system, self-supplies or interstate stock transfer will fall under the scanner of GST.

This will have a certain impact on the working capital requirements resulting in higher interest cost and eventually impact pricing policies.

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