Implications of Mandatory EPF And ESI Registration For Startups & MSMEs

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EPF & ESI Mandatory For Startups & MSMEs

Increased commercial activity is what promotes a country's growth and development and one of the most common ways to increase such activity is to incorporate a company. A corporation not only has a distinct identity from its members, limiting their liability, it also has perpetual succession, allowing it to own or sell property as well as bring or receive legal action on its own.

The Ministry of Corporate Affairs ["MCA"] announced the introduction of a new web form called Simplified Proforma for Incorporating Company Electronically Plus: INC-32 ["SPICe+"] to replace the current SPICe form. SPICe+ would offer 11 services to those looking to start a business in India through three central government ministries i.e., MCA, Ministry of Labor, and the Department of Revenue in the Ministry of Finance along with three State Governments i.e., Maharashtra, Karnataka, and West Bengal.

All new companies would be incorporated using the SPICe+ form. The MCA's action is part of the central government's 'Ease of Doing Business' initiative. The MCA issued the Companies (Incorporation) Amendment Rules, 2020, which took effect on February 23rd 2020 to include the aforementioned changes. With the implementation of SPICe+, registrations for Employees' Provident Fund ["EPF"] and Employees' State Insurance ["ESIC"] will no longer be issued separately by the various agencies and will be compulsory for all newly incorporated businesses. While obtaining a Goods & Services Tax Identification Number ["GSTIN"] is optional, registering with the EPF, ESIC, and profession tax (currently applicable in Maharashtra), along with opening a bank account, are all mandatory when forming a new company.

When the authorized capital of the company is up to INR 10,000,000 and the number of members is up to 20 in the case of a company without share capital, the integration of major incorporation procedures in the form of SPICe+ and submission of the same along with the required fee does not require payment. The processing and reservation of company names now takes significantly less time, with nearly 90% of applications approved within a single business day.

Further on, this will have a major impact on startups and micro, small and medium enterprises regarding ESI and EPF Schemes. Major developments expected to impact companies and employees are as follows:

- Medical & Sickness Benefits
- Maternity Benefits
- Easy Registration
- Death & Disablement Benefits
- Unemployment Allowances
- Taxation Effect
- Increased Compliance

I. Medical and Sickness Benefits

From the moment they begin insurable employment, all ESIC-registered individuals and their dependents receive full medical care. There is no spending limit for an insured person or a member of their family’s treatment. For a nominal annual premium of INR 120, retired and permanently disabled insureds, as well as their spouses, receive medical care.

II. Maternity Benefits

Maternity benefits are provided under the ESIC scheme in the form of 100% of the average daily wage in cash for up to 26 weeks in the case of confinement and 6 weeks in the case of miscarriage.

III. Ease of Registration

The government has accelerated company incorporation by drastically reducing the required time and cost with the help of automated processes and an efficient management system. As a result, there is more speed, transparency, uniformity, and less discretion.

IV. Death & Disablement Benefits

In the event of an employee’s death due to an occupational injury, ESIC benefits provide monthly payments to dependents. If there is a temporary disability, the ESIC will pay a monthly payment until the injury heals. The ESIC provides a lifetime payment in the event of permanent disability.

V. Unemployment Allowance

The ESIC scheme provides benefits such as unemployment benefits and monthly cash stipends for a maximum of 24 months in the event of an unintentional loss of employment or permanent invalidity caused by a non-employment injury.

VI. Taxation

Start-ups can benefit via more tax breaks than larger companies that are registered differently, such as gaining a 3-year tax holiday if recognized as a startup under Startup India Scheme, garnering the benefit of offsetting initial losses with future profits, and a corporate tax rate of 25% (plus cess) on turnover up to two crores, compared to the 30% rate for non-startup entities. This can be a huge help to business owners who struggle with funding in the early days of companies.

VII. Increased Compliance

Although the new form offering is likely to help businesses save time and money when incorporated, the mandatory registration for EPF and ESIC may impede businesses with fewer than 20 or 10 employees. The ESI scheme is for businesses with 10 or more employees, whereas the EPF scheme is for businesses with 20 or more employees. However, many startups and small businesses start with fewer than 10 employees. Furthermore, mandatory registration may compel businesses to implement all compliance measures, increasing the compliance burden.

Implications

SPICe+ has certainly reduced the cost and time associated with incorporation by performing it through a single-window application. Employees will benefit greatly from mandatory EPF and ESCI registrations. However, changes enabled by SPICe+ may make compliance regulations more difficult for startups, microbusinesses, and small businesses. The mandatory registration and compliance requirements of the EPF Act and the ESI Act may make it more difficult for startups to adhere to regulations even though failure to do so may result in fines under the respective Acts.

Furthermore, these developments would increase financial burden on businesses. Interestingly, this registration is not required if the company is founded in a region designated by ESIC as a “non-implemented area.” However, the company is not required to comply with the EPF and ESIC provisions until it exceeds the threshold amounts specified in the EPF and ESIC provisions.