

**Timely Payments to
Micro & Small Enterprises (MSEs)
Sec- 43B(h) of the
Income Tax Act**

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Relevant Provisions

Income Tax Act, 1961	Sec 43B(h)
MSMED Act, 2006	Sec 2(h), 2(m), 2(n), Sec 7(1), Sec 8(1), Sec 15, Sec 16 and Sec 23
Notifications/OM	MSME Notifications – S.O.2119(E), S.O.4926(E) – OM(office memorandum) dated 26.08.2008, 2/7/2021 & 1/9/21
Indian Contract Act, 1872	Sections 59, 60 and 61

Sec 43B(h) of IT Act

Notwithstanding anything contained in any other provisions of **this act**, a **deduction otherwise allowable** under this act in respect of '**Any sum payable** - to **a micro or small enterprises** – beyond the time limit specified in Sec 15 of MEMED Act, 2006, **shall be allowed** (irrespective of year of incurrence according to the method of accounting) **ONLY** in the **PY**, in which it **WAS ACTUALLY PAID** in computing income u/s 28 – Proviso – nothing contained in this section (except (h) shall apply which is actually paid on or before due date ... u/s 139(1) Expln.4 (e)/(g) - "**micro enterprise/small enterprise**" shall have the meaning as assigned to then in clause 2(h)/2(m) of MEMED Act - **Effective from 01/04/2024**

Sec 2(h)

Micro enterprise means an enterprise classified as such u/s 7(1) (a)(i)/(b)(i);

Sec 2(m)	Small enterprises mean an enterprise classified as such u/s 7(1) (a)(ii)/(b)(ii);
Sec 2(n)	Supplier means a micro or small enterprise, which has filed a memorandum - Sec 8(1) and includes NSIC, SIDCO of States/UT and a company/co-op society/trust/body..... Registered under any law for the time being;
Sec 7(1)	Micro: Investment in Plant & Machinery or Equipments doesn't exceed Rs.1 Cr and Turnover does not exceed Rs. 5 Cr Small: Investment in Plant & Machinery or Equipments doesn't exceed Rs.10 Cr and Turnover does not exceed Rs. 50 Cr; - As per Notification S.O.2119(E) dated 26.06.2020 as amended by S.O.4926(E) dated 18.10.2022.

Sec 8(1)	Any person, who intends to establish micro, small & medium enterprises engaged in service, may file while medium enterprise in manufacturing shall file memorandum for registration with the authority;
Sec 15	Where any supplier, supplies good/services, the buyer shall make payment on or before agreed date /if no agreement before the appointed date – Proviso – agreed date shall not exceed 45 days from the date of acceptance;
Sec 2(b)	Appointed Date means the day following immediately after expiry of 15 days from the date of acceptance or the day of deemed acceptance;

	<p>Explanation: (1) Day of acceptance means day of actual delivery of goods/rendering of service OR the Day, on which the objection (<i>if objected in writing within 15 days by the buyer</i>) is removed by the supplier – WHICHEVER IS LATER; (2) Day of deemed acceptance means date of actual delivery of goods/rendering of service where no objections is made w/l 15 days by the buyer;</p>
Sec 16	<p>Where any buyer fails to make payment to the supplier as per Sec 15, he is liable to pay compound interest with monthly rests at three times the rate notified by RBI, notwithstanding anything in agreement between buyer and supplier or in any law;</p>
Sec 23	<p>Notwithstanding anything in IT Act, 1961, the interest payable/paid shall not be allowed as deduction for the computation of income under IT Act;</p>

Background/Ratioale:

- **To promote timely payments to the MSME;**
- **Provisions of MEMED Act found to be inadequate and didn't address adequately the issues of delayed payments;**
- **Fear of losing business by suppliers when interest is claimed against delayed payment from buyers;**

Highlights

- 1. It applies to the transactions from 01/04/2023 onwards (not earlier);**
- 2. It applies only to MICRO & SMALL enterprises (Not Medium enterprises);**
- 3. It applies to dues outstanding as on 31st Mar every year – which needs to be checked whether they have been paid on or before due date as per Sec 15 of MEMED, Act;**

Application of
these provisions
practically

Q 1:

Does it apply to unregistered enterprises?

This applies only to the registered micro and small enterprises. Sec 15 talks about supplier and the word “supplier” is defined u/s 2(n) – Supplier means a micro or small enterprises, which has filed a memorandum with the authority as per Sec 8(1). Hence MSEs registered under Udyam alone will be covered. ***As per decision of SC (Gujarat State Civil Supplies Corporation Ltd. Vs Mahakali Floods Pvt. Ltd. & Anr. (2022) only registered MSMEs can claim the benefits of the act.***

Q 2:

Does it apply to the supplies made prior to the date of registration under MSME?

The registration under MSME is only prospective. Sec 43B(h) will not apply to the purchases made prior to the date registration or outstandings as on the date of registration.

SC - Silpi Industries V Kerala State Road Transport Corporation.

Q 3:

Does it apply to the sum payable to retail traders or wholesalers?

As per OM (No.5/2(2)/2020/E/P&G/POLICY dated 2/7/2021), retail traders/wholesalers are allowed to be registered under MSME only for the limited benefits of Priority Sector Lending and other benefits including provisions of delayed payments are excluded. Hence, they cannot be treated a supplier u/s 15.

Moreover, only manufacturers/service providers are referred in various places of provisions of MSMED Act except Sec 2(n), which includes certain type of traders as well.

Sec 2(e) Enterprises means an industrial undertaking/business concern/establishment engaged in either manufacture or providing/rendering services;

Sec 7(1) – Classification – enterprises engaged in the manufacture/production of goods or in providing/rendering of service;

Q 4:

Does it apply in respect of the amounts due towards purchase of capital good (Capex)?

Sec 43B(h) doesn't distinguish between capital and revenue expenses but it applies to any sum payable in respect of which a deduction is otherwise allowable under this act; It applies to amounts payable to MSEs for purchase of capital goods for which 100 % deduction is admissible under this Act. Ex. Sec 35 (Exp on Scientific research), Sec 35AD.

Q 5:

Can depreciation be disallowed if payment for purchase of fixed assets is delayed beyond time limit as per Sec 15?

Depreciation cannot be disallowed u/s 43B(h) as it is not a sum payable in respect of which deduction is otherwise allowable under this act.

Q 6:

What about delay in payments during the year but paid before end of the financial year, i.e. 31st Mar?

Ex. Op Bal	12,00,000/-
Purchases	18,00,000/- (paid with delay)
Payments	30,00,000/-
Clo Bal	-

The delayed payments during the year may escape the disallowance but will lead to the payment of interest u/s 16, which is currently around 20.25 % (three times the rate notified by RBI) and again disallowable u/s 23.

Q 7:

What about the outstanding dues at the year end but they were paid before the time limit as per Sec 15 of MSMED?

Ex. Op Bal	Nil
Purchase on 20/03/2024	60,000/-
Paid before 31/03/204	30,000/-
Bal as on 31/03/2024	30,000/- (paid on 02/04/24)

As the payments are made as per Sec 15 (though paid in the next year but before the due date as per Sec 15), they are still allowable in the year of incurrence.

Q 8:

What is the date of payment when the payment is made by cheque before the due date as per Sec 15 but the same is encashed later (after the due date)?

Ex. Service availed on 20/03/2024 for Rs. 50,000/-

Paid by cheque on 31/03/2024

Cheque encashed on 07/04/2024

In the normal commercial course of trade, if the payment is made by cheque and the same is honored, the date of payment shall be the date, on which the cheque is handed over. Supreme Court has upheld this in case of CIT Bombay Vs Ogale Glass Works Ltd.

Q 9:

What about o/s as on 31st Mar 2023 (op bal. as on 1st April 2023) - do they need to be paid to avoid disallowance?

Ex. Op Bal Rs. 1,20,000/-

CY Nil

Clo Bal Rs. 1,20,000/-

The disallowance u/s 43B(h) is applicable w.e.f. AY 24-25. Hence it will apply to only the purchases from MSEs on or after 1st April 2023 not prior to that.

Q 10:

Will the GST component in the dues attract Sec 43B(h) disallowance?

It is restricted to the net of GST only as the GST is claimed as ITC in the books. However, if the buyer treats it as an expense in the P&L, then the deduction towards GST also will be subject to payment as per Sec 15.

Q 11:

If payments made during the year do not cover the dues as on 1/4/23 plus purchases made during the year, how to find out disallowance if any?

In the following case, what will be the amount of disallowance?

Opening Bal (Cr) on 1/4/23	36,00,000
Purchases during the year 2023-24	18,00,000
Payments during the year 2023-24	30,00,000
Closing Bal (Cr) as on 31/03/2024	24,00,000

Both the Sec 43B(h) and MSMED Act are silent. It is a matter of appropriation towards dues. One can refer provisions of Indian Contract Act, 1872. Section 59, 60 and 61 deal with the appropriation.

Sec 59 – the person making payment (buyer) indicates the appropriation and if payment is accepted, then as per the same;

Sec 60 – if the debtor (buyer) omitted to indicate, then the creditor (seller) can apply at his discretion;

Sec 61 – if neither party specifies appropriation, then it should be towards debts in order of time.

Q 12:

What about provisions made instead of crediting individual creditors account?

The amount provisions represent sums payable for which deduction is otherwise allowable and therefore they have to satisfy Sec 15 for payments if those provisions are in respect of goods delivered or services rendered.

Q 13:

What about applicability of 43B(h) to the persons opting of presumptive taxation u/s 44AD/44ADA/44AE/44BBB?

The non obstante clause in sec 43B(h) apparently overrides all other provisions of act however the special provisions of Sec 44 AD/44ADA/44AE/44BBE also have non obstante clause (Sec 28 to 43C).

Sec 43B(h) overrides all other provision except the above.

Possible to take other view also – in view of decision in the case of Good Luck Kinetic Vs ITO – 2015 – ITAT Panaji.

Q 14:

What about applicability of Sec 43B(h) to charitable trusts?

Sec 11 of IT Act does not have any reference to the sec 43B(h) unlike 40(a)(ia), 40A(3) and 40A(3A). Hence it won't apply to trust while computing application of income. However, the trusts are liable to pay interest u/s 16 for delayed payments if any.

Q 15:

Will this provision apply to the MSEs also?

No such exemptions are there. Sec 15 uses the word buyer and hence it applies to the buyer, who are registered micro or small enterprises.

Q 16:

Will this apply to non-audit cases (like individual/HUF/Firm?)

Sec 43B(h) is applicable to all as it relates to the computation of income irrespective of quantum of turnover or status of the buyer – excepting those, who opt for presumptive scheme.

Q 17:

How investment in Plant and Machinery or Equipments are calculated for classification of MSME?

As per Notification No. 2119(E) dated 26.06.2020, it is linked to the income tax return – net investment value (depreciated cost, WDV, as per IT) – it shall have the meaning as per IT Rules - doesn't include land and building, furniture & fittings, cost of pollution control, research and development and industrial safety devices.

Q 18:

How is turnover calculated for classification?

As per Notification No. 2119(E) dated 26.06.2020, exports of goods or services or both shall be excluded for the purpose of classification. The turnover information is linked to the Income Tax Act or CGST Act and GSTIN.

Q 19:

What about upgraded enterprises – that is from Micro/Small to Medium?

Ex.

S No	Classification Year	Enterprise Type	Date of Classification
1	2023-24	Medium	12-05-2023
2	2022-23	Medium	20-06-2022
3	2021-22	Medium	16-05-2021
4	2020-21	Small	21-08-2020

As per Notification No. S.O.2119(E) dated 26.06.2020 (as amended by Notification No. S.O. 4927(E) dated 18.10.2022), in case of upward change in classification, an enterprise shall continue to avail of all non-tax benefits of existing category (before reclassification) for a period of three years from the date of such upward change.

Q 20:

What about reverse graduation (Downgraded) – Medium to Small?

As per Notification No. S.O.2119(E) dated 26.06.2020, the enterprise will continue in its present category till the closure of the financial year and the benefits of changed status will start only from the 1st April of financial year following the year in which the such change took place.

Q 21:

What about disallowance u/s 40(a)(ia) Vs 43B(h) – i.e. expenses already under disallowance for non-deduction of tax?

Sec 43B(h) – *a deduction otherwise allowable under this Act in respect of any sum payable.....*

In this situation, deduction cannot be said to be otherwise allowable to the extent of balance of amount survived after disallowance u/s 40(a)(ia) and hence the balance of 70% will be subject to the Sec 43B(h) disallowance.

Q 22:

How to check the status of enterprises by the buyer?

With the MSME Registration number, one can check in the portal (<https://udyamregistration.gov.in>) about the category (present and past also), Major Activity, date of registration.

THANK YOU