

# Amendments to the Income Tax Act, 1961 – Promoting timely payments to Micro and Small enterprises

## 1. Background

Section 43B of the Income Tax Act, 1961 deals with certain deductions that shall be allowed only on payment basis. Vide the Finance Act, 2023 a new clause (h) was added to Section 43B which states that any payment made to any micro or small enterprises beyond the specified time limit shall be allowed as a deduction only in the previous year ('PY') in which the actual payment is made and not on accrual basis, irrespective of the accounting system followed by the entity. In this alert, we have provided an overview of the new clause and the practical implications of the same for business entities.

## 2. Overview of the Micro<sup>1</sup>, Small<sup>2</sup> and Medium Enterprises Development (MSMED) Act 2006

- As per Section 15 of the MSMED Act, 2006 any payment to a micro or small enterprise should be made within the time period specified in the agreement (if any) between the supplier and the buyer and the same cannot exceed 45 days from date of acceptance (actual delivery of goods or services). In other words, even if the written agreement between the buyer and the supplier provides for a higher credit period, the credit period as per MSMED shall still be only 45 days.
- Further, in the absence of any written agreement, the payment should be made within 15 days from the date of acceptance of invoice.

## 3. Analysis of the new clause (h) under Section 43B

- The new clause states that any payment made to a micro or small enterprise beyond the time period specified under the MSMED Act, 2006 (refer Para 2 above) can be claimed as deduction only in the PY in which the actual payment is made, irrespective of the entity following accrual basis of accounting.
- In simple words, the new clause provides that payments to micro or small enterprises can be claimed as a deduction on payment basis. If there are certain invoices which are outstanding as on 31 March and paid within the due date in the subsequent PY, the aforesaid payment can be claimed as a deduction in the PY in which the expenses accrued. If not, the said expenses can still be claimed as a deduction in the PY in which the actual payment is made.
- Further, the proviso to Section 43B which allows the claim of deduction of the expenses in the PY if the same is not paid during the PY but paid on or before the due date of filing of return of income shall not be applicable to the aforesaid clause.

---

<sup>1</sup> Threshold limits for classification of an entity as a 'micro enterprise' is as follows:

- Investment in plant and machinery or equipment does not exceed Rs 1 crore; and
- Annual turnover does not exceed Rs 5 crores

<sup>2</sup> Threshold limits for classification of an entity as a 'small enterprise' is as follows:

- Investment in plant and machinery or equipment does not exceed Rs 10 crore; and
- Annual turnover does not exceed Rs 50 crores.

- The below table summarizes various scenarios where payment can be claimed as an deduction.

Date of acceptance of invoice	Due date in accordance with MSMED Act*	Payment date	Deduction	Reason
01/05/2023	15/06/2023	14/06/2023	✓	The amount can be claimed as deduction since it is paid within the due date under MSMED.
15/10/2023	29/11/2023	10/03/2024	✓	The amount can be claimed as deduction irrespective of the payment being made after the due date under MSMED since the same is paid during the PY 2023-24.
20/03/2024	04/05/2024	04/05/2024	✓	The amount can be claimed as deduction in PY 2023-24 since payment is made within the due date under MSMED, even though the payment is made after 31 <sup>st</sup> March 2024.
20/03/2024	04/05/2024	05/05/2024	X	The amount shall be disallowed in PY 2023-24 since it is paid after the due date under MSMED. However, it can be claimed as a deduction in the year of payment i.e., PY 2024-25.

\* The above dates are on the assumption that the invoices have a credit period of 45 days.

#### **4. Applicability of the provisions**

The aforesaid provisions are effective from assessment year 2024-25 and shall apply to every assessee undertaking a business activity (including MSME registered assessee).

However, it shall not apply to payments that are made to suppliers who are:

- Medium enterprises, since the word 'micro' and 'small' are only notified in the section.
- Engaged in the business of trade, retail or distribution since the definition of enterprise only covers manufacturing and service sectors.
- Not registered under the MSMED Act, 2006.

#### **5. Quick points of action**

##### **5.1 Points of action for payers**

- Obtain UDYAM registration certificates or written declaration in this regard from the vendors evidencing their registration under the MSMED Act, 2006 to check applicability of the above provisions.
- Complete the payments for the outstanding invoices due to Micro and Small vendors on or before 31 March 2024 to claim deduction for the said expenses in the current PY (i.e 2023-24). If not, the payment shall be made in PY 2024-25 but within the due date as specified under MSMED Act, 2006 to claim

deduction in PY 2023-24. If the same is not undertaken, the expense shall be disallowed in the tax computation for the PY 2023-24 and can be claimed only in the year of payment.

- Ensure that the agreements / purchase orders entered into with the vendor specifies a due date for payment, since the due date for making payment as per MSMED Act, 2006 in the absence of any due date in the agreement would be 15 days instead of extended period of 45 days.
- In case, there are any objection regarding acceptance of goods and services, the objection should be raised within 15 days of delivery of goods and services. In such a case, the day of delivery of goods or services will be the day on which such objection is removed by the supplier.

## **5.2 Points of action for payees**

- The vendors can mention their MSME registration number in the invoices to indicate to the recipient about the MSME registration.
- MSME registration can be obtained wherever applicable, so that timely payment can be made by the purchaser.

## **6. Concluding remarks**

The insertion of the new clause (h) under Section 43B is to ensure timely payments to micro and small enterprises and provide them with a better liquidity position. However, with the restricted credit cycle prescribed under the MSMED Act, 2006 there shall be a reluctance to purchase goods/avail services from MSME registered vendors.

Further, as we are on the verge of closure of PY 2023-24, it is critical that business entities revisit their creditor lists and identify if there are any MSME registered vendors. It is important that payments to such outstanding invoices are cleared by the end of 31 March 2024 to enable claim of the said expenses in PY 2023-24.

A new column is introduced in Part A – OI of ITR – 6 notified for assessment year 2024-25 to disclose the sum payable to micro or small enterprises beyond the specified time limit as per the MSMED Act. Accordingly, auditors and tax professionals have to ensure that the above provisions are complied with, especially in scenarios where there are invoices outstanding as on 31 March but paid within the due dates in the subsequent PY.

### **India – Chennai**

#### **M2K Advisors LLP**

7th Floor, Briley One,  
No. 30/ 64 Ethiraj Salai,  
Egmore, Chennai – 600 008,  
Tamil Nadu, India

### **India - Bengaluru**

#### **M2K Advisors LLP**

WeWork, No.43, Residency Road,  
Shanthala Nagar, Ashok Nagar,  
Bengaluru 560025

### **Singapore**

#### **M2K Advisors Pte Ltd**

The Octagon,  
105 Cecil Street, #13-02  
Singapore 069534

### **USA**

#### **M2K Advisors Inc**

16192 Coastal Highway,  
Lewes, County of Sussex,  
Delaware – 19958

### **UAE**

#### **M2K Advisors**

701 C Aspin Commercial Tower,  
Sheikh Zayed Road, Trade Center First,  
Dubai PO Box – 50810

### **Australia**

#### **M2K Advisors Pty Ltd**

Unit 605E, 888 Collins St,  
Docklands VIC 3008, Australia

For any queries, reach us at:  
[mukesh@m2k.co.in](mailto:mukesh@m2k.co.in); [swetha@m2k.co.in](mailto:swetha@m2k.co.in); [rithanya@m2k.co.in](mailto:rithanya@m2k.co.in)

*This deck is intended for general guidance only and hence should not be considered as an advice or opinion. We do not accept any responsibility for loss occasioned to any person acting or refraining from action as a result of any material in this deck. On any specific matter, reference should be made to the appropriate advisor.*