

Exploring the intricacies of section 43B(h)

In an effort to enhance support for the Micro and Small Enterprises, vide Finance Act, 2023, a new clause (h) was inserted in section 43B of the Income Tax Act, 1961 ('the Act') applicable from assessment year 2024-25 (fiscal year beginning on 01.04.2023). This significant amendment stipulates that if payment for purchases from "Micro" and "Small" enterprises are delayed beyond the credit period prescribed in section 15 of Micro, Small and Medium Enterprises Development Act, 2006 ('MSME Development Act, 2006'), the corresponding expenses would be disallowed in the year of incurrence. Nevertheless, such expense would qualify for deduction on payment basis in the financial year in which the amount is actually paid.

The aforementioned amendment would apply only to expenses incurred on or after 1st April 2023. Hence, payment for invoices issued on or after 1st April 2023, must be made within the specified time frame to qualify for deduction in the return of income for the assessment year 2024-25.

Section 15 of MSME Development Act, 2006 stipulates that the buyer must make payment to the supplier of goods or service within either (i) the mutually agreed time frame, not exceeding 45 days from the date of acceptance or, (ii) in the absence of agreement, within 15 days from the date of acceptance.

Even if the parties have mutually agreed to payment terms exceeding 45 days, the period would be capped at 45 days and due date would be ascertained accordingly.

It is pertinent to mention that only the outstanding as on 31st March 2024, which are due for more than 45 days (in case of written agreement, otherwise 15 days) would be covered within the ambit of section 43B(h) of the Act. However, payments made after 31st March 2024, but within the period of 45 days would be eligible for deduction.

It is noteworthy that while other clauses in section 43B allows deduction for expenditure on an accrual basis provided the payment is made before the due date for filing the return of income, the deduction for amount payable to MSEs covered under clause (h) is contingent upon payment being made within the time frame outlined in section 15 of the MSME Development Act, 2006.

It is imperative to note that transactions with traders would not be subjected to the aforementioned amendment. This has explicitly been clarified vide notification O.M. 5/2(2)/2021-E/P&G/Policy dated 02.07.2021, wherein, wholesale and retail trader(s) are eligible for Udyam registration solely for the purpose of Priority Sector Lending. The definition of an enterprise under MSME Development Act, 2006 encompasses only manufacturers and service providers. Hence, any amount payable to a creditor, being a trader, would not be subjected to the provisions of section 43B(h) of the Act.

Below are summarised different scenarios alongwith tax implications that necessitate consideration when transacting with MSEs:

Scenario	Tax implication
How can the buyer ascertain whether the supplier is registered under the MSME Act or not?	<p>The buyer must obtain a written declaration from the supplier regarding their registration status under the MSME Development Act, 2006.</p> <p>In the event where, despite diligent efforts, no communication regarding the MSME status is received from the supplier, it is advisable to maintain a copy of the relevant communication. This serves as a safeguard for the taxpayer against potential future litigation.</p>
Are the balances which are outstanding as on 31.3.2023 are also covered within the ambit of section 43B(h)?	No, only the balances outstanding as on 31.03.2024, and overdue by more than 45 days (or 15 days in the absence of a written agreement) are subject to the provisions of section 43B(h) of the Act.
If the buyer purchased goods on 01.07.2023 and made payment on 31.3.2024, will it be subject to disallowance?	Such payable amount would not be disallowed. Nevertheless, the buyer would be liable to pay interest on the outstanding balance for delayed payment which would be disallowed in the return of income.
If the buyer purchases goods on 20.03.2024, with a credit period of 45 days and remits payment on 25.04.2024, which falls within the 45 days period, will it be allowable?	Yes, considering the payment has been made within the credit period of 45 days, such expense would be allowed as deduction in the return of income for the assessment year 2024-25.
If the amount due as on 31.3.2024, is paid on 10.04.2024, i.e. before the due date of filing return, will it be allowed?	The proviso to section 43B explicitly excludes clause (h) from its purview. Therefore, the amount would not be allowed even if the same is paid before the due date of filing return of income. Such expense would be allowed in the return of income for the assessment year 2025-26.