

## SECTION 43B(H) IN PRACTICE: INSTITUTIONAL DESIGN, CONTRACTUAL REALITY, AND LIQUIDITY OUTCOMES FOR MSMES IN POST-AMENDMENT INDIA

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### Abstract:

The insertion of clause(h) to Section 43B of the Income Tax Act, 1961 represents a significant legislative intervention aimed at addressing habitual detentions in payments to micro and small enterprises (MSEs). By conditioning Tax deductibility on compliance with the payment timelines specified under the Micro, Small and Medium Enterprises Development Act, 2006, Parliament sought to realign marketable impulses in favor of timely agreement. While the statutory correction is now settled law, its functional effectiveness within India's being executive, contractual, and financial armature remains under- examined. This composition undertakes a post-legislative evaluation of Section 43B(h), fastening on its commerce with MSME status verification under the Udyam frame, the treatment of retention plutocrat in corner- grounded contracts, liquidity constraints arising from the Goods and Services Tax governance, and the practical enforceability of correctional interest under the MSMED Act. The study argues that without reciprocal institutional design and systemic collaboration, Section 43B(h) pitfalls generating compliance query and liquidity stress rather than fulfilling its defensive ideal. The composition concludes by proposing design acquainted reforms aimed at operationalizing legislative intent while conserving marketable certainty.

**Keywords:** Section 43B(h), MSME payments, delayed payment, retention plutocrat, GST working capital, nonsupervisory design

### Introduction:

Belated payments to micro and small enterprises have long been recognized as a structural point of India's marketable ecosystem. Despite statutory protections under the Micro, Small and Medium Enterprises Development Act, 2006(MSMED Act), enforcement has historically depended on the amenability and capacity of MSMEs<sup>891</sup> to assert their claims against larger buyers, frequently in conditions of unstable logrolling power. patient detentions have been constantly linked to liquidity stress, reduced creditworthiness, and constrained enterprise growth.

Section 43B of the Income Tax Act, 1961 has traditionally operated as a timing provision, allowing deductions only on factual payment for specified statutory arrears. The preface of clause(h) marked a departure from this sense by extending the payment- grounded deduction rule to marketable deals involving micro and small enterprises.<sup>892</sup> The ideal wasn't simply financial, but behavioral to bed payment discipline within the Tax system itself.

With the correction now in force, the central question is no longer one of legislative intent, but of nonsupervisory performance. Laws that seek to impact request behavior don't operate

<sup>891</sup> <https://www.taxguru.in/income-tax/section-43b-h-deduction-allowed-payment-basis.html>

<sup>892</sup> <https://www.indiafilings.com/learn/section-43bh-new-msme-45-days-payment-rule>

in insulation; their effectiveness depends on executive capacity, data integration,<sup>893</sup> contractual practice, and commerce with other financial administrations. This composition thus examines Section 43B(h) as law in operation, rather than law in abstraction.

## 2. Statutory and Regulatory Framework:

### 2.1. Section 43B(h) of the Income Tax Act, 1961

Section 43B(h) of the Income Tax Act, 1961 represents a significant shift in the way business expenditure relating to micro and small enterprises is treated for Tax purposes, with the clear ideal of administering fiscal discipline and guarding lower suppliers from delayed payments. This provision basically links the allowability of an expenditure under the Income- Tax Act to compliance with the payment timelines specified under the Micro, Small and Medium Enterprises Development Act, 2006(MSMED Act). Unlike earlier vittles of Section 43B, which primarily concentrated on statutory pretenses similar as Tax, Tax, or employer benefactions, clause(h) directly addresses marketable deals and seeks to remedy the long- standing issue of delayed payments to MSMEs, which frequently face cash inflow constraints due to their weaker logrolling power.

Under this provision, any sum outstanding by a taxpayer to a micro or small enterprise for goods supplied or services rendered isn't allowed as a deduction unless the payment is made within the time limits specified under Section 15 of the MSMED Act. The determination of the admissible payment period depends on whether there's a written agreement between the buyer and the supplier. In the absence of a written agreement, the law authorizations that payment must be made within fifteen days from the date of acceptance or supposed acceptance of goods or services. The conception of acceptance or supposed acceptance is important, as it prevents buyers

from indefinitely delaying payment by delaying acknowledgment or raising frivolous expostulations. Where a written agreement exists, the law allows a longer payment period, but indeed in similar cases, the maximum time limit is limited at forty- five days from the date of acceptance or supposed acceptance. This external limit is obligatory and cannot be extended indeed by collective concurrence of the parties, thereby booting contractual terms that give for longer credit ages.

The Tax consequence of non-compliance with these timelines is strict. However, the corresponding expenditure is disallowed in the time in which it else accrued under the mercantile system of account, if the buyer fails to make payment within the prescribed period. This means that indeed though the liability is genuine and has been recorded in the books, it cannot be claimed as a deduction while calculating taxable income for that time. The deduction is remitted and becomes permissible only in the time in which the factual payment is made to the micro or small enterprise. This medium operates as an interference against delayed payments, as it directly impacts the taxable gains of the buyer and may affect in advanced Tax outgo in the time of dereliction.

It's also important to note that this provision applies only to payments made to micro and small enterprises and not to medium enterprises, indeed though all three orders fall within the broader MSME frame. thus, taxpayers are needed to exercise due industriousness in relating the status of their suppliers, generally by carrying MSME enrollment details, to determine whether Section 43B(h) is applicable. Failure to do so can lead to unintended disallowances and controversies during assessment proceedings.

Overall, Section 43B(h) reinforces the legislative intent of the MSMED Act by using Tax law as an enforcement tool to ensure timely payments to lower enterprises. By postponing deductions until factual payment is made, the provision promotes better payment practices, improves

<sup>893</sup> <https://www.financialexpress.com/budget/msme-fin-budget-2023-may-end-msmes-delayed-payment-crisis-proposes-to-amend-section-43b-of-income-tax-act-check-details-2968381>

liquidity for micro and small enterprises, and discourages the use of prolonged credit cycles that can negatively affect their fiscal stability.

## 2.2. MSMED Act, 2006:

The Micro, Small and Medium Enterprises Development Act, 2006 was legislated with the clear ideal of guarding micro and small enterprises from habitual payment detentions and the fiscal stress that similar detentions beget. In practice, small businesses frequently operate with limited working capital and depend heavily on timely consummation of pretenses from buyers, especially larger corporates and government realities. Recognizing this imbalance in logrolling power, the MSMED Act lays down a statutory frame that makes timely payment a legal obligation rather than a matter of marketable convenience. Under the Act, where a supplier is a micro or small enterprise, the buyer is needed to make payment within the time agreed in jotting, which cannot exceed forty- five<sup>894</sup> days from the date of acceptance or supposed acceptance of goods or services. In the absence of any written agreement, the law authorizations payment within fifteen days. These timelines aren't simply directory in nature; they're enforceable scores backed by strict consequences in case of dereliction.

One of the most significant features of the MSMED Act is the provision relating to interest on delayed payments. However, the buyer becomes liable to pay emulsion interest, calculated with monthly rests, if the buyer fails to make payment within the prescribed period. This rate is designedly kept corrective, not compensatory, to discourage buyers from using delayed payments as a means of financing their own operations at the cost of small suppliers. Unlike ordinary marketable interest<sup>895</sup>, which may be negotiated or waived, interest under the MSMED Act arises automatically by operation of law once the detention occurs,

irrespective of whether the supplier has expressly demanded it. This statutory interest reflects the legislative intent to treat delayed payment to micro and small enterprises as a serious profitable wrong rather than a routine business issue.

Section 23 of the MSMED Act further strengthens this intent by addressing the Tax treatment of similar interest. It expressly provides that any interest outstanding or paid by a buyer under the vittles relating to delayed payments shall not be allowed as a deduction while calculating income under the Income Tax Act, 1961. The effect of this provision is twofold. First, it removes any implicit Tax advantage that a defaulting buyer might else have claimed by treating the interest as a normal business expenditure.<sup>896</sup> Second, it reinforces the correctional character of the interest by icing that the fiscal burden of non-compliance is completely borne by the buyer and not laterally participated with the public bankroll. This unequivocal disallowance leaves little compass for interpretational controversies and makes it clear that compliance with MSME payment timelines isn't voluntary or cost-neutral.

The Act also provides a devoted medium for disagreement resolution through the Micro and Small Enterprises Facilitation Council (MSEFC). A supplier who has not entered payment, along with applicable interest, may make a reference to the Council, which first attempts concession and, if that fails, proceeds to arbitration. Awards passed by the Council or through arbitration under its aegis have the same enforceability as a decree of a civil court. In proposition, this medium offers a briskly and less precious volition to conventional action, acclimatized specifically to the requirements of micro and small enterprises. still, in practice, the effectiveness of this system has depended largely on the action taken by the supplier. numerous small enterprises, due to lack of mindfulness, fear of losing unborn business, or

<sup>894</sup> <https://cleartax.in/s/section-43bh-of-income-tax-act>

<sup>895</sup> <https://www.mondaq.com/india/income-tax/1608608/applicability-of-section-43bh-of-the-income-tax-act-1961-on-payments-to-msme>

<sup>896</sup> <https://taxguru.in/income-tax/section-43bh-allowability-payments-msmes-beyond-statutory-timeline.html>

enterprises about dragged proceedings, vacillate to bring the vistles of the Act. As a result, enforcement has remained largely descendant - driven rather than controller-driven.

Despite these practical challenges, the MSMED Act represents a strong legislative statement in favor of payment discipline and fair treatment of micro and small enterprises. By combining obligatory payment timelines, steep emulsion interest for detentions, denial of Tax deductibility for similar interest, and a specialized disagreement resolution frame, the Act seeks to change settled marketable behavior its effectiveness eventually depends on mindfulness, amenability of suppliers to assert their rights, and harmonious interpretation by courts and authorities.<sup>897</sup> When read as a whole, the Act underscores that timely payment to micro and small enterprises isn't simply good business practice but a legal and profitable imperative backed by clear statutory consequences.

### 2.3. GST Framework and Liquidity:

The introduction of the Goods and Services Tax was intended to simplify India's indirect tax system by replacing multiple central and state levies with a unified framework, reducing cascading of taxes and improving transparency. While this reform has largely succeeded in creating a common national market and streamlining compliance, its impact on the liquidity position of businesses—particularly micro, small and medium enterprises—has been mixed. One of the most persistent challenges under the GST regime has been the continuation, and in some sectors the deepening, of inverted Tax structures, which has direct implications for working capital management and financial stability of MSMEs.<sup>898</sup>

An inverted Tax structure arises when the tax rate applicable on inputs is higher than the rate on the output supply. Under such a scenario, businesses pay more GST on raw materials, components, or input services than they collect on the final goods or services they supply. This imbalance results in the accumulation of input tax credit that cannot be fully utilized through output tax liability. Although the GST law provides for refunds of unutilized input tax credit in cases of inverted Tax structures, the process is neither automatic nor immediate. For MSMEs operating with limited financial buffers, this accumulation of credit effectively converts a portion of their working capital into a blocked asset.

In MSME-intensive sectors such as textiles, footwear, fertilizers, and certain segments of food processing and engineering goods, inverted Tax structures have become a structural issue rather than a temporary anomaly. These enterprises often operate on thin margins and depend heavily on regular cash flows to meet day-to-day operational expenses, including wages, rent, utilities, and repayments to suppliers. When a significant portion of their funds is locked in the form of unutilized input tax credit, their ability to reinvest in production, service debt, or respond to market opportunities is constrained. This situation is particularly acute for small firms that do not have easy access to formal credit or the bargaining power to extend payment cycles with vendors.

The refund mechanism, which is meant to alleviate this burden, is itself subject to procedural complexities. Businesses are required to file detailed refund applications, reconcile invoices, and comply with strict documentation requirements. Any discrepancy, however minor, can lead to queries, delays, or partial rejections. Moreover, refunds are processed after prescribed timelines, and in practice, these timelines are often exceeded due to administrative backlogs or system-related issues. During this waiting period, the enterprise bears the cost of funds without any

<sup>897</sup> <https://www.taxmann.com/post/blog/faqs-liability-of-buyer-u-s-15-of-msmed-act-to-make-timely-payments-to-mse-suppliers>

<sup>898</sup> <https://www.indiacode.nic.in/bitstream/123456789/2013/3/A2006-27.pdf>

compensatory interest that truly reflects the commercial cost of capital. For MSMEs<sup>899</sup>, this delay translates into increased reliance on short-term borrowings, higher interest costs, or reduced scale of operations.

The liquidity impact of such locked-in credits becomes even more pronounced during periods of economic slowdown or disruption. When demand weakens, output tax liability reduces, further limiting the scope for adjusting accumulated input tax credit. At the same time, fixed costs continue to accrue, and access to external finance becomes more difficult. In this context, the GST-induced working capital blockage can exacerbate financial stress and push otherwise viable enterprises into distress. Unlike larger corporations, MSMEs often lack dedicated tax teams or advanced systems to manage compliance efficiently, making the refund process more resource-intensive and uncertain.

While policy measures such as rate rationalization and periodic reviews of inverted Tax structures have been undertaken, the underlying issue remains unresolved in several sectors. The persistence of these structures indicates a disconnect between tax policy design and ground-level business realities. For the GST framework to truly support MSME growth and sustainability, the liquidity implications of tax rate inversions must be addressed more decisively, either through corrective rate adjustments or through a more efficient, time-bound, and predictable refund mechanism. Until then, unutilized input tax credit will continue to function as a silent drain on working capital, undermining the very objective of GST as a facilitator of ease of doing business.<sup>900</sup>

### 3. Review of Existing Literature:

The being literature dealing with Section 43B(h) of the Income Tax Act, 1961 reflects a growing

but still fractured academic and professional engagement with the provision. A substantial portion of the available work is guru acquainted, penned primarily by Tax advisers, chartered accountants, and compliance professionals. These jottings largely concentrate on the immediate practical consequences of the provision, similar as changes in inspection exposures, increased scrutiny during Tax assessments, and the threat of disallowance of expenditure<sup>901</sup> where payments to micro and small enterprises aren't made within the timelines specified under the MSMED Act.

similar narrative tends to give guidance on attestation, identification of MSME merchandisers, conciliation of checks, and the manner in which overdue quantities must be treated while calculating taxable income. Although these workshops are useful from a compliance viewpoint, they frequently borrow a roster-grounded approach and don't deeply interrogate the abstract or systemic counter accusations of linking Tax deductibility to payment timelines under a separate weal legislation.<sup>902</sup>

Another beachfront of literature adopts a more doctrinal perspective, examining the statutory construction of Section 43B(h) and its relationship with the MSMED Act, 2006. Scholars in this order focus on interpreting crucial expressions similar as "sum outstanding" and "micro or small enterprise," as well as the legal consequences of non-compliance with Section 15 of the MSMED Act. Considerable attention is paid to whether the disallowance under Section 43B(h) operates automatically or is contingent upon formal recognition of the supplier as an MSME, and how far the buyer is anticipated to corroborate similar status. These analyses also explore the legislative intent behind introducing clause(h) to Section 43B<sup>903</sup>, sticking it within the

<sup>899</sup> <https://cleartax.in/s/gst-inverted-duty-structure>

<sup>900</sup> [https://tutorial.gst.gov.in/userguide/refund/Refund\\_of\\_ITC\\_accumulated\\_due\\_to\\_inverted\\_tax\\_structure\\_%28RFD-01A%29.htm](https://tutorial.gst.gov.in/userguide/refund/Refund_of_ITC_accumulated_due_to_inverted_tax_structure_%28RFD-01A%29.htm)

<sup>901</sup> <https://gandhidham-icai.org/Pdf/Study-material/43B%28h%29.pdf>

<sup>902</sup> <https://www.taxmann.com/research/income-tax/top-story/1050100000023718/revolutionizing-business-payments-impact-of-sec-43bh-on-msme-dynamics-and-compliance-strategies-experts-opinion>

<sup>903</sup> <https://www.snrlaw.in/wp-content/uploads/2024/03/SR-Insights-Payments-to-Micro-and-Small-Enterprises-MSEs.pdf>

broader ideal of discouraging delayed payments and strengthening the fiscal position of small enterprises. still, much of this discussion remains confined to textual interpretation and case- law circumlocutions drawn from earlier clauses of Section 43B, without sufficiently addressing how the provision functions in real marketable settings where contracts, credit cycles, and assiduity practices vary significantly.

A third body of literature approaches the issue from a policy and profitable viewpoint, fastening on the habitual liquidity challenges faced by MSMEs in India. These studies punctuate delayed payments by larger buyers as a patient structural problem and dissect how statutory interventions, including the MSMED Act and Tax- grounded deterrents like Section 43B(h), end to correct this imbalance. Some policy papers also link the discussion to broader financial issues, similar as working capital constraints aggravated by GST compliance conditions, input Tax credit mismatches, and limited access to formal credit. From this standpoint, Section 43B(h) is seen as a financial tool intended to alter buyer behavior by adding the cost of delayed payments. While this literature provides precious macro-level perceptivity, it frequently treats Section 43B(h) as a standalone incitement medium and doesn't adequately examine the executive and verification challenges that arise during its perpetration.<sup>904</sup>

Across these beaches, a common limitation is the tendency to dissect individual confines of the provision in insulation. There's fairly little engagement with how multiple factors similar as the absence of standardized data- sharing mechanisms between Tax authorities and MSME enrollment databases, the diversity of contractual payment terms in marketable practice, and the liquidity pressures faced by buyers themselves – interact contemporaneously to shape the real- world

impact of Section 43B(h). also, utmost jottings stop short of offering apost-legislative evaluation of whether the provision effectively balances the binary objects of guarding MSMEs and maintaining marketable inflexibility for businesses. As a result, the being literature, though instructional,<sup>905</sup> leaves significant compass for a more intertwined assessment that situates Section 43B(h) within the broader nonsupervisory, financial, and profitable ecosystem governing business deals in India.

#### 4. Research Gap and Scope

This study is positioned against the background of adding nonsupervisory attention on timely payments to micro and small enterprises and the corresponding Tax consequences assessed on buyers for delayed agreements. Although Section 43B(h) of the Income Tax Act, 1961 has introduced a significant compliance obligation by linking deductibility of expenditure to adherence with payment timelines under the MSMED Act,<sup>906</sup> the academic and doctrinal engagement with its practical operation remains limited. The present exploration seeks to bridge this gap by examining areas where legal intent, executive practice, and marketable reality don't completely align.

One of the primary gaps lies in the manner in which the bracket of enterprises under the Udyam enrollment frame is applied for Tax compliance purposes. The Udyam system classifies enterprises on the base of investment and development, both of which are variable and may change from one fiscal time to another. still, the operation of Section 43B(h) requires buyers to determine, at the time of reserving expenditure and claiming deductions, whether the supplier qualifies as a micro or small enterprise. Being literature doesn't sufficiently examine how this time-sensitive identification is anticipated to be carried out in

<sup>904</sup> <https://bcajonline.org/journal/section-43bh-of-the-income-tax-act-and-msme-payments-interpreting-the-fine-print>

<sup>905</sup> [https://icmai.in/upload/Taxation/TaxBulletin/Tax\\_Bulletin\\_161.pdf](https://icmai.in/upload/Taxation/TaxBulletin/Tax_Bulletin_161.pdf)

<sup>906</sup> <https://www.taxmann.com/research/income-tax/top-story/10501000000023982/timely-payments-to-msmes-analysing-the-impact-of-section-43bh-amendment-experts-opinion>

practice, particularly when enterprise status may shift during the time or when streamlined Udyam information isn't readily available to the buyer. This creates query for taxpayers and raises questions about the institutional mechanisms for verification, exposure, and reliance on supplier affirmations, all of which remain under-analyzed in current education.

A alternate undetermined area concerns the treatment of retention plutocrat and corner grounded payments, which are common features in construction, structure, and large design contracts. In similar arrangements, a portion of the payment is contractually withheld until the completion of specified mileposts or disfigurement liability ages. While marketable practice treats similar totalities as contingent or remitted, Section 43B(h) operates on the conception of "sum outstanding" to a micro or small enterprise. The precise point at which retention plutocrat becomes "outstanding" for the purposes of disallowance has not been easily addressed either in judicial precedents or academic jotting. This lack of clarity creates practical compliance challenges, as businesses may face disallowance indeed where remittance is embedded in contractual terms rather than detention or dereliction. The exploration thus identifies a significant gap in understanding how statutory payment timelines interact with assiduity-specific contractual structures.<sup>907</sup>

The third gap emerges from the crossroad of Section 43B(h) with the Goods and Services Tax governance, particularly in relation to working capital pressures. GST requires Tax to be discharged on a tab base, frequently before factual damage of payment, thereby locking up finances in Tax exoduses. When this obligation is combined with the strict payment timelines commanded under the MSMED Act and corroborated through Section 43B(h), buyers may face compounded liquidity constraints. Despite the practical significance of this issue,

being studies tend to examine GST and income Tax vittles in insulation, without adequately theorizing their concerted impact on cash overflows and compliance works. This exploration addresses that elision by sticking Section 43B(h) within the broader financial ecosystem and analyzing its accretive effect on business liquidity.<sup>908</sup>

Eventually, there's limited examination of the truculent part of correctional interest under the MSMED Act from a nonsupervisory design perspective. While the Act prescribes a high rate of emulsion interest for delayed payments, little attention has been paid to whether this penalty functions as an effective interference or simply as a theoretical safeguard that's infrequently executed. The commerce between this correctional interest governance and the income tax disallowance under Section 43B(h) also remains underexplored. Understanding whether these measures authentically incentivize timely payment, or rather produce compliance burdens without corresponding behavioral change, represents an important gap in the literature.<sup>909</sup>

The compass of this study is designedly confined to micro and small enterprises, as Section 43B(h) doesn't extend its connection to medium enterprises. By fastening on this member, the exploration aims to give a detailed and environment-specific analysis of the legal, profitable, and executive challenges arising from the provision, while contributing to a further nuanced understanding of its real-world counter accusations.

## 5. Methodology

The methodology espoused in this study is primarily qualitative in nature and is predicated in a doctrinal as well as institutional frame of analysis. The exploration proceeds on the understanding that issues arising in taxation and nonsupervisory law cannot be adequately examined through numerical or statistical styles

<sup>907</sup> <https://www.snrlaw.in/payments-to-micro-and-small-enterprises-mses-implications-under-section-43bh-of-income-tax-act-1961>

<sup>908</sup> <https://cleartax.in/s/section-43bh-of-income-tax-act>

<sup>909</sup> <https://www.nagpuricai.org/seminar-presentations/DG-MSME.pdf>

alone, as they're deeply shaped by legislative intent, policy considerations, and executive interpretation. Consequently, the study relies on a close and methodical examination of statutory vittles, with particular attention given to the language of the Income Tax Act, applicable confederated legislation<sup>910</sup>, and emendations introduced through Finance Bills from time to time.

The legislative history of these vittles is also considered in order to understand the mischief sought to be addressed by the council and the broader profitable or compliance related objects underpinning similar enactments. Finance Bill memoranda,<sup>911</sup> explicatory notes, and administrative accoutrements are used as important illuminative aids, as they frequently clarify the explanation behind statutory changes and give sapience into how the law is anticipated to operate in practice. In addition to primary legislation, the exploration takes into account nonsupervisory guidance issued by Tax authorities, including leaflets, announcements, and interpretations, which play a significant part in shaping compliance works and executive enforcement. These accoutrements are examined not simply as binding instructions but as pointers of the institutional approach espoused by the Tax administration in enforcing the law. Policy documents and sanctioned reports are also appertained to, as they help stick the statutory frame within the larger environment of profitable policy, ease of doing business, and protection of vulnerable stakeholders. While judicial opinions aren't<sup>912</sup> the central focus of the study, prevailing illuminative trends in Tax administration and marketable practice are considered to the extent that they reflect how the law is understood and applied on the ground.

The methodology is designedly evaluative rather than empirical, as the ideal isn't to measure issues through data collection but to critically assess the structure and design of the

nonsupervisory frame itself. By espousing this approach, the study seeks to identify the beginning conditions and hypotheticals that impact nonsupervisory issues, similar as the balance between profit considerations and marketable realities, the part of compliance timelines, and the commerce between different statutory administrations. This system allows for a nuanced assessment of how legal vittles operate within institutional settings and how they may produce intended or unintended consequences for stakeholders. Overall, the chosen methodology enables a coherent and in- depth analysis of the legal and policy frame, icing that conclusions are drawn from a careful reading of authoritative sources and an informed understanding of the nonsupervisory terrain, rather than from insulated compliances or purely theoretical constructs.

## 6. Analysis

### 6.1. MSME Verification and Administrative Design:

Udyam enrollment has been specified as the primary and sanctioned medium for relating and classifying micro, small and medium enterprises under the MSME frame. At the time of enrollment, the status of an enterprise is determined on the base of its investment in factory and ministry or outfit and its development, as declared by the enterprise. still, these parameters aren't stationary in nature. During the course of a fiscal time, an enterprise may expand its operations, cross the specified thresholds, or restructure its business, performing in a change in its MSME status. similar changes may do gradationally and may not be incontinently reflected on the Udyam portal<sup>913</sup>.

In practical terms, this creates a significant executive challenge for buyers who are needed to misbehave with statutory vittles that depend upon the MSME status of their merchandisers. At present, there's no flawless, real- time integration between the Udyam enrollment

<sup>910</sup> <https://incometaxindia.gov.in/pages/acts/income-tax-act.aspx>

<sup>911</sup> <https://incometaxindia.gov.in/pages/circulars.aspx>

<sup>912</sup> <https://www.niti.gov.in>

<sup>913</sup> [https://www.udyamregistration.gov.in/Udyam\\_Verify.aspx](https://www.udyamregistration.gov.in/Udyam_Verify.aspx)

database and the Income Tax system through PAN-based data sharing. In the absence of such a medium, buyers are impelled to calculate on tone affirmations handed by merchandisers or on stationary instruments downloaded from the Udyam portal, which may not directly represent the seller's current eligibility. This places buyers in a vulnerable position, as they've limited means to singly corroborate whether the enterprise continues to qualify as a micro or small enterprise<sup>914</sup> at the applicable point of time.

This gap in executive design effectively transfers the threat of incorrect bracket from the nonsupervisory system to the taxpayer. Indeed, where a buyer has acted in good faith and exercised reasonable industriousness, any posterior reclassification of the seller may expose the buyer to adverse Tax consequences. From a nonsupervisory and governance perspective, such an approach weakens legal certainty and predictability. However, the nonsupervisory frame must be supported by a robust and intertwined data structure that allows stakeholders to pierce accurate and over- to- date information, if compliance scores are made contingent upon a status that can change stoutly. In the absence of similar integration, the compliance governance pitfalls getting uncertain and arbitrary, thereby lacing the ideal of chastened and fair enforcement.

## 6.2. Retention Money and Contractual Reality:

Retention plutocrat, by its veritably nature, isn't a laid over payment of a quantum that has formerly come due, but a tentative contractual right that arises only after specific post-completion scores are fulfilled. In utmost marketable contracts, particularly in construction, structure, and service arrangements, retention plutocrat is designedly withheld to secure performance during the disfigurement liability or bond period.<sup>915</sup> The

contractor doesn't acquire an unconditional right to admit this quantum simply because the work has been completed or certified for interim purposes. rather, the right to admit retention plutocrat remains contingent upon satisfactory performance over time, rectification of blights, and compliance with contractual norms. This distinction is pivotal because the law has constantly recognized that a liability can be said to accrue only when it becomes fairly enforceable and not simply when work is executed or measured.

Judicial interpretation in both Tax and contract law has constantly drawn a clear line between the addendum of liability and the crystallization of an obligation to pay. A liability accrues when the obligation is definite and enforceable, whereas crystallization occurs when all conditions attached to that obligation are satisfied. Retention plutocrat falls exactly in the ultimate order. Until the quested conditions are met, the quantum remains uncertain and contingent, and the payer is under no legal coercion to release it. Courts have thus treated retention plutocrat as not forming part of the contractor's immediate income, precisely because the annuity itself is deficient and tentative at that stage still it effectively ignores the marketable and legal substance of similar arrangements, if retention plutocrat is treated as "outstanding" incontinently upon acceptance or instrument of work. Acceptance of work for functional or counting purposes doesn't automatically exclude the contractor's continuing liabilities<sup>916</sup> under the contract. Conflating acceptance with crystallization pitfalls distorting the timing of deductions and income recognition. In the environment of Section 43B(h), such an approach may lead to disallowance of quantities that aren't fairly due or recoverable at the applicable time. This is particularly problematic because Section 43B operates on the premise that the liability has formerly accrued but is allowed as a deduction only upon factual payment. Applying it to

<sup>914</sup> <https://www.indiafilings.com/learn/section-43bh-new-msme-45-days-payment-rule>

<sup>915</sup> <https://www.scribd.com/document/920623721/2025-06-09T15-19-2025-175-Taxmann-Com-232-Article-MSME-Compliance-Dynamics-a-Tale-of-Two-Stakehol>

<sup>916</sup> <https://www.indiafilings.com/learn/section-43bh-new-msme-45-days-payment-rule>

retention plutocrat, which has not yet progressed into a outstanding liability, stretches the provision beyond its intended compass.

More importantly, this interpretation has the implicit to disrupt long- standing marketable practices. Retention clauses are an accepted threat- allocation medium designed to cover the interests of the payer while icing quality and compliance by the contractor. However, businesses could face endless disallowance of licit charges simply because the contractual conditions for release have n't yet been satisfied, If Tax law were to treat these contingent totalities as incontinently outstanding. In the absence of clear legislative or executive explanation, such an interpretation introduces query and undermines the principle that Tax treatment should follow the real legal and marketable character of deals rather than a superficial reading of contractual mileposts.

### 6.3. GST Working Capital and Liquidity Interaction:

The commerce between GST vittles and working capital operation has come a critical issue for businesses, particularly micro, small and medium enterprises. Under the GST frame, one of the most significant challenges arises from reversed Tax structures, where the Tax rate on inputs is advanced than the Tax rate on outside inventories. In similar cases, businesses routinely accumulate input Tax credit that cannot be incontinently utilized. Although this credit is fairly available, in practical terms it remains locked for long ages, thereby confining the free inflow of finances. For enterprises that operate on thin perimeters and calculate heavily on nonstop cash rotation, this accumulation effectively converts a Tax medium into a working capital blockage<sup>917</sup>.

The problem becomes more severe when delayed payments are regard into the equation. MSMEs frequently warrant strong logrolling power and are impelled to extend credit to larger buyers. When payments aren't entered

within the anticipated time, the enterprise is forced to finance its operations through internal reserves or external borrowing. At the same time, GST liability on outside inventories must be discharged irrespective of whether the trade proceeds have actually been realized. As a result, businesses face a situation where Tax is paid in cash while corresponding input credits remain unutilized, leading to a double strain on liquidity.

The preface of Section 43B(h) of the Income-Tax Act further alters this geography by shifting the Tax consequence of delayed payments onto the buyer. While the provision is intended to cover MSMEs by encouraging timely payments, its commerce with GST dynamics is complex. Buyers who fail to pay MSMEs within the prescribed period lose the deduction for similar expenditure until the payment is actually made. This effectively increases the cost of detention for buyers and acts as a statutory pressure medium. still, from a marketable perspective, this may also disrupt established force- chain connections, as buyers may seek to talk credit terms, prices, or indeed shift to indispensable suppliers to avoid implicit Tax disallowances.<sup>918</sup>

When these vittles operate contemporaneously, the liquidity outgrowth isn't determined by any single law in insulation. rather, it emerges from the concerted effect of GST credit blockages, mandatory Tax payments on addendum, delayed realization of receivables, and income tax consequences linked to payment timelines. For MSMEs, this accretive operation can affect in patient cash inflow stress, indeed when the business is profitable on paper. The situation highlights a broader reality of the financial ecosystem, where well- intentioned vittles aimed at profit protection or MSME support may, when concentrated together, produce unintended fiscal pressure. Understanding this commerce is essential for policymakers and businesses

<sup>917</sup> <https://taxguru.in/income-tax/msme-income-tax-act-1961-msmed-act-2006.html>

<sup>918</sup> <https://www.compliancecalendar.in/learn/section-43b-h-msme-45-days-payment-rule>

likewise, as sustainable liquidity depends not simply on compliance with individual bills, but on how those bills serve together in practice.

#### 6.4. Penal Interest and Enforcement Dynamics

The MSMED Act contains strong vittles on correctional interest with the clear intention of discouraging delayed payments to micro and small enterprises and compensating them for the fiscal stress caused by similar detainments. In law, the rate of correctional interest is designedly kept high so that buyers are disincentivized from using MSMEs as informal sources of credit. still, the practical working of these vittles reveals a significant gap between what the enactment pledges and what MSMEs are actually suitable to apply. In reality, utmost micro and small enterprises operate in conditions of unstable logrolling power and are heavily dependent on a limited number of larger buyers for regular business. Because of this marketable dependence, MSMEs<sup>919</sup> are frequently reticent to demand correctional interest indeed when they're fairly entitled to it, as doing so may strain business connections, affect in loss of unborn orders, or lead to informal blacklisting. For numerous small businesses, durability of work is perceived as more important than administering a legal claim, indeed at the cost of delayed payments.

Another important issue lies in the way enforcement mechanisms are structured. While the law provides for recovery of pretenses along with correctional interest through legal and quasi-judicial processes, the responsibility to initiate action rests entirely on the affected MSME. There's no automatic or system- driven enforcement touched off by delayed payment itself. This individualized enforcement model places a procedural and cerebral burden on small enterprises, which frequently warrant the time, coffers, or legal support needed to pursue claims against financially stronger buyers. As a result, the trouble of correctional interest remains largely theoretical in numerous cases,

rather than a routinely applied consequence of non-compliance.

This situation highlights that nonsupervisory effectiveness depends not only on the inflexibility of penalties specified in legislation but also on how fluently and constantly those penalties can be executed in practice. Indeed, though the statutory language of the MSMED Act is strict, its truculent impact is weakened when enforcement is sporadic and complaint-driven. Larger buyers, apprehensive of the disinclination of MSMEs<sup>920</sup> to escalate controversies, may continue to delay payments with limited fear of consequences. thus, the core issue isn't the absence of harsh legal vittles but the absence of a systemic enforcement frame that reduces dependence on individual action. Without mechanisms that encourage or ensure routine compliance similar as automated monitoring, institutional enforcement, or stronger buyer responsibility – the correctional interest vittles are doubtful to achieve their intended ideal of guarding MSMEs and promoting timely payments.

#### 7. Policy Counteraccusations and Recommendations

1. The policy intent behind Section 43B(h) is to ensure that micro and small enterprises admit timely payments and aren't forced to finance larger buyers through dragged credit cycles. still, for this provision to achieve its willed impact without causing avoidable compliance controversies or functional difficulty, certain systemic and executive advances are necessary. One of the foremost conditions is the creation of a dependable and robotic medium for relating whether a supplier qualifies as a micro or small enterprise.<sup>921</sup> At present, businesses frequently face query because MSME status may not be borne at the time of entering into a sale, or it may change during the time. A PAN based integration between the Udyam Registration portal and the income tax

<sup>920</sup> <https://cleartax.in/s/msme-samadhan>

<sup>921</sup> <https://taxconcept.net/income-tax/critical-issues-on-msmes-under-section-43bh-of-income-tax-act>

<sup>919</sup> <https://www.casemine.com/search/in/retention%2Bmoney>

system would bring much demanded clarity. However, both taxpayers and the tax authorities can avoid controversies arising from retrospective claims or inconsistent affirmations, thereby enhancing pungency and trust in the system, if MSME status is automatically empirical at the time of return form or during assessment.

2. Another area that requires careful policy attention relates to contractual terms, particularly in diligence where payment structures are staggered by design. In sectors similar as construction, structure, and engineering services, it's common to withhold a portion of the payment as retention plutocrat to secure performance or cover blights. Without clear guidance, there's a threat that similar quantities may be treated as incontinently outstanding totalities, indeed though they're contractually remitted and contingent upon unborn performance. Issuing a clarificatory indirect that distinguishes genuine retention plutocrat from ordinary trade payables would reduce interpretational conflicts and help unintended disallowances. similar explanation would also admire marketable realities while icing that the defensive ideal of Section 43B(h)<sup>922</sup> isn't adulterated.

3. Liquidity constraints faced by buyers, especially those operating on thin perimeters, also earn consideration. While the law correctly prioritizes timely payment to MSMEs, enforcement without corresponding liquidity support mechanisms may strain working capital, particularly in cases where buyers are awaiting refunds or credits from the government. A coordinated approach that aligns GST refund processing with MSME payment scores could help address this issue. Faster and further predictable GST refunds would enable businesses to meet their statutory payment timelines without resorting to fresh borrowing, thereby supporting compliance while maintaining fiscal stability across the force chain.

4. Eventually, the effectiveness of Section 43B(h) shouldn't rest solely on MSMEs initiating enforcement or lodging complaints, as lower enterprises may vacillate to do so due to fear of marketable retribution. A further institutionalized reporting frame could address this imbalance. Banks, statutory adjudicators, or indeed payment platforms could be needed to flag patient detainments in payments to registered MSMEs through structured reporting systems. similar data-driven oversight would allow controllers to identify habitual defaulters and take corrective action without placing the burden on MSMEs themselves. Over time, this would foster a culture of timely payment, reduce action, and strengthen confidence in the formal business ecosystem. In sum, thoughtful executive collaboration, contractual clarity, liquidity support, and systemic reporting can inclusively ensure that Section 43B(h) functions as a fair and effective tool for MSME protection rather than a source of unintended disunion.<sup>923</sup>

### 8. Significance of the Study:

The significance of this study lies in its deliberate shift down from a narrow, textbook-grounded reading of Tax legislation towards a deeper examination of how non-supervisory vittles serve once they enter the real profitable and executive geography. Rather than treating Section 43B(h) of the Income Tax Act as a bare compliance demand assessed on taxpayers, the study approaches it as a living nonsupervisory medium whose success or failure depends largely on institutional behavior, executive capacity, and the impulses created for different stakeholders. This perspective is important because legislative intent alone doesn't guarantee issues, particularly in complex financial systems where multiple laws, authorities, and request practices interact contemporaneously.<sup>924</sup>

<sup>922</sup> <https://cleartax.in/s/section-43bh-of-income-tax-act>

<sup>923</sup> <https://www.mondaq.com/india/income-tax/1608608/applicability-of-section-43bh-of-the-income-tax-act-1961-on-payments-to-msme>

<sup>924</sup> <https://www.financialexpress.com/budget/msme-fin-budget-2023-may-end-msmes-delayed-payment-crisis-proposes-to-amend-section-43b-of-income-tax-act-check-details-2968381>

By bearing a post-legislative evaluation, the study moves beyond the conventional supposition that the enactment of a provision automatically ensures the protection of micro and small enterprises. Section 43B(h) was introduced with the stated ideal of strengthening payment discipline and perfecting liquidity for MSMEs by linking Tax deductibility to timely payments. still, the factual impact of this provision can only be assessed by examining how Tax authorities, businesses, adjudicators, and MSMEs themselves respond to it in practice. The study thus highlights the gap that frequently exists between legislative design and institutional prosecution, an issue that's constantly overlooked in traditional doctrinal Tax analysis.

Another important donation of this study is its reframing of MSME protection as a system-design challenge rather than a problem of individual non-compliance. Delayed payments to MSMEs are frequently attributed to the disinclination or negligence of buyers, but this explanation is deficient. The study underscores that institutional sins similar as limited enforcement capacity, fractured disagreement resolution mechanisms, lack of collaboration between Tax and MSME authorities, and information asymmetries play a decisive part in lacing the intended benefits of Section 43B(h). By drawing attention to these structural issues, the study encourages a more nuanced understanding of nonsupervisory effectiveness that goes beyond condemning taxpayers or businesses for non-adherence.<sup>925</sup>

The applicability of this analysis extends to policymakers who are engaged in designing or reforming financial and non-supervisory fabrics. Laws affecting MSMEs are frequently legislated with strong weal objects, but without sufficient attention to how they will be enforced, covered, and executed. This study provides policymakers with perceptivity into the significance of aligning Tax vittles with executive realities and

institutional capacities. It suggests that effective MSME protection requires not only well-drafted bills but also probative enforcement mechanisms, clear guidance, and inter-agency collaboration. similar perceptivity is particularly precious in a frugality where MSMEs play a critical part in employment generation and profitable stability.<sup>926</sup>

The study also holds significance for courts and quasi-judicial bodies that are decreasingly called upon to interpret and apply Section 43B(h). Judicial interpretation frequently oscillates between strict statutory construction and intentional approaches. By sticking the provision within its broader nonsupervisory and institutional environment, the study offers courts a richer logical frame for understanding the provision's objects and practical counter accusations. This can prop in developing interpretations that balance profit considerations with the legislative intent of guarding MSMEs, thereby contributing to further coherent and harmonious justice.

For scholars and experimenters, the study adds value by demonstrating the significance of post-legislative analysis in Tax and nonsupervisory education. It challenges the dominance of purely doctrinal approaches and lawyers for an evaluative system that considers issues, institutional behavior, and systemic constraints. In doing so, it opens avenues for interdisciplinary exploration<sup>927</sup> that combines Tax law, nonsupervisory proposition, and public administration. Overall, the study's significance lies in its capability to broaden the discussion on Section 43B(h) from a question of legal compliance to one of nonsupervisory design and institutional performance, making it a meaningful donation to contemporary financial and nonsupervisory converse.

<sup>925</sup> <https://www.cbfnludelhi.in/post/assessing-the-overreach-a-critique-of-section-43b-h-of-the-income-tax-act-1961>

<sup>926</sup> <https://www.tandfonline.com/doi/full/10.1080/13572334.2020.1780008>

<sup>927</sup> <https://ials.sas.ac.uk/ials-blog/browse-past-posts/effective-legislation-and-post-legislative-scrutiny>

## 9. Conclusion

Section 43B(h) marks a significant shift in the legislative approach toward long-standing payment detentions faced by micro and small enterprises, a problem that has still distorted marketable connections for decades. By linking the allowability of expenditure under the Income Tax Act directly to timely payment scores under the MSMED Act, the provision seeks to move beyond emblematic protection and introduce a palpable profitable consequence for defaulting buyers. In substance, it attempts to correct a structural imbalance where small suppliers, despite being fairly defended, frequently demanded the logrolling power or coffer to apply their rights. The denial of Tax deduction for delayed payments is intended to serve as an interference<sup>928</sup>, nudging larger and financially stronger realities toward further disciplined payment behavior and, in turn, perfecting cash inflow certainty for lower enterprises still, while the intent behind Section 43B(h) is plainly corrective, its effectiveness cannot be judged in insulation from the broader marketable and institutional ecosystem in which it operates. The provision assumes that statutory disallowance alone will restate into behavioral change, but business practices are shaped as important by contractual morals and request realities as by Tax consequences. In sectors where long credit cycles are customary, the unforeseen severity introduced by this section may produce disunion rather than compliance. Buyers may respond by renegotiating terms, reducing procurement from registered micro and small enterprises, or restructuring deals in ways that adulterate the practical benefit of the law. similar issues, though unintended, threat undermining the veritably class the provision seeks to cover.

Another area of concern lies in the absence of sufficient contractual and procedural clarity. numerous marketable arrangements with micro and small enterprises operate without detailed

written agreements, counting rather on purchase orders or informal understandings. In similar cases, determining the exact date of acceptance, the applicable credit period, and the point at which disallowance is touched off becomes contentious. This query exposes businesses to action and interpretational controversies, particularly during Tax assessments, where factual nuances may be viewed else by taxpayers and authorities. Without clearer alignment between marketable attestation norms and statutory prospects, Section 43B(h) may inadvertently increase compliance threat rather than reduce dereliction.<sup>929</sup>

From a financial and executive viewpoint, the provision also raises questions of collaboration between Tax enforcement and enterprise regulation. While the MSMED Act provides mechanisms for disagreement resolution through Facilitation Councils, these processes remain largely descendant - driven and are frequently underutilized due to time and cost constraints. Section 43B( h), on the other hand, operates automatically through the Tax system, without reference to whether a payment disagreement is genuine or queried. This creates a script where Tax disallowance may do indeed in cases of bona fide disagreement over quality, volume, or performance, thereby straining liquidity for the buyer without inescapably perfecting issues for the supplier.

For the law to achieve its defensive pledge, it must be supported by reciprocal institutional design and policy consonance. Greater mindfulness and standardization of written contracts, clearer guidance on conciliation between marketable controversies and Tax consequences, and bettered integration between MSME facilitation mechanisms and Tax administration are essential. Inversely important is a balanced enforcement approach that recognizes the diversity of business models and credit practices across diligence<sup>930</sup>. Without

<sup>928</sup> <https://taxguru.in/income-tax/section-43bh-income-tax-act-law-intention-application-loopholes.html>

<sup>929</sup> <https://www.mondaq.com/india/income-tax/1608608/applicability-of-section-43bh-of-the-income-tax-act-1961-on-payments-to-msme>

<sup>930</sup> <https://cleartax.in/s/section-43bh-of-income-tax-act>

similar systemic support, Section 43B(h) risks getting a blunt instrument well- intentioned, but uneven in its impact.

In conclusion, Section 43B(h) reflects a decisive legislative trouble to address settled payment asymmetries affecting micro and small enterprises, motioning a shift from unresistant protection to active profitable enforcement. Yet, statutory intent alone cannot ensure success. Unless corroborated by institutional collaboration, contractual discipline, and realistic financial administration, the provision may induce query and liquidity stress rather than sustainable reform. A system acquainted approach, rather than a purely corrective one, is thus essential to restate the law's ideal into meaningful and continuing protection for micro and small enterprises.

