MSME PAYMENT SECURITY LAWS AND RECOVERY OF DELAYED DUES

Sneha Pandit*

INTRODUCTION

What happens when the economic backbone of nation begins to crack under the burden of delayed payment and financial insecurity faced by the MSME the MSME stands for the micro small medium Enterprises the words codified under ‘section 7 of MSMED Act the MSME are managed under the ministry of MSMEs MSME classified based on their turnover micro have net turnover up to 5 crores of macro businesses the small business have turnover up to 50 crores and medium business have net turnover up to 250 crores according to MSME ministry.

DEFINITION AND SCOPE

The operational survival of MSMEs arises due to negative cash flow, delayed payments, and the debt trap of borrow money union ministry’s samadhan portal reveals that MSMEs are trapped in systemic red tape and complex administration. This same issue also presented in MSME IN the IBC of march report stated MSME already struggle with delayed payments and ineffective legal remedies resorting to the IBC often compounds risk their claims may appear modest in absolute terms recovering dues is often critical to the MSME’s survival[3] before flaws move to actual law and section the legislature enacted the MSMED act 2006 its sub sections as chapter V, section 15, 16 under section 2(d) section 18,19,23 section 43(h) of income tax act 1961, finance act 2023 amendment.

RESEARCH QUESTIONS

1. To what extent does the statutory definition of a ‘’buyer’’ under ‘’section 2(d) of MSMED 2006’’ effectively hold large private corporations and public sector undertakings (PSUs) accountable for delayed payment in practice?

*BA LLB, SECOND YEAR, MODERN LAW COLLEGE.

2. How effective is the compounding triple interest penalty mandated under section 16 as an effective financial deterrent against payment defaults, given the asymmetric bargaining power inherent between buyers and MSMEs?
3. What systemic institutional and procedural bottlenecks within the Micro and small enterprises facilitation councils MSEFC impede the resolution of payment disputes within the statutorily prescribed timeframes?
4. How has the judiciary interpreted the overriding nature of the MSMED Act through landmark precedents regarding arbitration and statutory compliance?
5. How does the introduction of section 43B (h) of the Income Tax Act 1961 interface with the MSME Act to enforce corporate payment Compliance?

LEGAL FRAMEWORK

To evaluate the operational friction within the recovery pipeline it is essential to parse the mandatory machinery established under chapter V of the MSMED act 2006 titled delayed payment to micro and small enterprises the primary shield for small enterprises the primary small suppliers is section 15 which aggressively curtails traditional contract terms to protect the economically weaker party under this provision b where a suppliers supplies any goods or services to any buyer the buyer shall make a payment therefor on or before the date agreed upon between him and the supplier in writing or, where there is no agreement in this behalf before the appointed date according to official act the statute strictly caps this contract freedom declaring that in no case the period agree upon between the supplier and the buyer in writing shall exceed forty-five days from the days from the day of acceptance.

To enforce compliance section 16 introduces a severe financial deterrent if a buyer fails to make payment within the mandated timeline the ‘’buyer shall notwithstanding anything contained in any agreement between the buyer and the supplier or in any law for the time being in force be liable to pay compound interest with monthly rests to the supplier on that amount from the supplier on that amount from the appointed day or as the case may be from the date agreed upon at three times of the bank rate notified by the reserve bank because section 2(d) defines buyer using the absolute term ‘’whoever’’ this heavy financial liability applies uniformly to private corporation public sector undertakings (PSUs) and government departments alike.

This payment security framework is provided by the Finance Act 2023, which inserted section 43B (h) of the Income Tax Act 1961. The amendment forces buyers to clear dues within 45 days to avoid heavy tax penalties; this ensures timely payment.

CASE LAW ANALYSIS

The operational security of the delayed payment framework relies on a robust judicial architecture established across six foundational supreme court judgment the core principle of statutory supremacy was cemented in Silpi Industries v IRCTC, which leveraged the non-obstante mandate of section 24 to rule that chapter V operates as a special legislative shield overriding general statutes like the arbitration and conciliation act 1996 this anti evasion stance was reinforced in Gujarat State Civil Supplies Corporation Ltd v Mahakali Food Pvt. Ltd. 2023 confirming that private contracts cannot divest the facilitation council MSEFC its exclusive jurisdiction under section 18 to block corporate stalling tactics Gujarat State Disaster Management Authority v Aska Equipments Ltd. 2021 interpreted the section 19 75% pre deposit rule as an absolute non-waivable jurisdictional bar for appellate courts.

Conversely the judiciary introduced strategic thresholds to enforce commercial discipline and prevent systemic exploitation in vaishno enterprises v Hamilton Medical AG the court established a strict temporal limit holding that chapter v protections apply exclusively to transactions executed after formal MSME registration this boundary was refined in m/s sonali power Equipments Pvt. Ltd. v Chairman MSEB, which drew a sharpen structural distinction between section 18(2) conciliation exempt from the Limitation Act 1963 and section 18(3) statutory arbitration which remains bound by strict limitation deadlines synthesized with shanti conductors Pvt. Ltd. v Assam State Electricity Board, which recognized the three times bank rate penal interest as an absolute substantive right attaching automatically by operation of law the judicial trajectory is clear the supreme court aggressively enforces rapid financial recovery for small suppliers but demands rigorous procedural compliance to prevent the machinery from being weaponized to resurrect stale commercial claims.

CRITICAL EVALUATION

The article’s main argument is that the judiciary has fortified the protections of chapter v profound systemic gap persists between statutory design and institutional reality the primary inadequacy lies in the acute operational backlog choking the micro and small enterprises facilitation councils MSEFC although section 18(5) explicitly mandates that references must be decided within ninety administrative under staffing and soaring corporate defaults render this timeline purely illusory furthermore non-compliant buyers routinely exploit the structural ambiguity surrounding the transition from conciliation section 18(2) to formal arbitration under section 18(3) to orchestrate endless procedural delays by stalling the final award buyers successfully evade the seventy-five percent pre-deposit mandate of section 19 turning a rapid recovery mechanism into an exhausting administrative hurdle that actively freezes vital MSME liquidity.

This structural vulnerability becomes clearer when evaluated against global alternatives in the United Kingdom under the late payment of Commercial Debts (Interest) Act 2006 the landmark decision of the English high court in Ruttle Plant Hire Ltd v Secretary of State established that the statutory right to late-payment interest cannot be structurally frustrated or contracted out by a buyer raising late unquantified counterclaims or procedural technicalities however while the UK model relies on a decentralized self-executing statutory framework that enforces immediate contractual accountability through ordinary commercial avenues the Indian model creates an internal inconsistency. It mandates aggressive public policy intervention through the MSEFC but fails to provide the infrastructural capacity to support it, forcing economically weaker suppliers to choose between lengthy institutional gridlock or damaging commercial relationships. Corporate buyers' counterclaims cannot justify this structural injustice.

CONCLUSION

The MSMED Act, 2006 provides a strong statutory framework for protecting Micro and Small Enterprises against delayed payments by imposing strict payment timelines, compound interest liability, and a specialised dispute-resolution mechanism through the MSEFC. The judicial approach examined in this article demonstrates that the Supreme Court has consistently strengthened these protections while also requiring strict compliance with statutory and procedural requirements. The interaction of Section 43B(h) of the Income Tax Act with the MSMED framework further reflects an attempt to promote timely corporate payment practices.

However, the effectiveness of these safeguards remains significantly constrained by institutional delays and procedural bottlenecks. Although Section 18(5) envisages expeditious resolution, administrative understaffing, increasing defaults, and procedural disputes can prevent MSMEs from obtaining timely recovery of their legitimate dues. The gap between the statutory design and its implementation therefore continues to undermine the very objective of providing liquidity and financial security to small enterprises.

The comparative discussion also indicates that India's framework requires greater institutional capacity and procedural efficiency to translate statutory rights into effective remedies. While the existing legal regime imposes substantial obligations upon buyers, delayed adjudication can compel MSMEs to bear the economic consequences of prolonged disputes and may even affect their commercial relationships.

Therefore, the MSMED payment-security framework must evolve beyond merely imposing substantive liabilities and focus equally on preventing procedural abuse and institutional delay. Strengthening MSEFC infrastructure, ensuring adherence to statutory timelines, discouraging dilatory tactics, and making the recovery mechanism more efficient would help transform the MSMED Act from a theoretical statutory shield into an effective instrument of economic justice and financial security for MSMEs. This would also give practical effect to the article's central argument that procedural bad faith must be addressed alongside payment defaults.

REFERENCES

- Micro, Small and Medium Enterprises Development Act 2006, s 7
- Ministry of Micro, Small and Medium Enterprises annual report 2025-26
- Micro, small and medium enterprises in IBC March 2026 report
- Micro, small and medium enterprises development act, 2006 ch V ss 15,16,18,19,23 finance act 2025
- MSMED Act 2006 ch V
- MSMED Act, 2006 ss 15
- MSMED Act 2006 ss 16
- MSMED Act 2006 s 16 and s 2(d)
- Income-tax Act, 1961 s 43B (h)
- Silpi Industries v Kerala State Road Transport Corporation [2021] ssc 790
- Gujarat state civil supplies corporation Ltd v Mahajali food Pvt Ltd [2023] 401
- Gujarat State Disaster Management Authority v Aska Equipments Ltd [2021] SCC 693
- Vaishno Enterprises v Hamilton Medical AG [2023] ssc 401
- Sonali Power Equipments v Chairman, MSMB [2025] ssc 1
- Shanti Conductors v Assam State Electricity Board [2019] SCC 529