Recent developments in CSR landscape, tax and regulatory considerations

October 2021

Building a better working world

Glossary

Term	Definition
AOGPU	Advancement of objects of general public utility
CA 2013	Companies Act 2013
CARO	Company Auditor's Report Order
CBDT	Central Board of Direct Taxes
CFO	Chief Financial Officer
CSR	Corporate Social Responsibility
CSR Rules	(Corporate Social Responsibility Policy) Rules, 2014 read with Companies (Corporate Social Responsibility Policy) Amendment Rules, 2021
FAQ	Frequently Asked Questions
FC	Foreign Contribution
FCRA	Foreign Contribution Regulations Act, 2010

Term	Definition
FY	Financial Year
GN	Guidance Note
ICAI	The Institute of Chartered Accountants of India
ITA	Income Tax Act
NPO	Non Profit Organizations
PY	Previous Year
SBI	State Bank of India
SOP	Standard Operating Procedure
u/s	Under Section
w.e.f	With Effect From

Webinar

Recent developments in CSR landscape, tax and regulatory considerations

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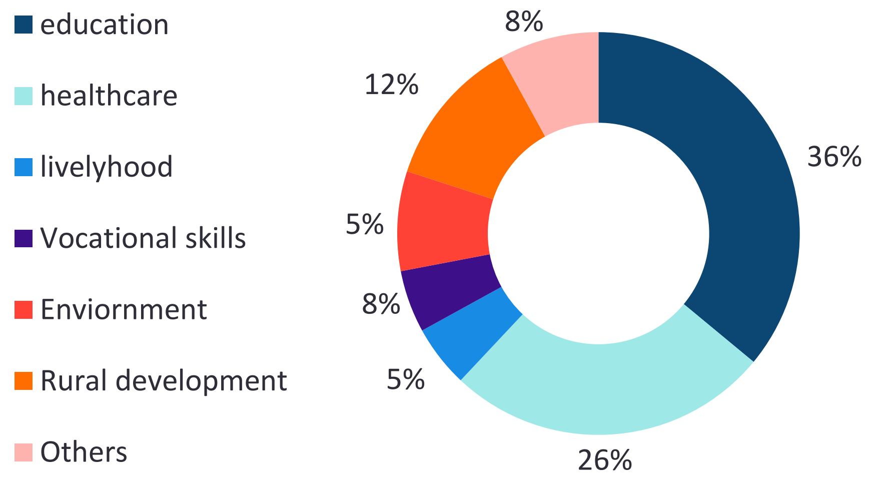
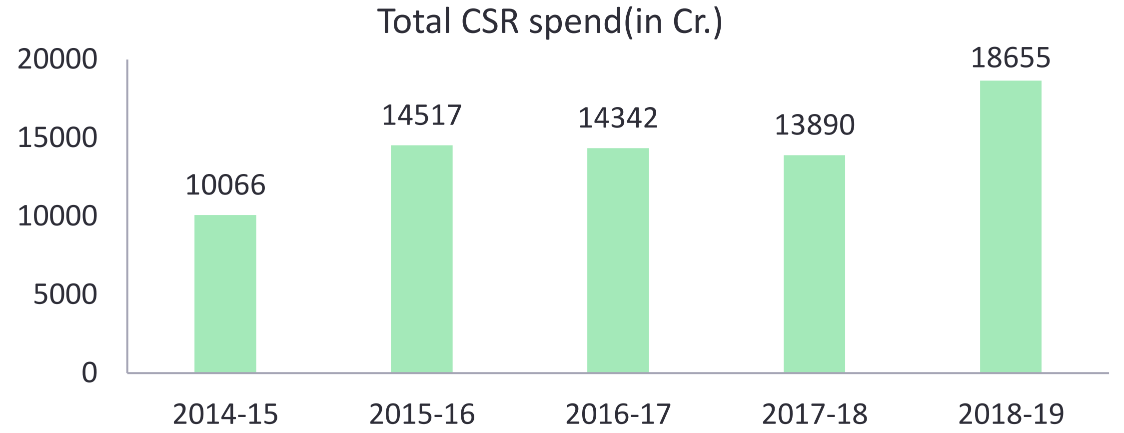
Corporate India:
CSR and its tax deductibility

EY

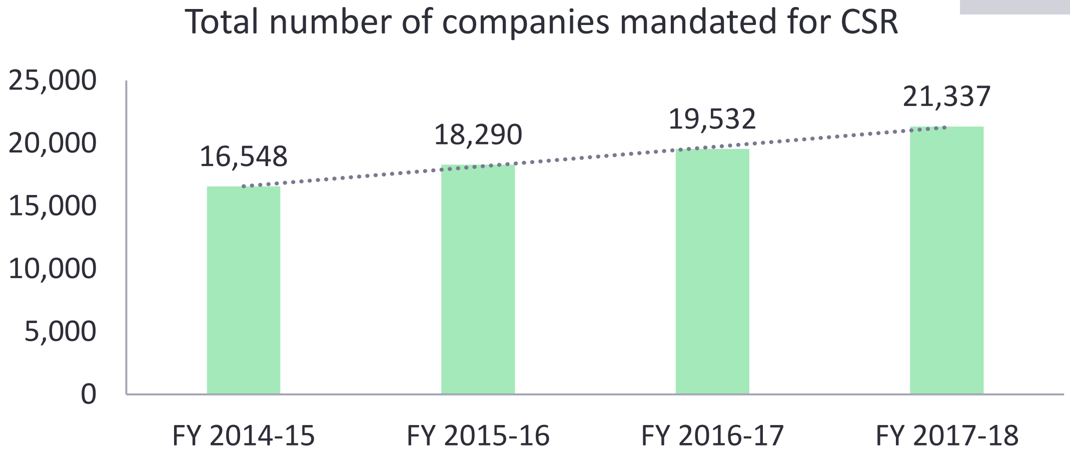
Compliance and CSR spend trends in India since 2014-15

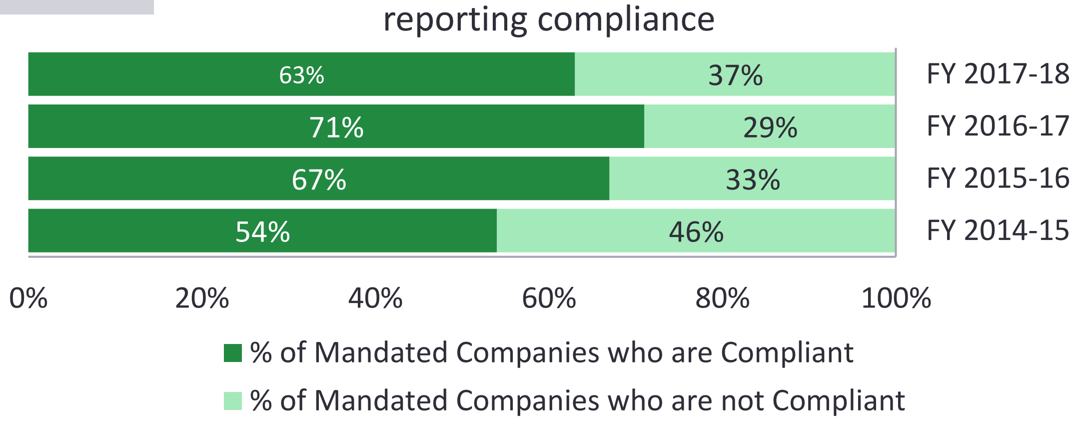
CSR spend





CSR reporting





Source: Ministry of Corporate Affairs, 2019

CSR – Key amendments under Companies Act

Definitions under CSR rules

- CSR - Negative list included
- CSR policy – Focus on approach & direction to select, implement, monitor CSR
- Ongoing projects- multi-year project not exceeding 3 FYs

Disclosures and reporting

- Display of specified information on the website made mandatory
- Enhanced disclosures in the CSR Annual Report
- Clause XX of CARO 2020 – treatment of unspent amount depending upon nature of the project (Ongoing or other than ongoing)

CSR implementation

- Implementation agencies registration under ITA and CA 2013
- Inclusion of international organizations to design, monitor and evaluate the CSR projects as well as capacity building
- Board to satisfy itself on the utilization of funds and to get CFO or person alike certification for the same

Formulation of annual action plan

- List of CSR projects
- Manner of execution
- Modalities of utilization of funds and implementation Monitoring and reporting
- Impact assessment

CSR expenditure

- No direct ownership of CSR assets created/ acquired
- Transfer of unspent amounts (to be recorded as liability)
- Penalty introduced- company and every officer of the company
- Carry forward of excess spend (to be recorded as prepaid asset)
- Impact assessment introduced

MCA issued FAQs on CSR vide General Circular No. 14/2021 on 25 August 2021 in supersession of earlier issued FAQs and for clarifying various issues related to CSR as per the amendments.

CSR – Amendment in disclosures in Schedule III

Current practice

As per GN to Schedule III, following shall be disclosed:

- Gross amount required to be spent during FY
- Amount spent on:
  - Construction / acquisition of any asset and
  - On purpose other than above
- Details of related party transactions in relation to CSR activities
- Movement of provision (created on account of shortfall)

Amended Schedule III

The following shall be disclosed in relation to CSR:

- Amount required to be spent during FY
- Amount of expenditure incurred
- Shortfall as at year end
- Total of PYs shortfall
- Reason for shortfall
- Nature of CSR activities
- Details of related party transactions in relation to CSR activities
- Movement of provision (created on account of shortfall)

Key consideration

- CSR is now a legal obligation after the amendment to the CSR provisions requiring an entity to deposit unspent amounts.
- Entities need to be careful that business expenses are not mis-represented as relating to CSR.
- As per ICAI FAQ on Accounting for amounts to be incurred towards Corporate Social Responsibility (CSR) pursuant to the Companies (Corporate Social Responsibility Policy) Amendment Rules, 2021, CSR expenses are expensed as incurred, and at end of year, provision is made for unspent amount.

Disclosure requirement as per amended schedule III

- No specific format is prescribed.

Implementation steps

1 Review the CSR Policy and assess if it complies with the new requirements

2 Refresh the roles of Board / CSR Committee / CFO and set-up new SOPs

3 Compute the CSR obligation for the FY

4 Identify CSR activities and mode of implementation for the FY

5 Formulate the annual action plan, engage formally with qualifying Implementation Agencies

6 Implement the projects and regularly monitor the activities / spend; CFO to certify annual spend

7 Assess the total underspend/ excess spend at the end of FY and its treatment under Tax, Accounting and Company law

8 Evaluate and finalize the additional disclosures in the annual report/ website

CSR expenses – tax deductibility

Allowability of expense u/s 37(1)

As per explanation 2 to Section 37(1) of the ITA, any expenditure incurred on the activities relating to corporate social responsibility referred to in section 135 of the CA 2013 shall not be deemed to be an expenditure incurred by the assessee for the purposes of the business or profession. Key consideration are as under:

- Claim for deduction for CSR expenditure incurred in excess of minimum 2% stipulated under section 135
- Claim for deduction for CSR expenditure incurred CSR provisions are not applicable on taxpayer due to threshold limits

80G deduction

Where a company make CSR contribution to an implementing agency registered u/s 80G of ITA, though the CSR Expenditure is disallowed under section 37 of ITA, the company may claim deduction under section 80G on the basis of receipts/certificates issued by such organization. Key consideration are:

- Any company opted for a concessional tax rate of 22% u/s 115BAA of the Act will not be entitled to claim deduction under section 80G with respect to the CSR Expenditure

NPOs/ Implementing agencies: key considerations

Overhaul of tax exemption registration process

As per the erstwhile provisions, registrations/ approvals granted to charitable institutions for claiming exemptions were irrevocable except where the conditions for claiming exemptions were violated

W.e.f. 1 April 2021, ***New Provisions*** to apply for ***Registration*** u/s 12AB of the ITA

Registration u/s 12AB

- **Application** for re-registration u/s 12AB within 3 months from 1 April, 2021 (extended till 31 March 2022)
- **Automatic approval** granted for a period of 5 Years
- **For re-registration** 6 months prior to expiry of 5 years in case of existing registered NPOs

- **Application** to be made at least 1 month prior to FY relevant to AY for which registration sought
- **Provisional approval** for 3 years commencing from AY from which registration is sought
- **For re-registration** 6 months prior to expiry of 3 years or within 6 months of commencement of activities in case of new NPOs

- In case of adoption or modification of objects, application for registration within 30 days therefrom
- In any other case, application for registration to be made 1 month prior to the commencement of the previous year

The CBDT vide notification No. 19/ 2021 dated 26 March 2021 has notified rules and forms for tax registrations by trusts/ institutions under the ITA. bb

Note: Similar amendments have been made in the registration process specified for charitable institutions covered under section 10(23C) and 80G of ITA

Possible consequences/ risks of non-compliance

1. Delay in filing applications for re-registrations can jeopardize the tax exemptions granted to charitable institutions and donors under section 12A/ 12AA and section 80G of ITA respectively

2. Risk of increased enquiries and scrutiny under other laws applicable to the charitable institutions (like FCRA, 2010, Indian Trust Act, 1882, CA, 2013 etc)

3. Reputational damage, regulatory non-compliance and loss of tax exemptions for companies having their own foundations as a CSR vehicle

CSR expenses – tax deductibility

Violation of any material law

Provisions of ITA [Sec 12AA(4)(b) or 12AB(5)(b)]:

- Non-compliance with requirement under any other law, which is material to achieve objects
- Order, direction or decree holding such non-compliance has attained finality or is undisputed

Impact on trigger :

- Power to revoke 12AA/12AB registration exists
- Consequently, exit tax provisions u/s 115TD of the ITA, could trigger

Action points:

- Assess applicable laws/ regulations
- Robust internal controls to undertake timely compliance

Advancement of objects of general public utility

Provisions of ITA [Sec 2(15) read with 13(8)]:

- "Charitable purpose" does not include AOGPU;
- If trade, business or commerce is undertaken or fee charged for an activity in the course of undertaking AOGPU
- Aggregate receipts exceed 20% of total receipts

Impact on violation:

- Denial of exemption u/s 11 of ITA

Action points:

- Determine trading receipts and compliance with 20% threshold

Finance Act 2021 – key amendments

Corpus donation*

- Any corpus donation received by charitable trust was earlier exempt from 85% application rule. Now, this exemption is available only if such corpus donation is specifically invested or deposited into any of the prescribed modes under the ITA.
- Any application out of corpus shall not be considered as application for charitable or religious purposes. However, if any amount is deposited or invested back in the corpus funds from out of income of any year, the same shall be regarded as application of that year.

Loan or borrowings

- Any application from loans or borrowings shall not be regarded as application for charitable or religious purposes. However, repayment of loan or borrowing from out of income of any year shall be regarded as application of income in the year of repayment.

**Contribution towards corpus fund of implementing agencies will not qualify as CSR spend.*

Foreign Contribution (Regulation) Act, 2010

Background

- CSR implementing agencies wish to receive foreign contributions needs to obtain registration under the FCRA which permits registered/ approved entities to receive FC, subject to strict conditions and disclosures.
- The enforcement of FCRA provisions have become stringent over the years and the NPOs are being subject to a lot of scrutiny.
- The Central Government has amended certain provisions of the FCRA vide the Foreign Contribution (Regulation) Amendment Act, 2020 ('Amendment Act') on 29 September 2020.
- The amendments brought in are wide, ranging from:
  a) restrictions on transfer of foreign contributions;
  b) cap on administrative expenditure incurred by the NPO;
  c) receipt of foreign contributions only in a designated SBI account; etc.
- Given the strict enforcement and stringent penalties for violation of the FCRA provisions, it might be imperative for NPOs to review the impact of these far-reaching amendments and re-look at their compliance and risk mitigation strategy.

1 Prohibition on transfer of FC to any other person

2 Lowering the cap on admin expenses

3 Designated FCRA Bank Account with SBI

4 Power to prohibit a FC recipient from utilising/receiving funds

5 Power to prohibit a FC recipient from utilising/receiving funds

6 Scrutiny at the time of renewal

7 Permits surrender of certificate

Key amendments in FCRA

1. The transfer of FC to any other person is now prohibited.
2. A person who receives FC must use it only for the purpose for which the FC is received. They must not defray more than 20% (earlier limit 50%) of the FC for meeting administrative expenses.
3. FC must be received only in an account designated by the bank as ‘FCRA account’ in SBI, New Delhi. Another FCRA account may be opened for keeping or utilizing the received contribution.
4. If a person accepting FC is “found guilty” of violating any provisions of the FCRA, the unutilized/ unreceived FC could be utilized/ received, only with the prior approval of the government. The Amendment Act now empowers Government to restrict usage of unutilized FC if, based on “summary inquiry the Government has a reason to believe” that such person has contravened provisions of the FCRA.
5. Under the FCRA, certain persons are prohibited to accept FC. The Amendment Act has added “Public servants” (as defined under the Indian Penal Code) to the list. The term “Public servant” includes any person who is in service or pay of the government, or remunerated by the government for the performance of any public duty.
6. The Amendment Act provides that the government may conduct a scrutiny of the organization at the time of the renewal of the registration. This lays greater emphasis on book keeping and internal controls.
7. The Amendment Act enables the central government to permit surrender of registration certificate, post inquiry.

Amendments in FCRA – key impact areas

	1	2	3
Key amendments	Prohibition on transfer of FC received by a FCRA registered person to another person	Cap on administrative expenses lowered from 50% to 20% of FC received in a financial year	Designated FCRA bank account with SBI for receipt of FC
Potential impact	▶ Transfer of FC to other FCRA registered NPOs was permitted under the earlier law ▶ Earlier structures involving nodal organizations receiving and transferring funds would be impacted as onward transfer of FC is now prohibited ▶ NPOs need to consider the amendments in their FC structures as well as operating models and existing contractual agreements	▶ Lowering of the cap on admin expenses could impact the quality/ functioning of the NPOs ▶ NPOs may need to segregate the amount of administrative expenditure vs amount of project cost on scientific basis to ensure that the threshold is not breached ▶ Definition of "administrative expenses" under the FCRR to be carefully interpreted while segregating expenditure ▶ Impact on funds flow for on-going projects to be considered	▶ NPOs are required to open FCRA account with the SBI main branch ▶ Centralizing of account opening could increase the overhead costs of NPOs ▶ This change could further increase the transparency in fund flow and any non-compliances could be scrutinized closely by the authorities

Caution Point : For administrative ease, organizations to ensure that CSR contribution is not disbursed in FCRA account(s) of implementing agencies which is being regulated under FCRA.

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