

Donation under CSR - Is it Eligible for Sec.80G Deduction?

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The concept of social responsibility can be traced back to ancient times. In earlier days, there was a religious tradition of daan and seva, which operated in India, helping to shape the relationship between the privileged and the deprived. Majority of the philanthropic activities were carried out by the religious institutions, which also continues till date. In the early 19th century, corporate bodies started doing this activity through trusts and institutions, controlled by members of business families. After the opening of the Indian economy in the year 1991, there was a fundamental shift from the philanthropy mode to multistakeholder approach, whereby the companies were also responsible to all their stakeholders, including employees and community. It is a fact that corporate social responsibility ('**CSR**') benefits the society at large and also to the company in many ways, i.e. in terms of brand recognition, reputation, increased sales and customer loyalty, better financial performance, greater ability to attract talent and retain staff, organisational growth, easier access to capital, etc.

Till the year 2013, there was no legislated CSR in India. It was only on August 29, 2013, CSR was legislated by introducing section 135 in the Companies Act, 2013 ('**CA 2013**'), which was made applicable from the financial year 2014-15. Infact, India has been the first country to legally mandate CSR and then the journey began. The total CSR expenditure in the financial year 2018-19 was Rs. 11,867 crores^[1], which has been the highest spent by the corporates and we feel proud to be a part of such nation.

The question that has always been litigated is whether expenditure on CSR activity is eligible for tax deduction under the Income Tax Act, 1961 ('**IT Act**'). After CSR was made mandatory for prescribed corporates, another facet of the litigation has emerged with reference to donations made as part of CSR obligation. In this Article, we have highlighted the recent controversy that has ignited for allowability of deduction under section 80G of the IT Act for the CSR qualifying donation.

What is Corporate Social Responsibility under the CA 2013?

CSR provisions are presently applicable to companies with an annual turnover of Rs. 1,000 crore and more, or a net worth of Rs. 500 crore and more, or a net profit of Rs. 5 crore and more. Accordingly, qualifying company is mandated to spend 2% of the average profits of the last three years on CSR activities.

CSR has been defined in Companies (Corporate Social Responsibility Policy) Rules, 2014 ('Rules') in an inclusive manner as follows:

Corporate Social Responsibility (CSR) means and includes, but is not limited to -

- (i) Projects or programmes relating to activities specified in Schedule VII to the Act; or*
- (ii) Projects or programmes relating to activities undertaken by the Board of Directors of a company (Board) in pursuance of recommendations of CSR Committee of the Board as per declared CSR Policy of the company subject to the condition that such policy will cover subjects enumerated in Schedule VII of the Act .*

Additionally, under the CA 2013, there are separate regulations provided for CSR committee, functions to be formed by the committee, functions of the Board, ways to carry on the CSR activities, disclosure of the CSR expenditure in the annual accounts, etc.

Tax Deductibility for CSR expenditure

Prior to 2013, some of the voluntary CSR activities took the form of contributions for establishing a medical college^[2], installation of traffic signals^[3], public welfare scheme^[4], establishing drinking water facilities^[5], etc. Such activities, when found to be having nexus with the business of the taxpayer and were incurred wholly and exclusively for the purpose of the business, were allowed as a tax deductible expenditure. In a few other instances, the expenditure incurred on the CSR activities were not allowed as a deduction, but were eligible for deduction under section 80G, subject to meeting the conditions therein.

However, having regard to the fact that CSR expenses have a philanthropic nature and were not necessarily a business expense, the Parliament legislated that CSR expenses would not be eligible for deduction under section 37 of the IT Act. For this purpose, Explanation 2 to section 37(1) was inserted vide the Finance (No 2) Act, 2014 (applicable from the assessment year 2015-16), which provided that any expenditure incurred by an assessee on the activities relating to CSR referred to in section 135 of CA 2013, shall not be deemed to be an expenditure incurred by the assessee for the purpose of business or profession and shall not be allowed as deduction under section 37(1) of the IT Act. The intent of Parliament in bringing the said provision is given in the Explanatory Memorandum to the Finance (No.2) Bill, 2014 and is reproduced as under:

CSR expenditure, being an application of income, is not incurred wholly and exclusively for the purposes of carrying on business. As the application of income is not allowed as deduction for the purposes of computing taxable income of a company, amount spent on CSR cannot be allowed as deduction for computing the taxable income of the company. Moreover, the objective of CSR is to share burden of the Government in providing social services by companies having net worth/turnover/profit above a threshold. If such expenses are allowed as tax deduction, this would result in subsidizing of around one-third of such expenses by the Government by way of tax expenditure.

The existing provisions of section 37(1) of the Act provide that deduction for any expenditure, which is not mentioned specifically in section 30 to section 36 of the Act, shall be allowed if the same is incurred wholly and exclusively for the purposes of carrying on business or profession. As the CSR expenditure (being an application of income) is not incurred for the purposes of carrying on business, such expenditures cannot be allowed under the existing provisions of section 37 of the Income-tax Act. Therefore, in order to provide certainty on this issue, it is proposed to clarify that for the purposes of section 37(1) any expenditure incurred by an assessee on the activities relating to corporate social responsibility referred to in section 135 of the Companies Act, 2013 shall not be deemed to have been incurred for the purpose of business and hence shall not be allowed as deduction under section 37. However, the CSR expenditure which is of the nature described in section 30 to section 36 of the Act shall be allowed as deduction under those sections subject to fulfillment of conditions, if any, specified therein.

Thus, it is a clear that the CSR expenditure referred to in section 135 cannot be claimed as a tax deductible expenditure under section 37(1) of the IT Act. However, CSR expenditure, which is of the nature described under sections 30 to 36 of the IT, was allowable as a deduction, say CSR expenditure laid out or expended on Scientific Research related to the business is allowable under section 35(1)(i) and

35(1)(iv), etc.

As an aside, it may be mentioned that there have been conflicting views whether the Explanation to section 37(1) is retrospective or prospective in its operation.

Expenditure on CSR could take many forms. There could be expenditure on projects directly undertaken by companies, such as setting up and running schools, social business projects, etc. Such expenditure would include expenditure otherwise falling for consideration under section 37(1) of the IT Act. On the other hand, companies, instead of undertaking or participating directly in a project, may choose to give donations to institutions that are engaged in undertaking such projects. While expenditure falling within the ambit of section 37(1) would undoubtedly not qualify, the issue is whether donations, which indirectly help to meet the CSR obligation, would qualify for deduction under section 80G, if the donation otherwise satisfies the conditions laid down in that section.

A Controversy - Whether deduction under section 80G is allowable for CSR contribution?

After the amendment, some tax authorities have disputed the claim of deduction under section 80G for eligible donations, qualifying for CSR under the CA 2013. The tax authorities contend that the intention of the legislature was never to allow deduction for CSR expenditure, else it would result in subsidizing the CSR expenditure by one-third amount. Furthermore, CSR expenditure is not 'voluntary', but 'mandatory' in nature.

Taxpayer's Arguments

The taxpayer can make the following arguments to support their claim for deduction under section 80G:

a) Section 80G(1) provides that in computing the total income of the assessee, there shall be deducted, in accordance with the provisions of this section, such sum paid by the assessee in the previous year as a donation. Further, section 80G(2) list down the sums on which deduction shall be allowed to the assessee. Section 80G falls in Chapter VIA, which comes into play only after the gross total income has been computed by applying the computation provisions under various heads of income, including the Explanation 2 to section 37(1).

Thus, there is no correlation between section 37(1) and section 80G. Principles governing what is not allowable under section 37(1) have been explained in the section itself (i.e. what is allowable, the conditions subject to which it is allowable, the extent to which it is allowable) and also what is not allowable under section 80G.

b) Section 80G specifically mentions two instances (viz, section 80G(2)(a)(iihk) and (iihl), i.e., contributions towards Swacha Bharat Kosh and Clean Ganga Fund), where CSR expenditure is not allowable as deduction under section 80G.

c) Section 80G(2)(a) allows deduction for '*any sums paid by the assessee in the previous year as donations*'. Thus, the deduction allowable is for sums paid as donation. Donations paid to the said Kosh and Fund are not allowable under section 80G(2)(a)(iihk) and (iihl). What is not allowable is however amounts spent by the assessee in pursuance of CSR in pursuance of section 135 of the CA 2013. Contributions to the said Kosh and Fund are CSR activities included in Schedule VII to the CA 2013. The disallowance for deduction under section 80G vis-à-vis CSR can be restricted only to contributions to these Funds under CSR. It is a well-established rule of interpretation that one has to look merely at what is stated in the statute; there is no scope for intendment in law. So only contributions to these two funds will not qualify for deduction under section 80G(2)(a). There is no blanket ban of deduction under section 80G for donations, which also qualifying under CSR.

d) Furthermore, amid Covid-19 pandemic, the Government had provided various relaxation and measures and also sought contributions to the PM CARE fund to deal with the pandemic. Such contributions are eligible as CSR expenditure under the CA 2013 and for deduction under section 80G of the IT Act. Thus, it can be said that the intent of the legislature is not to restrict deduction under section 80G, even if the contribution qualifies as CSR expenditure under the CA 2013.

e) In the Memorandum to the Finance Bill, it has been clarified that no deduction will be allowed for CSR expenditure as a business expenditure, but makes no reference to ineligibility or restriction in claiming deduction under section 80G for donations made pursuant to CA 2013 obligations. Also, in the Memorandum, it has been clarified that CSR expenses which fall for consideration under sections 30 to 36 of the IT Act are allowable. Thus, a position emerges that the intent of the Legislature was not to blanketly disallow CSR expenses.

f) The Ministry of Corporate Affairs ('MCA') has issued Frequently Asked Questions ('FAQ') through General circular no. 01/2016 dated January 12, 2016 (FAQ No. 6) has clarified that as follows:

Question No. 6: What tax benefits can be availed under CSR?

*Answer: No specific tax exemptions have been extended to CSR expenditure per se. The Finance Act, 2014 also clarifies that expenditure on CSR does not form part of business expenditure. **While no specific tax exemptions have been extended to expenditure incurred on CSR, spending on several activities like Prime Minister's Relief Fund, scientific research, rural development projects, skill development projects, agriculture extension projects etc, which fund place in Schedule VII, already enjoys exemptions under different sections of the Income-tax Act, 1961.***

This clarification issued by one arm of the Government, supports the view that deduction under section 80G is allowable on such contributions.

g) Deduction under section 80G is qua the philanthropic activity for service to the public and society and cannot be denied on the basis of statutory obligation, which in any case will not change the nature of the philanthropic activity.

h) It may be noted that in the case *Escorts Skill Development v. CIT*^[6], the Delhi Tribunal allowed section 12AA and section 80G registration to a captive section 8 company, which was created to redeem CSR obligation of the parent. Thus, the Tribunal have indirectly upheld that contribution of parent company to such a company will be eligible for section 80G and CSR obligation provided the conditions therein are met.

Jurisprudence on allowability of deduction under section 80G

Recently, this issue has been tested in the following decisions:

- In *Goldman Sachs Services Pvt. Ltd. v. JCIT*^[7], the Assessing Officer ('AO'), without verification of the donations, disallowed deduction under section 80G on the basis that the donations were in the nature of CSR expenditure and not in the nature of 'voluntary contribution'. The Bangalore Tribunal observed that the CSR expenditure was required to be incurred as per the CA 2013 and as per the amendment introduced to section 37 of the IT Act, a deduction for the same was not available under section 37 of the IT Act. However, the assessee had claimed deduction of donation under section 80G. The Tribunal noted that CSR contributions to Swachh Bharat Kosh and Clean Ganga Fund, were specifically excluded from the ambit of section 80G of the IT Act. In view of this, the Tribunal inferred that other CSR qualifying donations are eligible for deduction under section 80G, subject to the assessee satisfying the requisite conditions prescribed for deduction under section 80G of the IT Act. The Tribunal remanded the matter for examination and verification of facts.
- In another set of decisions^[8] of Bangalore Tribunal, the deduction under section 80G was disallowed, since CSR qualifying donations were not 'voluntary contributions'. The Tribunal allowed the deduction under section 80G and held that, *assessee cannot be denied the benefit of claim under Chapter VI A, which is considered for computing 'Total Taxable Income. If assessee is denied this benefit, merely because such payment forms part of CSR, would lead to double disallowance, which is not the intention of Legislature.*
- An inference can be also drawn from the decision^[9] of Delhi Tribunal, wherein the CIT(A) had held that the expenditure in the nature of CSR expense should be allowable as deduction under sections 35AC and 80G of the IT Act.

Conclusion

It may indeed be true that expenditure incurred on voluntary CSR activities may not meet the business purpose test. However, there were instances where the judicial authorities have allowed such CSR expenses. Perhaps, to crystallise the position beyond doubt, the legislature denied the claim of such expenses on CSR activities under section 37(1) from the business profits, effective from the assessment year 2015-16. The legislature did not want such expenditure to be, in a sense, subsidised by the government by making such compulsory CSR expenditure as a tax deductible expenditure.

Already in certain charges of the tax department, deduction under section 80G is being denied for which appeals are pending before the CIT(A). On the other, some first appellate authorities have allowed the claim. With a view to reduce the Vivad on this subject, it would be better, if either a clarification is issued by CBDT or a suitable amendment is brought out to put an end to the controversy that is slowly gathering steam.

[1] Source: https://www.business-standard.com/article/companies/companies-spent-rs-11-867-cr-on-csr-activities-in-fy19-highest-so-far-119121200394_1.html

[2] NMDC Ltd. v. JCIT (2015) (Hyderabad Tribunal)

[3] CIT v. Infosys Technologies Ltd. (2014) (Karnataka)

[4] Sri Venkata Satyanaryana Rice Mill Contractors Co. v. CIT (1996) [\[TS-5093-SC-1996-O\]](#) (SC)

[5] CIT v. Madras Refineries Ltd. (2004) [\[TS-5804-HC-2003\(MADRAS\)-O\]](#) (Madras)

[6] (2019) (Delhi Tribunal)

[7] (IT(TP)A No.2355/Bang/2019) (Bangalore Tribunal)

[8] First American (India) Pvt. Ltd v. ACIT (ITA No.1762/Bang/2019) / [\[TS-5676-ITAT-2020\(BANGALORE\)-O\]](#) & Allegis services (India) Pvt. Ltd v. ACIT (ITA No.1693/Bang/2019) / [\[TS-5678-ITAT-2020\(BANGALORE\)-O\]](#)

[9] National Seeds Corporation Ltd. v. ACIT [ITA No. 6794/Del/2014]