

## GST and Corporate Social Responsibility: Provisions and Challenges

*This article discusses the impact of GST law on the multifold modes of CSR activities. Further, the question “whether Input Tax Credit (ITC) is admissible on expenditure incurred by a company towards CSR activities as per the provisions of Companies Act, 2013” has been a constant issue of confusion and ambiguity. With the adverse impact of the COVID-19 pandemic, where a lot of organizations are incurring CSR expenditure to fight against the pandemic, the matter has become more problematic across the nation since the GST law does not specifically speak on this issue and the government has not come out with any clarification thereon. Read on...*



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### 1. Introduction to Corporate Social Responsibility

The concept of Corporate Social Responsibility (CSR) is well known throughout the business world. It not only speaks of contributions made towards the benefit of the less privileged but also calls for making oneself accountable to the society. Many think that CSR is a new concept. However, in our country, kings have been practicing CSR for thousands of years. Even Kautilya’s *Arthashastra* speaks about this:

*“Shresta Dharma- the better off one is in the society, the*

*higher should be one’s sense of responsibility”*

In India, with the enactment of the Companies Act, 2013, it has now become mandatory for Companies to take up CSR projects on social welfare activities. In the present times, the ambit of CSR activities has grown manifold and is playing an important part in achieving the sustainable development goals and private-public partnership in nation building. CSR has also played a very important role in supporting the social and economic development of the country during the COVID-19 pandemic.



## 2. GST implications on the modes of discharging Corporate Social Responsibility

The implications of GST on the various modes which may be adopted by any corporate to discharge its Corporate Social Responsibility u/s 135 of Companies Act, 2013 read with Schedule VII are depicted below

- a. Direct Contributions to various funds such as Swatch Bharat Kosh, PM Cares Fund etc. The contributions to such funds are made in form of monetary donations. GST is not applicable on such monetary contributions as Section 2(52) & Section 2(102) of CGST Act, 2017 specifically excludes money from the definition of Goods as well as Services respectively.
- b. Providing funds to any registered trust or society or to a company registered u/s 8 of Companies Act, 2013. Usually, under this scenario,

a MOU is entered into between the company and recipient trust or society. By implementing such a MOU, the corporate discharges its CSR requirement. Although the corporate is not directly performing any CSR activity and such activities are provided by the trust or society to the ultimate beneficiaries, but still the trust or society may need to charge GST on the funds received by it.

The Authority for Advance Ruling, New Delhi in the case of *Indian Institute of Corporate Affairs* [[2019] 107 taxmann.com 413] ruled that the amount paid by the companies to external agencies for CSR activities to undertake specified projects would be considered as 'Consideration' and therefore, executing CSR activities as per company's direction would be interpreted as Supply and GST would be applicable on the same.

Hence, drafting the terms and clauses of MOU plays a pivotal role in such cases. Any direct nexus between the amount paid and the supply of taxable service towards a specified project would make the activity leviable to GST.

- c. Discharging CSR activities by providing manufactured/traded goods or services directly to the beneficiaries. Under this



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mode, companies provide their own manufactured or purchased goods such as masks, sanitizers, PPE, food products etc. to the beneficiaries to discharge its Corporate Social Responsibility. Alternatively, services such as providing temporary shelter, COVID-19 education or awareness programme etc. may also be provided by the company to discharge its CSR.

### GST on supply of goods for CSR activities

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# Indirect Taxes

Entry No. 1 of Schedule I of the CGST Act, would be relevant in the current scenario, i.e., “*Permanent transfer or disposal of business assets where input tax credit has been availed on such assets*”. Since the registered person’s own products, viz. manufactured or traded goods, are being distributed free of cost for CSR activities, these would be “finished goods” in the business of the registered person, hence they can be called as business assets. The ITC availability on such goods have been discussed later in this article.

Hence, if the registered person has availed ITC on the said goods (business assets), the permanent transfer of these goods would amount to supply, even though it is given without any consideration, thereby attracting GST.

## **GST on supply of services for CSR activities**

Services supplied free of cost for CSR activities would not be covered under any entry of Schedule I to the CGST Act. Entry 1 on “*Permanent transfer or disposal of business assets*” particularly covers goods i.e., business assets but not services. Entry No. 2 “*Supply of goods or services between related persons or between distinct persons*” would also not be applicable, as the services provided under CSR must not be towards any related persons or distinct persons.

Hence, any services provided without any consideration for

CSR activities would not be a supply, thereby not attracting GST. On the contrary, CSR activities done through other agencies to undertake specific projects for consideration may get covered under the scope of supply and would be liable for GST as pointed out in Para 2.2 above. However, if the said service is specifically exempt under Notification No. 12/2017-Central Tax (Rate) as amended, then there would be no GST payable.

## **Input Tax credit on supply of goods or services for CSR activities**

Since all such goods and services are provided without charging any monetary or non-monetary consideration, a moot question that pops up every now and then is **whether GST paid on the goods and services used for CSR activities will be available as input tax credit (ITC)? Let us discuss the provisions and challenges.**

### **3. Relevant Provisions**

a. Section 16(1) of the CGST Act, 2017 defines the eligibility for taking input tax credit:

*“16. (1) Every registered person shall, subject to such conditions and restrictions as may be prescribed and in the manner specified in Section 49, be entitled to take credit of input tax charged on any supply of goods or services or both to him which are **used or intended to be used in the course or furtherance of***

*his business and the said amount shall be credited to the electronic credit ledger of such person”*

b. Section 2(17) of the CGST Act, 2017 defines Business as:

*“2. (17) Business includes –*

*a. any trade, commerce, manufacture, profession, vocation, adventure, wager or any other similar activity, whether or not it is for a pecuniary benefit;*

*b. any activity or transaction in connection with or incidental or ancillary to sub-clause (a);*

*c. ....”*

c. Relevant extracts of Section 135 of the Companies Act, 2013 that deals with CSR:

*“135. (1) Every company having net worth of rupees five hundred crore or more, or turnover of rupees one thousand crore or more or a net profit of rupees five crore or more during the immediately preceding financial year] shall constitute a Corporate Social Responsibility Committee of the Board consisting of three or more directors, out of which at least one director shall be an independent director.*

*.....*

*(5) The Board of every company referred to in sub-section*

(1), shall ensure that the company spends, in every financial year, at least two per cent of the average net profits of the company made during the three immediately preceding financial years or where the company has not completed the period of three financial years since its incorporation, during such immediately preceding financial years, in pursuance of its Corporate Social Responsibility Policy:

.....

- (7) *If a company is in default in complying with the provisions of sub-section (5) or sub-section (6), the company shall be liable to a penalty of twice the amount required to be transferred by the company to the Fund specified in Schedule VII or the Unspent Corporate Social Responsibility Account, as the case may be, or one crore rupees, whichever is less, and every officer of the company who is in default shall be liable to a penalty of one-tenth of the amount required to be transferred by the company to such Fund specified in Schedule VII, or the Unspent Corporate Social Responsibility Account, as the case may be, or two lakh rupees, whichever is less."*

#### **4. Does CSR activities pass the Business Test? Can it be considered to be "used or intended to be used in**

#### ***the course or furtherance of business"?***

As per the GST law, to avail input tax credit it is *sine qua non* for the goods / service to be used in the course or furtherance of business. Considering the wide definition of the term 'business' under the GST law, there is no requirement to establish a direct one to one linkage in order to avail ITC. Even incidental / ancillary activities can be treated as 'in the course of business' and procurements made for undertaking such activities are eligible for ITC. The first test of ITC eligibility is for it to be considered '*used or intended to be used in the course or furtherance of business*'.

- a. It has been held by the Hon'ble CESTAT Mumbai, in the case of ***Essel Propack Ltd. v. Commissioner of CGST* [[2020] 117 taxmann.com 409]** that **CSR is not a charity any more since it has got a direct bearing on the manufacturing activity of the company** which is largely dependent on smooth supply of raw materials and the same also augments the credit rating of the company as well as its standing in the corporate world. Therefore, **sustainability is dependent on CSR without which companies cannot operate smoothly for a long period** as they are dependent on various stakeholders to conduct business in

an economically, socially and environmentally sustainable manner. It was further observed that CSR, which was a mandatory requirement for the public sector undertakings, has been made obligatory also for the private sector and **unless the same is treated as input service in respect of activities relating to business, production and sustainability of the company itself would be at stake.**

- b. Further, Hon'ble High Court of Karnataka in the case of ***CCE v. Millipore India (P) Ltd.* [[2011] 16 taxmann.com 363]** observed that the concept of corporate social responsibility is to discharge a statutory obligation. It further observed that when the employer spends money to maintain their factory premises in an eco-friendly manner, certainly, the tax paid on such services would form part of the costs of the final products. It upheld the Tribunal's decision that the service tax paid in all these cases would fall within the input services and the assessee is entitled to the benefit thereof.
- c. It is pretty evident, as has been laid down in various pronouncements, that a Company is compulsorily required to undertake CSR activities in order to run its business. '*In the course or furtherance of business*' includes all activities which are incidental / ancillary



to the business which are incurred during the course of business. As a result, **CSR activities is an essential part of the business process as a whole and thus can be construed to be incurred 'in the course or furtherance of business'**. Hence, this clears the first test of ITC eligibility. Let's move to the next one.

## 5. Can ITC of CSR activities be restricted u/s 17(5)(h) by treating them as gifts?

- a. Section 17(5)(h) of the CGST Act, 2017 states:

*"17(5) Notwithstanding anything contained in sub-section (1) of section 16 and sub-section (1) of section 18, **input tax credit shall not be available** in respect of the following, namely:—*

.....

*(h) goods lost, stolen, destroyed, written off or disposed of by way of gift or free samples;*

....."

- b. The Authority for Advance Ruling, Kerala denied ITC on CSR expenses by considering them as 'disposal by way of gift' in the case of **Polycab Wires Private Limited [2019 (24) G.S.T.L. 103 (A.A.R. - GST)]**. In the said case, the applicant had distributed electrical goods to people affected by flood in Kerala against discharge of its CSR obligations. The Kerala AAR held that the applicant distributed electrical items on free basis without collecting any money and for these transactions input tax credit would not be available

as per Section 17(5)(h) of the KSGST Act and CGST Act.

However, in the above ruling, the Hon'ble AAR has not discussed the matter in detail and simply ruled that ITC would not be available on goods distributed free of cost as CSR expenditure without extending any plausible reasoning. To begin with, it may be necessary to dwell on the concept of gift.

### c. What is the meaning of the term 'Gift'?

The term 'Gift' has not been defined under the GST law, however in common parlance, gift is provided to someone occasionally, without consideration and which is voluntary in nature. The **Gift Tax Act (18 of 1958)** had defined the word gift to mean transfer by one person to another of any existing movable or immovable property voluntarily and without consideration in money or money's worth.

#### i. **Black's Law Dictionary (Fourth Edition)** defines gift as:

*"A voluntary transfer of personal property without consideration. A parting by owner with property without pecuniary consideration. A voluntary conveyance of land, or transfer of goods, from one person to another made gratuitously, and not upon any consideration of blood or money."*

#### ii. A similar definition has been given in **Webster's Third New International Dictionary (Unabridged)**



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where the author defines gift as:

*"Something that is voluntarily transferred by one person to another without compensation; a voluntary transfer of real or personal property without any consideration or without a valuable consideration-distinguished from sale."*

- iii. Further, the Hon'ble Supreme Court of India, in the case of **Ku. Sonia Bhatia v. State of UP [AIR 1981 SC 1274]**, cited the definition of 'gift' from *Corpus Juris Secundum, Volume 38* in the following words:

*"A 'gift' is commonly defined as a voluntary transfer of property by one to another, without any consideration or compensation therefor. A 'gift' is a gratuity and an act of generosity and not only does not require a consideration, but there can be none."*

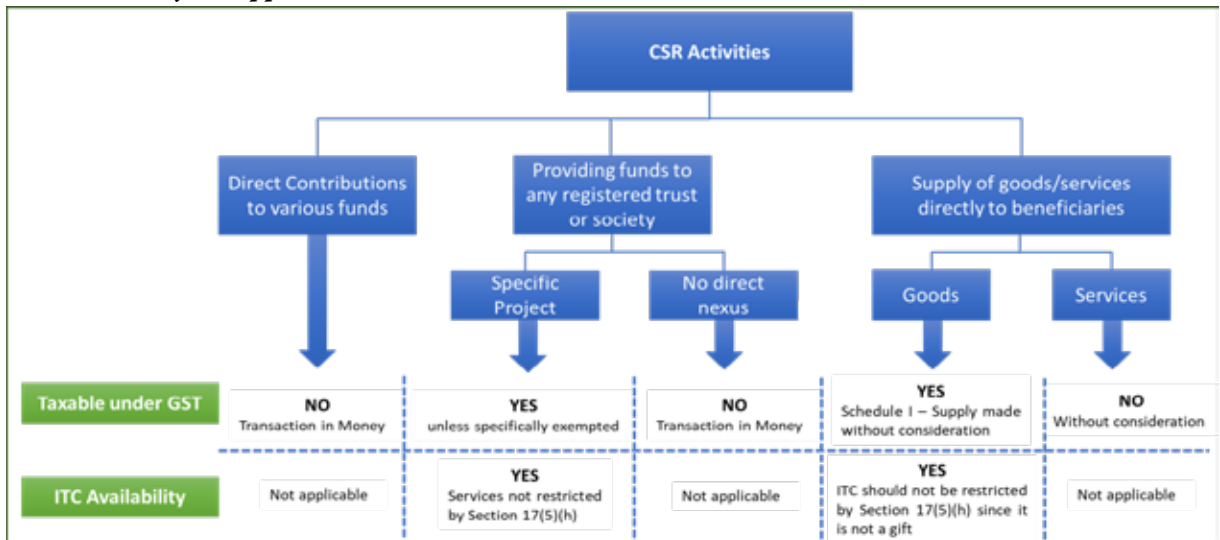
- d. Additionally, it has been held by the Authority for Advance Ruling, UP in the case of **Dwarikesh Sugar Industries Ltd [[2021] 125 taxmann. com 329]**:

*“...we are in unison with the applicant that a clear distinction needs to be drawn between goods given as ‘gift’ and those provided/supplied as a part of CSR activities. While the former is voluntary and occasional, the latter is obligatory and regular in nature. CSR expenses incurred by the applicant*

can only be termed as ‘gifts’. However, when a company spends on CSR activities, it is mandatorily required by Section 135 of the Companies Act to do so. Failing to comply with the same leads to penal actions which might jeopardize the sustainability of the company. The same principle has been laid down in multiple cases including

is no scope for intendment where the words used by the legislature are clear and unambiguous. Therefore, this reduces the disputable position of ITC availability on CSR expenses with respect to services and ITC would be available on services used for CSR activities.

To summarize the above discussion,



*have been mandated under the Companies Act, 2013. It is the applicant's obligation to incur such expenses in order to be in compliant with the law. Since CSR expenses are not incurred voluntarily, accordingly, we are of the opinion that they do not qualify as ‘gifts’ and therefore its credit is not restricted under section 17(5) of the CGST Act, 2017”*

*Essel Propack Ltd (supra) among others. Hence, it should be within the accepted bounds of law to construe that CSR expenses cannot be termed as gifts and ITC on the same cannot be restricted u/s 17(5)(h) of the CGST Act.*

### Availability of ITC on services used for CSR activities

A deeper observation of Section 17(5)(h) brings out that no restriction is placed on free distribution of services. Section 17(5)(h) only restricts ITC on free distribution of goods by way of gifts or free samples. Hence, even if services are given free of cost for such activities, ITC on the same would not be restricted. It is a well-settled principle that there

### Concluding Remarks

The provision for availing Input Tax Credit has been the peacemaker amidst the chaos subsequent to the introduction of GST. So far, the seamless procedure for utilizing input credit has been commendable, however, it is not free of its own entanglements and there is still a lot of ambiguity. In these times of adversity, where a lot of organizations are incurring CSR expenditure to fight against the pandemic, it is the need of the hour for CBIC to come up with some positive clarifications to clear the sky relating to such confusions on the availability of ITC. This will ensure the active participation of trade and industry to further strengthen the fight against this pandemic. ■■■

- e. In view of the above, for a supply to be considered as a gift, the supply must be made without any contractual obligation and should be voluntary in nature. Supplies made out of love and affection or such other non-legal considerations