

AccountAble™

106: CSR and FCRA

AccountAble 106: Rev. July '16

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Many companies in India give money to NGOs, schools, hospitals, etc. Sometimes the money is given directly. In other cases, the money is given through the company's own foundation. This may also be done as part of the company's CSR¹ activities.

If the company is a foreign source, then FCRA² comes into play. However, few companies are familiar with FCRA. The definition of 'foreign source' has also been amended in May'16. This issue of AccountAble discusses the FCRA requirements related to CSR activities.

COMPANIES AS 'FOREIGN SOURCE'

Original FCRA 2010 treated an Indian company as a foreign source, if more than 50% of its shares were held by foreigners etc. This was a tricky clause,³ and a Parliamentary Committee had recommended that this should be dropped. This recommendation was not accepted by MHA. As a result, many Indian companies with foreign shareholders became foreign source. This resulted in problems for their CSR activities. Finally, the Parliament changed the provision with retrospective effect from May'11. The amended clause reads:

- (j) "foreign source" includes, —
- (i) the Government of any foreign country or territory and any agency of such Government;
 - (ii) any international agency, not being the United Nations or any of its specialised

agencies, the World Bank, International Monetary Fund or such other agency as the Central Government may, by notification, specify in this behalf;

- (iii) a foreign company;
- (iv) a corporation, not being a foreign company, incorporated in a foreign country or territory;
- (v) a multi-national corporation referred to in sub-clause (iv) of clause (g);
- (vi) a company within the meaning of the Companies Act, 1956, and more than one-half of the nominal value of its share capital is held, either singly or in the aggregate, by one or more of the following, namely:—
 - (A) the Government of a foreign country or territory;
 - (B) the citizens of a foreign country or territory;
 - (C) corporations incorporated in a foreign country or territory;
 - (D) trusts, societies or other associations of individuals (whether incorporated or not), formed or registered in a foreign country or territory;

¹ Corporate Social Responsibility

² Foreign Contribution (Regulation) Act, 2010

³ It's often difficult to establish exact shareholding pattern for widely-held companies.

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(E) foreign company;

Provided that where the nominal value of share capital is within the limits specified for foreign investment under the Foreign Exchange Management Act, 1999, or the rules or regulations made thereunder, then, notwithstanding the nominal value of share capital of a company being more than one-half of such value at the time of making the contribution, such company shall not be a foreign source;

(vii) a trade union in any foreign country or territory, whether or not registered in such foreign country or territory;

(viii) a foreign trust or a foreign foundation, by whatever name called, or such trust or foundation mainly financed by a foreign country or territory;

(ix) a society, club or other association of individuals formed or registered outside India;

(x) a citizen of a foreign country;

CONFUSION COMPOUNDED

However, this amendment has caused quite a bit of confusion. Many people now think that all companies registered in India are Indian sources. This is not true. Under the amended law, a company can still be a foreign source for any of the following five reasons:

1. It is a foreign company - meaning it's a company formed or registered abroad.
2. It is a subsidiary of a foreign company.
3. It is a branch of a foreign company.
4. It is part of a multinational corporation (MNC). The MNC should be controlled from outside India.
5. It's a company where foreigners hold more than 50% shares - *and* the foreign shareholding exceeds the FDI norms.

Each of these clauses are independent. That means a company meeting even one out of four conditions will become a foreign source.

Foreign Company – Indian Source?

Can a foreign company become an Indian source? Never. Foreign companies are always a foreign source under FCRA. This remains true even if all the shares are held by Indian citizens or by Indian companies. Therefore, if an Indian company acquires a foreign company, the foreign

company will continue to remain a foreign source.

Trick or Treat?

If that's somewhat clear, try this simple quiz. Go through the following list, and tick the companies which are still a foreign source:

1. Bata India Ltd.
2. Blue Star
3. Britannia Industries Ltd.
4. Café Coffee Day
5. Greaves Cotton
6. Hindustan Unilever Ltd.
7. Housing Development Finance Corporation Ltd. (HDFC)
8. ICICI Bank Ltd.
9. iGate Global Solutions Ltd., Bangalore
10. ING Vysya Bank Ltd.
11. Jet Airways (India) Ltd.
12. Maruti Suzuki India Ltd.
13. Mphasis Ltd.
14. Sesa Goa Ltd.
15. Sterlite Industries India Ltd.
16. Siemens Ltd.

Done? Turn to page 4 to find out how many did you get right.

CSR FOUNDATIONS

What happens if a company classified as foreign source forms a public trust in India for CSR? The trust should get FCRA registration before accepting any grant or donation from the mother company. Secondly, the CSR grant and the interest on these funds will be foreign contribution. Therefore, all the usual FCRA restrictions come into play. These funds cannot be given to political parties, media, government officers, etc. If the funds are given to another NGO, then it should have FCRA registration or prior-permission.

ITEMS COVERED

FCRA covers donative transactions related to money, material and securities. However, it does not cover use of facilities without charge, or volunteering. It also leaves out some receivers such as hospitals.⁴

⁴ For more on this, see 'What's Covered' pp. 40-45 and 'Other Areas' p.72, AccountAble Handbook: FCRA 2010 at www.AccountAid.net.

CASE STUDIES

Let us now consider two hypothetical cases.

In the first case, an international mining company set up operations in India. It also started CSR activities around its plant through grants to a number of NGOs, and to its own Trust. The mining company was a subsidiary of an Australian company, and therefore a foreign source. However, the company was not aware of this. As a result, it did not check FCRA status of the receiving NGOs. This continued for several years, till the lapse was pointed out in a special audit. The company then applied to FCRA Department for compounding the offence, and obtaining FCRA registration for its Trust.

In the second case, a large Indian bank has set up a Trust to run its CSR activities. 56% of its shares are held by Foreign Institutional Investors, though it is not a subsidiary of any foreign company. The bank has made several corpus grants to the Trust, running into hundreds of crores. The trust uses interest earned on the corpus to make grants to a number of NGOs. It also runs programs directly.

The Trust is managed by people with a business background. Most of the governing body members in the Trust are also from the bank and associated companies. None of them are aware of the FCRA requirement. Is the bank defaulting on FCRA compliance?

The bank would have been classified as a foreign source, if the FCRA was not amended. However, due to the retrospective amendment, there is no longer any violation.

PRECAUTIONS

What should you do to ensure you don't end up with FCRA problems?

For NGOs

Check the FCRA status of any company that donates money or material to you. You could find this out by googling the company on the net. If the company is part of a foreign group, it is likely to be a foreign source. Visiting the company's website often helps. Subsidiaries of a company must also disclose this information in notes to audited accounts.

If there is any doubt, you should email the company as follows:⁵

To comply with requirements of Foreign Contribution

⁵ For more on this, see 'Company under Foreign Control' p.52, AccountAid Handbook: FCRA 2010, available at www.AccountAid.net

The Politics of Change

After CSR became mandatory in 2014, some Indian corporate leaders expressed their unhappiness at being classified as 'foreign source' under FCRA. In 2015, national media ran stories on how companies under Indian control were being treated as 'firangees' under FCRA. The Government responded by proposing a change in Dec'15. This was notified on the MHA website.

The FCRA amendment was then included in the Finance Bill 2016. This was a bit unusual as the amendment was not really part of a money bill. It was also proposed as a retrospective amendment effective 1-May-11.

Some activists smelled a rat. Both BJP and Congress are fighting an FCRA court case for having accepted foreign contribution from Vedanta group. The activists thought that this was a ploy to get both parties off the FCRA hook. One web-paper wrote a story on this - the cry was then taken up by mainstream media.

However, the story was based on a misunderstanding. The amendment benefits only those companies which are controlled from India. Subsidiaries of foreign companies still remain a foreign source. Therefore, companies such as Sterlite Industries India, Sesa Goa, will continue to be foreign sources, as they are subsidiaries of Vedanta Resources plc. And Vedanta is a foreign company, registered in England.

Moreover, if the government was trying to save BJP and Congress in the FCRA case, it wouldn't help for another reason. The case relates to donations accepted up to 2009, when FCRA 1976 was in force. This point is also emphasised in the Mar'14 judgement of Delhi High Court (ADR vs. UOI & Others). Therefore, amending FCRA 2010 would not help at all.

Unfortunately, the wide media coverage of this poorly researched story had a side-effect. Thousands of people now think that all Indian companies are out of FCRA purview. This is resulting in FCRA violations on a daily basis.

If Sir Walter Scott was to write about FCRA, he might very well say:

Oh, what a tangled web we weave
When first we register to receive!

(Regulation) Act, 2010, we need to find out whether a donor / supporter is classified as a foreign source or Indian source. As FCRA provisions are complex, we request the following information about [full name of the company] which will help our legal advisers guide us on this issue:

1. Whether your company is a foreign company or corporation i.e. registered or incorporated outside India [Yes/No/Can't say]
2. Whether your company is a branch of a foreign company or corporation [Yes/No/Can't say]
3. Whether your company is part of a foreign multi-national corporation (MNC) [Yes/No/Can't say]
4. Whether your company is a subsidiary of a foreign company or of a foreign multi-national corporation [Yes/No/Can't say]
5. Whether more than 50% of the company's nominal capital is held by foreigners (including foreign citizens, foreign governments, foreign corporations, FIIs, foreign companies, foreign MNCs or their subsidiaries or foreign trusts / firms etc.) [Yes/No/Can't say]
6. Whether the foreign shareholding in 5 above exceeds FEMA / FDI norms [Yes/No/Can't say]

Once you get this information, talk to your auditors. If they cannot help you, send an email to query@accountaid.net with the details.

For Companies

Find out whether you are classified as a foreign source. If yes, then make sure:

- Your Finance and CSR teams have clarity about FCRA.⁶
- Grants⁷ are given only to NGOs with FCRA.
- The NGO knows that you are giving them foreign funds.
- You do not give any donations or grants to political parties, politicians, media persons, judiciary, government servants, etc. If you are giving a gift to such an individual, make sure that its market value is less than Rs. 25,000.

⁶ Visit FCRA Department's website at <https://fcraonline.nic.in/> for circulars and notices. Also see AccountAble issues or the AccountAid Handbook on FCRA 2010 at www.AccountAid.net.

⁷ Money, material (equipment, supplies, etc.) or securities

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Interpretation of law: Interpretation of law given here is of a general nature. Please consult your advisors before taking any important decision.

Questions and doubts? AccountAid provides complimentary advice to implementing NGOs and NGO auditors on matters related to accounting or financial regulation. You can send your questions by e-mail (query@accountaid.net) or letter. You can also discuss these over the phone.

Comments: Your comments and suggestions can be sent to AccountAid India, 55-B, Pocket C, Siddharth Extension, New Delhi-110 014; Phone: 011-2634 3128; Phone/Fax: 011-2634 3852; e-mail: query@accountaid.net.

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Answers to Quiz: Companies 1, 6, 9, 12-16 are presently foreign sources under FCRA as per information on internet. Please re-validate independently at time of taking any decision regarding foreign source status.

query@accountaid.net