ASPEN NETWORK OF DEVELOPMENT ENTREPRENEURS

For-Profit Social Enterprise on Social Stock Exchange

A Legal Explainer

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TrustLaw

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TRILEGAL

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Abbreviations

Abbreviation	Definition
AIF	Alternative Investment Fund
AIR	Annual Impact Report
BSE	Bombay Stock Exchange
CGST	Central Goods and Services Tax
CSR	Corporate Social Responsibility
GDP	Gross Domestic Product
GST	Goods and Services Tax
IPO	Initial Public Offer
ITA	The Income Tax Act
LTCG	Long-Term Capital Gains
MCA	The Ministry of Corporate Affairs
NSE	National Stock Exchange
SDG	Sustainable Development Goal
SEBI	Securities and Exchange Board of India
SGB	Small and Growing Business
SME	Small and Medium-sized Enterprises
SSE	Social Stock Exchange
STCG	Short-Term Capital Gains
STT	Securities and Transaction Tax
ZCZP	Zero Coupons Zero Principal

Chapter 1: Introduction

India needs a significant capital injection to achieve the Sustainable Development Goal (SDG) targets by 2030 and deal with climate change. As India continues to lag in the critical SDG goals of alleviating poverty, ending hunger, reducing inequality and ensuring decent jobs and economic growth, its development finance gap stands at a staggering 13 percent of its gross domestic product (GDP).[1] Additionally, climate mitigation and adaptation goals are increasing pressure on government spending.

Impact investing is a promising solution for the much-needed capital injection. Impact investing has made significant strides in catalysing philanthropic and commercial capital to identify and support impact businesses tackling critical social challenges. It has equipped India with the ability to tap into the much larger pools of private capital available in global markets. This is necessary to rapidly scale and deepen the work of successful social enterprises delivering services to and increasing the incomes of low-income populations.

The past few years have witnessed the development of several blended finance structures, particularly social and development impact bonds. These instruments leverage philanthropic capital as outcome funding to mobilise return-seeking capital to underwrite the risk of social service delivery. Thereby channelling it towards development outcomes by pricing social targets in terms of financial returns. Initiatives like the Social Stock Exchange (SSE) and amendments to corporate social responsibility regulations that channel additional capital and enable results-based financing have the potential to increase and broaden the pooled funds available to social enterprises and help them scale.

In December 2022, the Securities and Exchange Board of India (SEBI) approved the introduction of the SSE as a special segment on the Bombay Stock Exchange (BSE). This was done based on the suggestions of a working group and technical group that created a framework to provide social enterprises with an additional avenue to raise funds. Given this context, ANDE India, under the aegis of its Small and Growing Business (SGB) Finance Learning Lab, sought to produce this explainer. ANDE India collaborated with TrustLaw, the legal pro bono service of the Thomson Reuters Foundation, to facilitate the pro bono connection with Trilegal to develop this Social Stock Exchange Explainer with the objective of providing focused guidance on how impact investors, local and foreign, can leverage the SSE to make investments in social enterprises in India. Consequently, while the SSE framework addresses both for-profit and non-profit enterprises, this explainer's scope is limited to for-profit enterprises.

In November 2020, ANDE India brought out a Social Success Note Playbook as part of its SGB Finance Learning Lab, and this explainer is the next step in continuing to meet one of the Learning Lab's goals of increasing knowledge around elements of blended finance that can help social enterprises scale.

[1] A. Sheth, J. Batabyal, N. Nundy, A. Misra, and P. Pal. "India Philanthropy Report 2023". Dasra | Bain & Company, Inc. 2023.

Chapter 2: What is a Social Stock Exchange?

The rising gap between private capital and the social sector has prompted the need for innovative finance solutions. A social stock exchange is one such opportunity for social sector organisations that eases the process of fundraising. It offers to bridge the gap between funders and social sector organisations through a platform that operates similarly to a stock exchange. Regulated by SEBI, India's Social Stock Exchange will allow social enterprises to raise capital by issuing securities while disclosing pertinent information to social impact investors. Following SEBI approval, SSE segments have been established on both the National Stock Exchange[2] (NSE) and the BSE.[3]

1. The Global Phenomenon of Social Stock Exchanges

The world's first SSE was launched by Brazil in 2003. Since then, several countries such as South Africa, Portugal, Canada, the United Kingdom and Singapore have also established social stock exchanges. However, SSEs have seen limited operational longevity.

Four out of the seven SSEs launched around the world had to close operations. Currently, only Jamaica, Singapore and Canada have operational SSEs.

There are many reasons behind their short life spans. Most of the SSEs were launched as private entities. Some SSEs performed the role of mediators between donors and social enterprises. Some were dependent on donations for the upkeep and daily operation of the SSE. The lack of a sustainable business model and unreliability of fund flows adversely affected their long-term performance, thus limiting investor interest.

2. What Makes the Securities and Exchange Board of India's Social Stock Exchange Stand Out?

India's SSE will be a part of existing stock exchanges. SEBI's regulation of the SSE differentiates India's approach from other countries. For instance, Brazil, Singapore and the United Kingdom's SSE platforms were managed as private sector entities and Canada's SSE is registered as a non-profit.[4] While Singapore's SSE is operated by the Stock Exchange of Mauritius and regulated by Mauritius's Financial Service Commission,[5] Jamaica's SSE is a corporate social responsibility initiative of the Jamaica Stock Exchange.[6] India's move to house its SSEs as separate segments of established stock exchanges is expected to give SSEs access to supportive infrastructure, thereby boosting their performance and viability.

As a platform, an SSE is a meeting point of mutual interests. But India's Social Stock Exchange's role goes beyond mere matchmaking between funders and social enterprises. SEBI's Working Group's[7] and Technical Group's[8] plans set out extensive disclosure requirements before and after a listing of securities.

The goal is to increase transparency and smoothen communication between funders and recipients. Detailed disclosure requirements help investors receive critical insights on the social enterprises delivering impact,

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2 V. Sreedhar. "NSE Gets Sebi Nod to Set Up Social Stock Exchange". *The Economic Times.* 2022 (December 23).

3 Business Today. "Sebi Grants Final Nod for Social Stock Exchange as Separate Segment on BSE: Who can list on it?" *Business Today*. 2020.

4 "SVX". Accessed on October 9, 2023.

5 IIX Global. "IIX Social Sustainability Bonds: Changing Finance, Financing Change." *The Rockefeller Foundation & IIX Global*. 2017.

6 "Corporate Social Responsibility." *Jamaica Stock Exchange.* Accessed on October 9, 2023.

7 "Working Group Report on Social Stock Exchange." *Securities and Exchange Board of India.* 2020.

8 "Technical Group on Social Stock Exchange." *Securities and Exchange Board of India*. Accessed on October 9, 2023.

thus providing investors with clarity on an entity's vision, goals and strategies. At the same time, the SSE offers social enterprises greater visibility for their projects and eases access to a large pool of impact capital. The Indian model of SSE’s success will lie in the strength of the three pillars of transparency, fund mobilisation and fund utilisation.

Chapter 3
Listing on the Social Stock Exchange as a For-Profit Social Enterprise: A Stepwise Guide to Fundraising

The creation of a regulatory space for an SSE in India opens a new avenue of fundraising for the nation's developmental sector. Social sector organisations often struggle to find the right donors and investors. For-profit enterprises are balancing expectations of business viability and deliverable impact while looking for the right investor. India's policymakers and regulators seek to ease these challenges. The SSE is expected to promote private capital flow towards development impact projects with a sustainable revenue stream.

The financial regulator has amended two key regulations to create a robust framework for the operation of the Social Stock Exchange in India. These regulations are:

1. Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018 (ICDR Regulations),[9]
2. Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015 (LODR Regulations).[10]

Additionally, SEBI's circular released on 19 September 2022 prescribes disclosure parameters, including impact reporting, for social enterprises to safeguard accountability and transparency. The regulations also empower the stock exchanges to articulate any additional requirements concerning registration.

This explainer will help you navigate the process and requirements of listing yourself as a for-profit social enterprise on the SSE. It will also provide a comprehensive understanding of the disclosure requirements expected of by the regulator once you register or list on the SSE.

1. How Are For-Profit Social Enterprises Different from Not-For-Profit Organisations in Raising Funds on the Social Stock Exchange?

There are two kinds of social enterprises (i.e., for-profit organisations and not-for-profit organisations). While both can be listed on the SSE, the law recognizes the two differently and prescribes separate procedures. They are primarily distinguished on the basis of their manner of legal incorporation. The flowchart below explains this legal difference succinctly.

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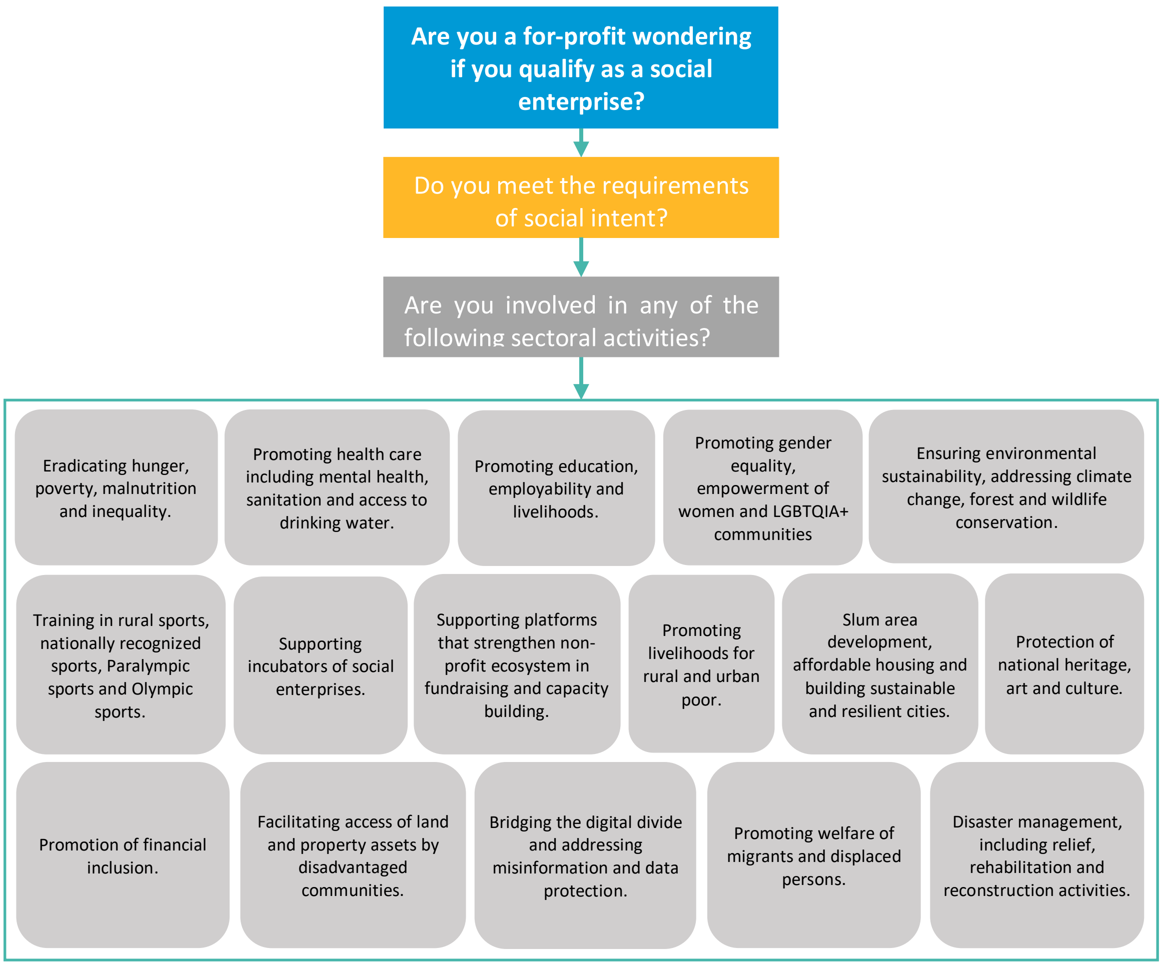
9 As per the third amendment by the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2022 w.e.f. 25.7.2022.

10 As per the third amendment by the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2022 w.e.f. 25.7.2022.

Figure 1: Types of Social Enterprises

2. Eligibility Criteria for Social Stock Exchange Listing

To start fundraising on the SSE, you must first be a social enterprise as per the criteria given by the SEBI regulations. A quick look at the flowchart below will let you know whether you fulfil the necessary conditions to be a social enterprise.



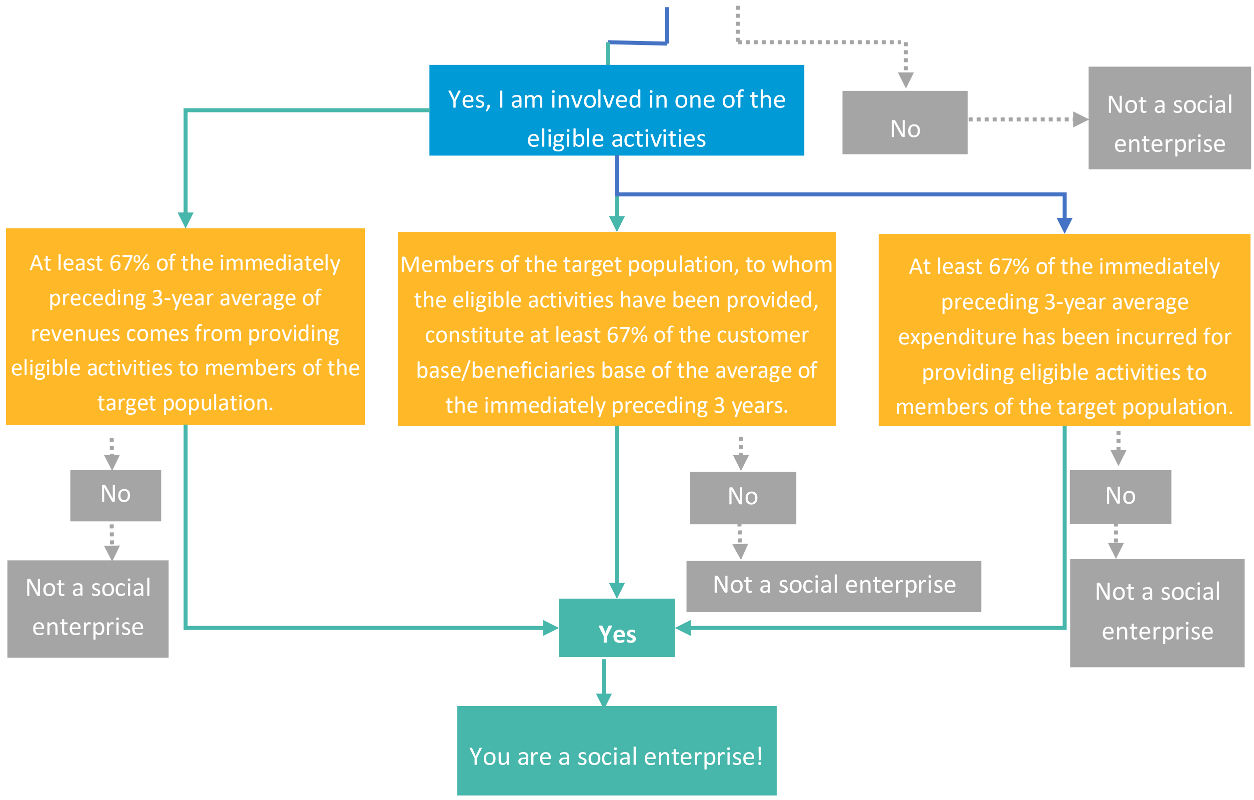


Figure 2: Eligibility Criteria of Social Enterprises for the Social Stock Exchange

3. Who Cannot Be a Social Enterprise?

Some organisations are excluded from the framework of a social enterprise. Thus, you may have fulfilled all the conditions of Figure 2 but may still not be able to list on the SSE since you cannot be considered a social enterprise. Check Figure 3 to know whether you fall within the ambit of barred organisations from SSEs.

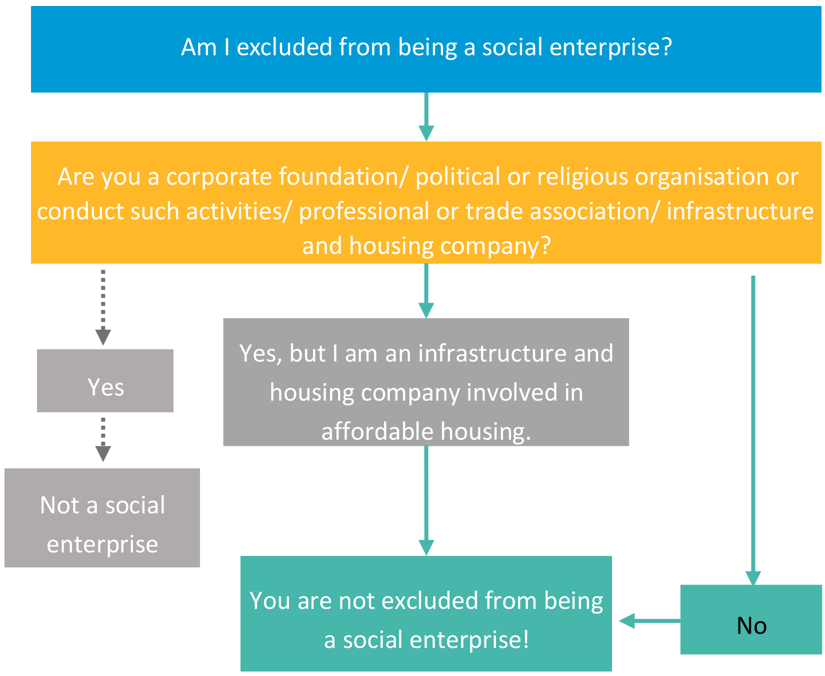


Figure 3: Organisations Excluded from the Definition of Social Enterprise

4. Disqualifying Events from Raising Funds on the Social Stock Exchange

Despite fulfilling eligibility requirements and being safe from the exclusion criteria, you may be debarred from raising funds on SSE in case any of the prescribed events occur. Please see the flowchart below to learn which events risk your disqualification from the SSE.

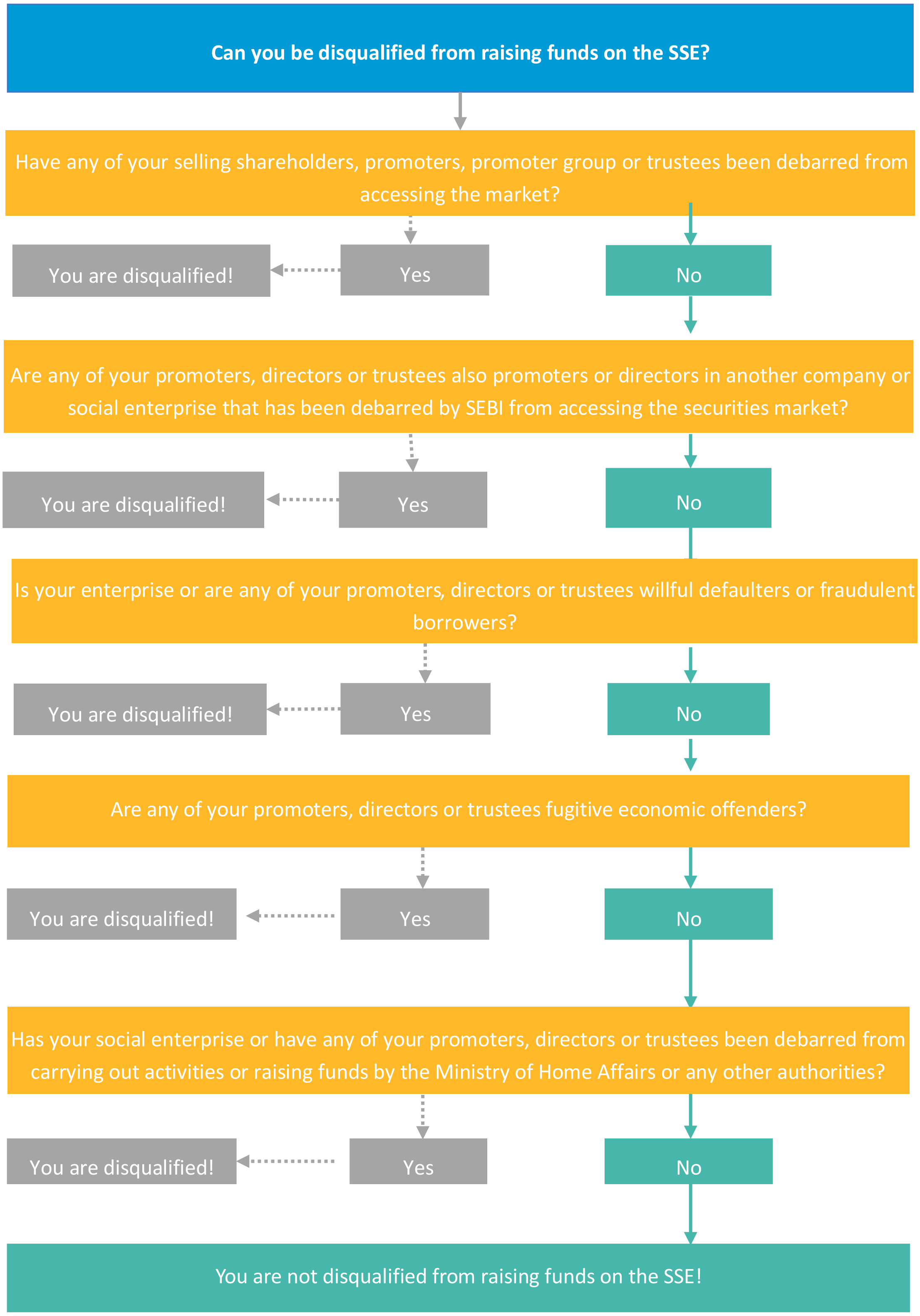


Figure 4: Disqualification from Raising Funds on the SSE

5. Process of Fundraising on the Social Stock Exchange for a For-Profit Social Enterprise

For-profit social enterprises can issue securities on the Main Board, Small and Medium-sized Enterprises (SMEs) Platform or Innovators Growth Platform. To do this, they must comply with the SEBI (Issue of Capital and Disclosure Requirements) Regulations 2018 and SEBI (Listing Obligations and Disclosure Requirements) Regulations 2015.

The flowchart below explains the steps of the listing process for a for-profit social enterprise.

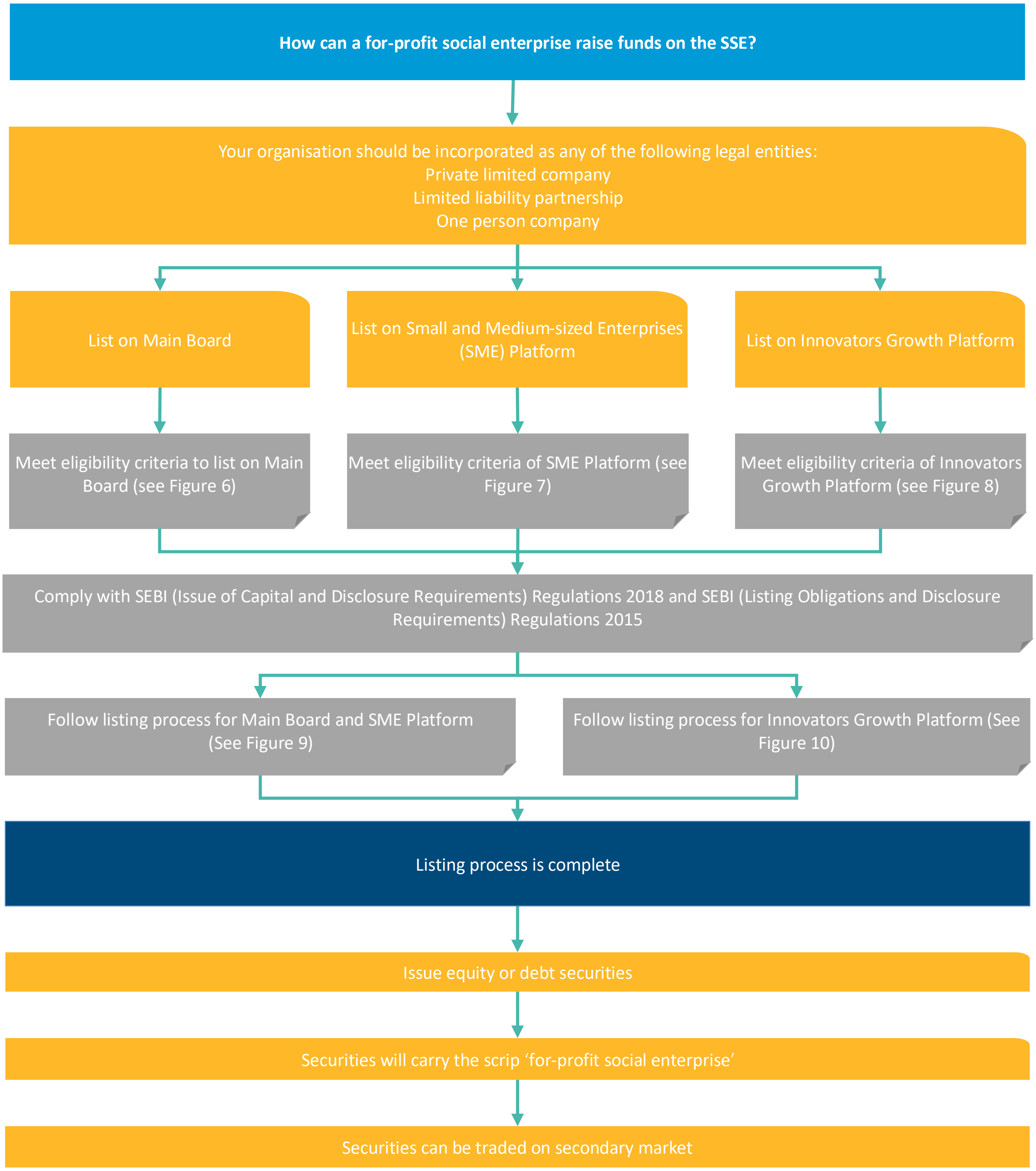


Figure 5: Listing on the Social Stock Exchange for For-Profit Social Enterprises

A. What Are the Eligibility and Disclosure Requirements for the Main Board, Small and Medium Enterprises Platform and Innovators Growth Platform?

As indicated in the above figure, each platform has its respective conditions and obligations for security issuers. Given below is a bird's eye view of the eligibility and listing criteria on the Main Board, SME Platform and Innovators Growth Platform.

Outline of listing equity instruments on the Main Board

Financials

- The paid-up equity capital of the applicant must not be less than 10 crores and the capitalisation of its equity should not be less than 25 crores.
- Net tangible assets of at least 3 crores, calculated on a consolidated basis, in each of the preceeding three full years and not more than 50% are held in monetary assets.

Conditions Precedent to Listing

- The applicant must have adhered to the conditions precedent to listing generally as under:
- 1. Securities Contracts (Regulations) Act of 1956.
- 2. Companies Act of 2013.
- 3. SEBI Act of 1992.

Track Record

- The applicant seeking listing or the promoters/promoting company must have a track record of at least three years.

Redressal Mechanism of Investor Grievance

- The applicant must provide to the Stock Exchange all details of pending investor grievances against itself/its listed subsidiaries along with information relating to the mechanisms evolved for redressing these.

Rejection Cooling off period

- The applicant must not have had any rejections by the Exchange in the last six months.

Non-eligible issuers

- If the issuer, any of its promoters, promoter group, directors or selling shareholders are debarred from accessing the capital market by the Board
- If any of the promoters or directors of the issuer is a promoter or director of any other company that is debarred from accessing the capital market by the Board.
- If the issuer or any of its promoters or directors is a wilful defaulter or a fraudulent borrower.
- If any of its promoters or directors is a fugitive economic offender.

Figure 6: Eligibility for Listing Equity Instruments on the Main Board[11] [12]

[11] Details of defaults in respect of payment of interest and/or principal to the debenture/bond/fixed deposit holders by the applicant, promoters/promoting companies/group companies or subsidiary companies shall also be provided to the Stock Exchange. These will be considered while evaluating the application for listing.

[12] Figure 6 gives a brief outline of the eligibility requirements under the Issue of Capital and Disclosure Requirement Regulations that are mandatory, and also the eligibility requirements laid down by the NSE. The exchanges have their own specific requirements that must be fulfilled as well.

Outline of listing equity instruments on the SME Platform

Incorporation

- The issuer must be a company incorporated under the Companies Act 1956/2013 in India.

Post-Issue Paid-Up Capital

- The post-issue paid-up capital of the company (face value) shall not be more than Rs. 25 crore.

Track Record

- The applicant seeking listing or the promoters/promoting company must have a track record of at least three years.

Eligibility for Promoters

- Promoters must have a minimum of three years of experience in the same line of business and hold at least 20% of the post-issue equity share capital individually or together.
- The company/entity should have operating profit from operations for at least two out of the three financial years preceding the application, and its net worth should be positive.

Other Listing Requirements

- 1. No BIFR reference or Insolvency proceedings should have been made against the applicant and promoting companies.
- 2. The company must not have received any winding-up petition by an NCLT/Court.
- 3. The company must not have faced any regulatory or disciplinary action by stock exchanges or regulatory authorities in the past three years.

Disclosures in the Offer Document

- 1. Any regulatory or disciplinary action taken by a stock exchange or regulatory authority against the promoters/promoting company(ies), group companies, or companies they promote in the past year.
- 2. Payment defaults on debentures, bonds, fixed deposits, or to banks/financial institutions by the applicant or related parties in the last three years.
- 3. Information about the litigation record of the applicant, promoters/promoting company(ies), group companies or their promoted companies, including the nature and status of the litigation.
- 4. Status of criminal cases filed against the directors, including details of any ongoing investigations related to the alleged commission of offenses and their potential impact on the company's business.

Rejection Cooling off Period

- The applicant company must not have had any rejections by the Exchange in the last six months.

Figure 7 Eligibility for Listing Equity Instruments on the SME Platform

Outline of listing on the Innovators Growth Platform

Pre-Issue Capital

- On the date of filing the draft offer document with SEBI, 25% of the pre-issue capital of the company should have been held by one of the following for at least two years:
- 1. Qualified institutional buyer as mentioned in ICDR.
- 2. Family trust with net worth of more than Rs. 500 crore.
- 3. Accredited investors (AI) for the purpose of the Innovators Growth Platform.
- 4. Category III Foreign Portfolio Investor or an entity meeting the listed criteria.

Conditions Precedent to Listing

- The issuers on IGP must adhere to conditions precedent to listing emerging from:
- 1. Securities Contracts (Regulations) Act 1956.
- 2. Companies Act 2013.
- 3. Securities and Exchange Board of India Act 1992.
- 4. Any rules and/or regulations framed under the foregoing statutes, as well as any circular, clarifications and guidelines issued by the appropriate authority under the foregoing statutes.

Other Listing Conditions

- 1. The company, its promoter, group company or director must not appear in the willful defaulters' list of RBI.
- 2. No winding up petition against the company must be admitted by a competent court.
- 3. The company, group companies or subsidiaries must not have been referred to the Board for Industrial and Financial Reconstruction within a period of five years prior to the date of application for listing.
- 4. No regulatory action must have been taken against the company within a period of five years prior to the date of application for listing

Disclosures in the Offer Document

- 1. Defaults in respect of payment of interest and/or principal to the debenture/bond/fixed deposit holders, banks, FIs by the applicant, promoters/promoting company(ies), group companies or companies promoted by the promoters/promoting company(ies) during the past three years. An auditor's certificate shall also be provided by the issuer to the exchange, in this regard.
- 2. The applicant, promoters/promoting company(ies), group companies or companies promoted by the promoters/promoting company(ies) litigation record, the nature of the litigation, and the status of the litigation.
- 3. In respect of the track record of the directors, the status of criminal cases filed or the nature of the investigation being undertaken with regard to the alleged commission of any offense by any of its directors and its effect on the business of the company, where all or any of the directors of the issuer have or has been charge-sheeted with serious crimes like murder, rape, forgery, economic offenses, etc.

Figure 8: Eligibility Criteria for Listing Instruments (Debt and Equity) on the Innovators Growth Platform

Outline of listing debt instruments on the Main Board and SME Platform

Default in Payments

- The applicant must not be in default of payment of interest or repayment of the principal amount relating to any debt instruments, issued to the public, for a period of more than six months.

Credit Rating

- The applicant must have obtained a credit rating from at least one credit rating agency.

Debenture Trustee and Redemption Reserve

- The applicant must have appointed at least one debenture trustee in compliance with the Companies Act of 2013 and the SEBI (Debenture Trustees) Regulations of 1993. It should have also created a debenture redemption reserve in accordance with the Companies Act of 2013 and the rules therein.

Charge/ Security on Assets

- An applicant who proposes to create a charge/security on its assets in respect of secured debt instruments must ensure that:
- 1. The assets are sufficient to discharge the principal amount.
- 2. The assets are free from encumbrances.
- 3. Where a security in favour of a lender is already created on the assets, or the issue of debt instruments is to be secured by a security on leasehold land, the consent of such lender/lessor for a second charge must be submitted to the debenture trustee before opening the issue.
- 4. For instruments secured by a second charge, the asset cover will be arrived at after reducing the liabilities of a first charge.

Redemption

- The applicant must redeem the convertible debt instruments in terms of the offer document.

Figure 9: Eligibility Criteria for Listing Debt Instruments on the Main Board and SME Platform[13]

[13] The eligibility requirements for listing debt instruments on the Main Board (as contained in Regulations 9 and 10 of the ICDR Regulations) are the same as those for listing debt instruments on the SME (as contained in Regulations 231 and 232 of the ICDR Regulations).

B. Process for For-Profit Social Enterprises Undergoing Initial Public Offer on the Main Board and Small and Medium-Sized Enterprises Platform or Innovators Growth Platform

The listing process on stock exchange platforms is provided under SEBI regulations and is akin to the regular process followed by all companies undergoing an initial public offer (IPO). However, the regulations have eased the process of listing on the Innovators Growth Platform for startups.

The following figures provide a brief overview of the listing process stages that for-profit social enterprises will undertake while conducting their IPO on the Main Board and SME Platform (See Figure 9) and on the Innovators Growth Platform (See Figure 10).

Outline of the initial public offer process on Main Board and SME Platform

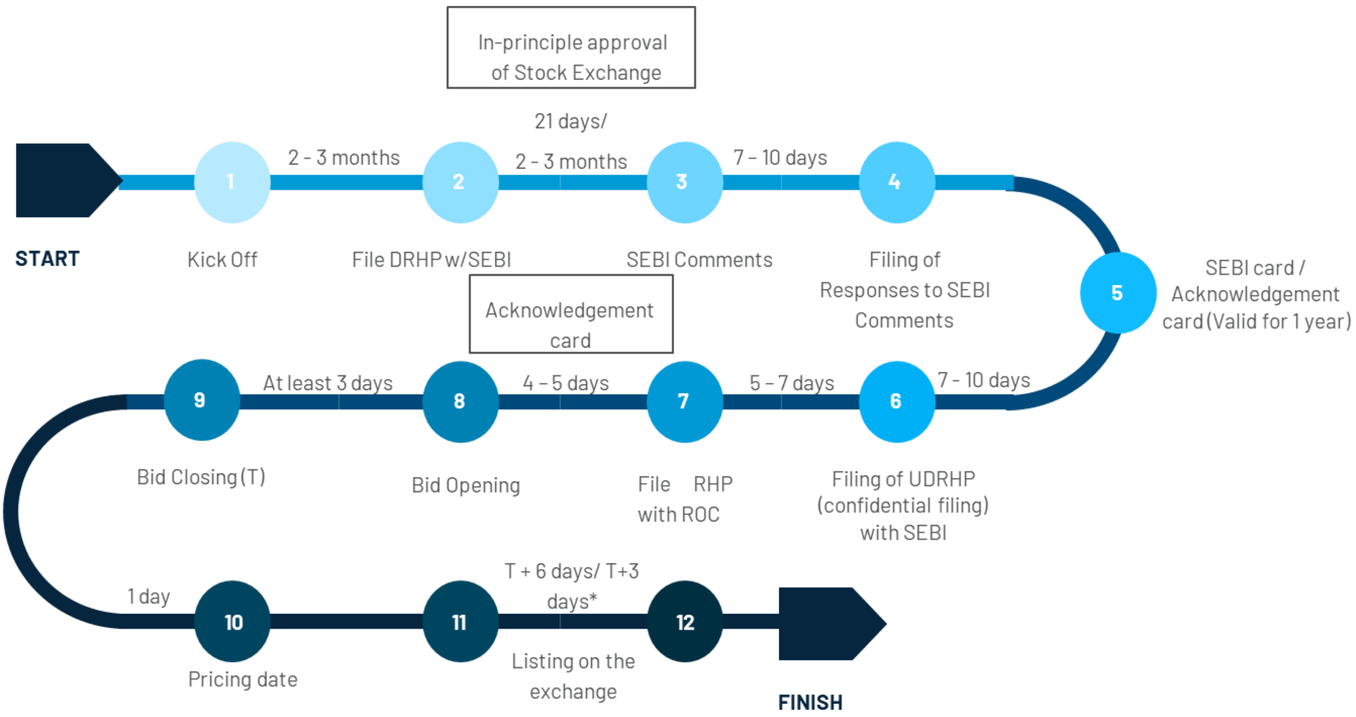


Figure 10: Stages of the initial public offer on the Main Board and SME Platform[14]

[14] Through its circular dated August 9, 2023, SEBI reduced the duration of the period, between the issue closure to listing from six to three working days. The T+3 timeline will be applicable on a voluntary basis for public issues opening after September 1, 2023 and mandatory for issues opening on or after December 1, 2023. Additionally, in its board meeting dated September 30, 2022, SEBI introduced an alternative method for IPOs where the offer document may be pre-filed by the issuing company. The document will be made available to the public after SEBI's initial review. The existing system of non-confidential IPOs will continue; companies may choose among the two methods.

Outline of the initial public offer process on the Innovator Growth Platform

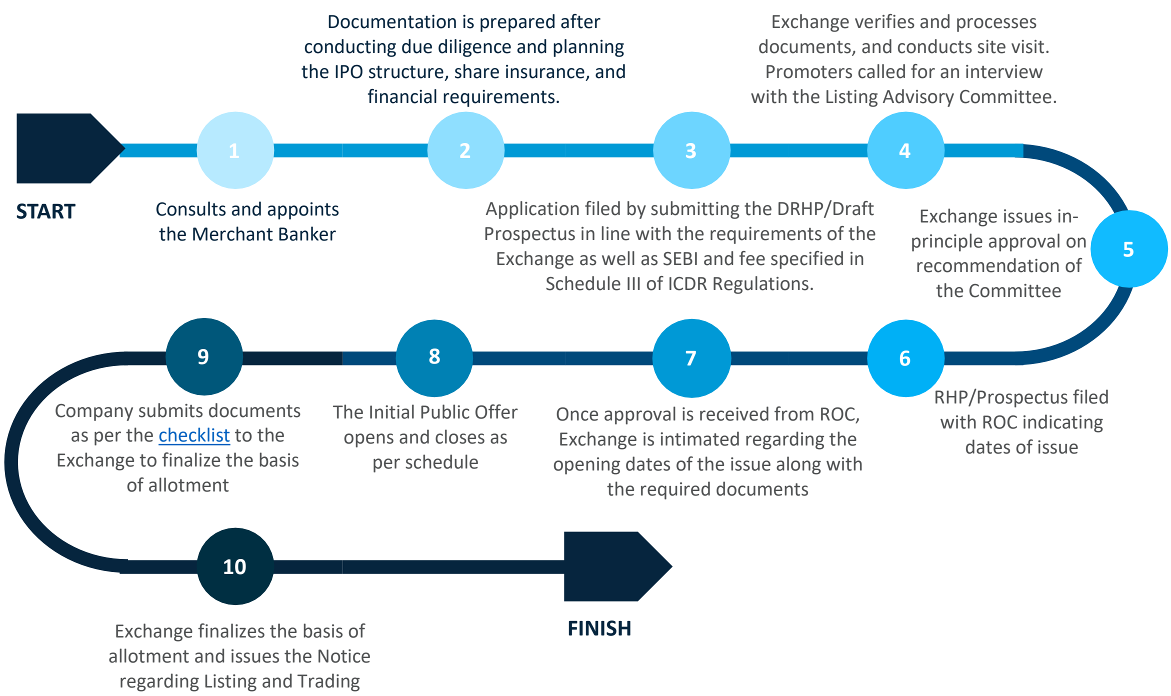


Figure 11: Stages of the initial public offer on the Innovators Growth Platform

6. Is It Mandatory for Social Enterprises to Register on the Social Stock Exchange?

Between for-profit enterprises and non-profit organisations, registration is mandatory for non-profit organisations only.[15] For-profit enterprises need not register on the SSE to raise funds through it. However, they must comply with all applicable SEBI regulations as needed for their fund-raising model.

7. Who Can Invest in Securities Issued by Social Enterprises on SSE?

Only institutional investors and non-institutional investors can invest in securities issued on the Social Stock Exchange.[16] Securities listed by for-profit social enterprises are listed on other stock exchange segments as well. Hence, they can receive investment from retail investors.[17]

8. Can Instruments Listed by For-Profit Social Enterprises be Traded on the Secondary Market?

Instruments issued by for-profit social enterprises are available for trading on the secondary market.

15 Regulation 292F (1). "Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations". 2018 [Last amended on January 14, 2022]; "Frequently Asked Questions (FAQs) on Social Stock Exchange." *National Stock Exchange*.

16 Regulation 292C. "Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations." 2018 [Last amended on January 14, 2022].

17 "Frequently Asked Questions (FAQs) on Social Stock Exchange." *National Stock Exchange*.

9. What Are the Mandatory Disclosures Required by For-Profit Social Enterprises?

All social enterprises are required to provide an annual impact report and disclose any material events as and when necessary.

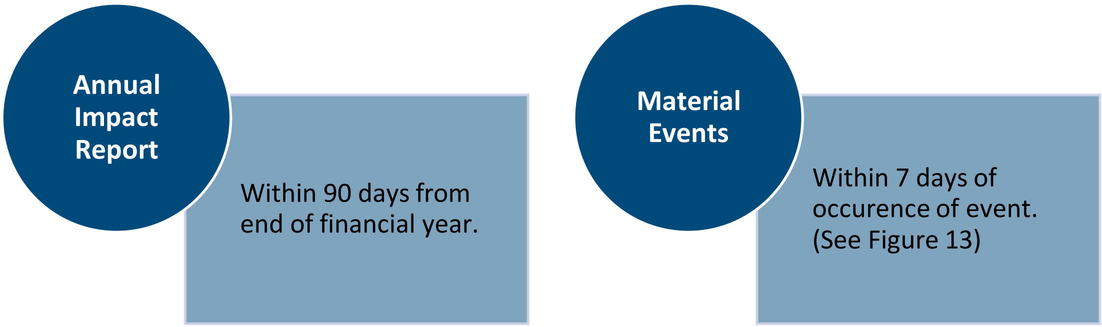


Figure 12: Mandatory Disclosures by Social Enterprises

10. What Should a Social Enterprise Disclose in an Annual Impact Report?

All social enterprises must disclose their annual impact report (AIR) in line with Regulation 91E of the LODR Regulations.

The AIR must capture the qualitative and quantitative aspects of the social impact generated by the entity and project (if applicable) for which funds have been raised on the SSE.

The following details must be captured by the AIR:

a. Strategic intent and planning

b. Approach

c. Impact score card

(Refer to Annexure I for the format and Annexure II for guidance)

11. Which Events Are a Social Enterprise Expected to Disclose to the Social Stock Exchange?

A social enterprise should disclose information about any material event. It is also expected to provide specific and adequate replies to any query asked by the SSE as soon as reasonably possible.

Moreover, everything disclosed to the SSE should also be disclosed on the social enterprise's website.

A. What Is a Material Event?

Put simply, a material event is any event that impacts a social enterprise's ability to achieve the outputs or outcomes declared to investors. Such an event should be disclosed within a reasonable period but no later than seven days after the event's occurrence.

B. How Should a Social Enterprise Prepare to Disclose a Material Event?

The regulations expect the board and management to establish a system to determine materiality. This includes formulating a policy on determining material events and appointing key personnel to oversee disclosures.

The figure below explains the regulatory expectations for the disclosure of material events.

How can social enterprises prepare to disclose material events?

Formulate policy on determining materiality of events.

↓

Ensure board or management approval of policy on determining materiality of events.

↓

Board authorization of one or more key managerial personnel to determine materiality of an event and ensure disclosure to SSE.

↓

Provide contact details of key managerial personnel.

Figure 13: Preparation for the Disclosure of a Material Event by a Social Enterprise

C. How Should a Social Enterprise Disclose a Material Event?

The regulations provide the process and requisite details that should be followed by a social enterprise while disclosing material events. The infographic below gives an overview of the stages of disclosing and the details required.

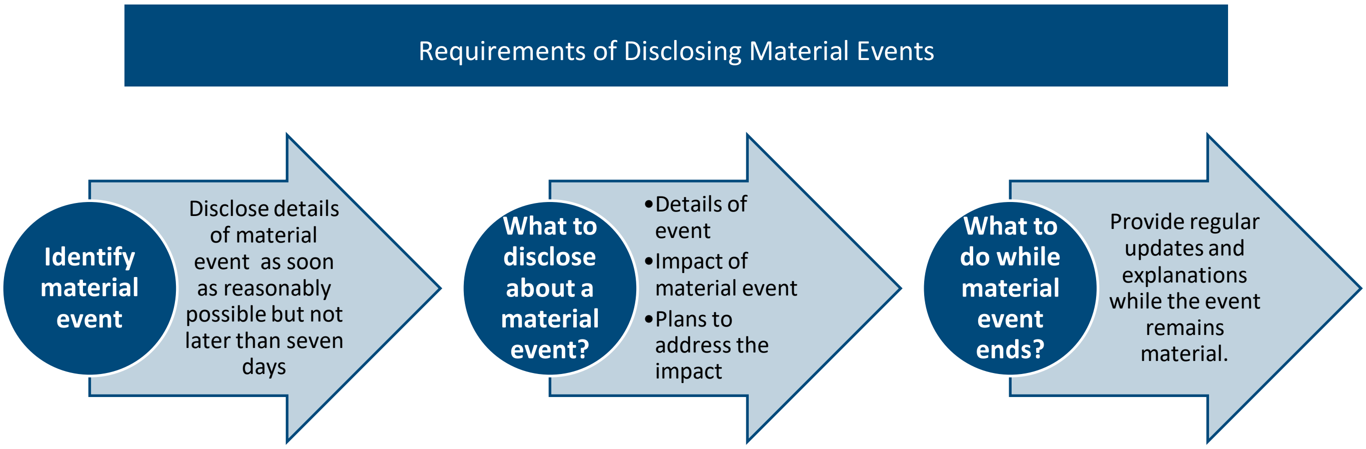


Figure 14: The Process for Disclosing Material Events

D. What Should One Do if a Material Event Is Reported in the Media?

The social enterprise can confirm or deny any reported event on its own initiative to the SSE or stock exchanges.

CHAPTER 4: Finance Models Involving For-Profit Enterprises and Legal Considerations

Once securities have been issued, for-profit social enterprises will have to address legal requirements arising from other Indian laws and regulations applicable to their securities and related transactions. This chapter presents a comprehensive understanding of laws and regulations that may have an impact on transactions from the securities issued on the Social Stock Exchange and related platforms.

1. Income Tax Act

A. What Income Tax Considerations Arise for a For-profit Entity Raising Funds on the Social Stock Exchange?

1. Capital Gains Tax on Equity Instruments

As per Section 112A of the Income Tax Act (ITA), long-term capital gains (LTCG) arising from a listed equity share will be taxed at 10% without the indexation benefit. Securities Transaction Tax (STT) is chargeable only to such transactions undertaken through a recognized stock exchange, and the Section is applicable only when STT is paid.[18] This implies that the off-market trade of listed equity shares (e.g., LTCG) does not fall under the ambit of Section 112A, and the applicable tax rate for such transactions is 20% with indexation benefits or 10% without indexation benefits, whichever is lower.

Short-term capital gains (STCG), where a transaction is chargeable with STT, fall under Section 111A and are taxed at 15%. Not chargeable to STT, those transactions will be added to the total income and are taxable at applicable slab rates.

The figure below provides a succinct explanation of the requirements applicable to equity issues.

18 Ministry of Finance. 2017. "Notification No. 43/201 [F. No. 370142/09/2017-TPL]/SO 1789". *Government of India Press*.

Capital Gains Tax on Equity Instruments of For-Profit Social Enterprise on SSE			
S. No.	**Description**	**On-market trade**	**Off-market trade**
1	Holding period	i. 'Short-term capital gains' if held for 12 months or less before transfer; and ii. 'Long-term capital gains' if held for more than 12 months.	
2	Long-term capital gains tax[19]	Section 112A[20] provides that capital gains arising from the transfer of a long-term capital asset, being an equity share in a company or a unit of an equity-oriented fund, shall be taxed at the rate of 10% of such capital gains exceeding Rs. 1,00,000. Provided that STT is paid on the transfer of such shares and acquisitions (in the case of an equity share in a company). Note that the indexation benefit is not provided.	i. 20% after giving effect to indexation benefit if available (exclusive of applicable surcharge and cess); or ii. 10% before giving effect to the indexation benefit (exclusive of applicable surcharge and cess), whichever is lower.
3	Short-term capital gains tax[21]	Section 111A[22] provides that capital gains arising from the transfer of a short-term capital asset being an equity share in a company or a unit of an equity-oriented fund shall be taxed at the rate of 15% (exclusive of applicable surcharge and cess as applicable). Provided that STT is paid on the transfer of such shares and acquisition	Section 111A excludes off-market trade (i.e., STCG) arising on the sale of equity shares other than a recognized stock exchange. In such cases, income is taxable at applicable slab rates.

Figure 15: Income Tax on Capital Gains of Equity Instruments Issued by For-Profit Social Enterprises

19 Income Tax Department. 2023. " Tax on Long-Term Capital Gains." Income Tax Department.
20 Section 112A, Income Tax Act. 1961.
21 "Tax on Long-Term Capital Gains." Income Tax Department. 2023.
22 Section 111A, Income Tax Act, 1961.

2. Capital Gains Tax on Debt Instruments

While Section 112A of ITA deals with taxation on LTCG on equity shares in a company, a unit of an equity-oriented fund or a unit of a business trust, Section 112 is the provision for taxation on LTCG other than those covered under Section 112A. Long-term capital assets under Section 112 cover "listed securities".

The explanation to this section reads as,

For the purposes of this sub-section, —

> *(a) the expression "securities" shall have the meaning assigned to it in clause (h) of Section 2 of the Securities Contracts (Regulation) Act, 1956 (32 of 1956);*
>
> *(aa) "listed securities" means the securities which are listed on any recognized stock exchange in India;*
>
> Section 2(h)(i) of the Securities Contracts (Regulation) Act, 1956 includes *"shares, scrips, stocks, bonds, debentures, debenture stock or other marketable securities of a like nature in or of any incorporated company or other body corporate".*

(Emphasis added.)

Upon analysing Section 112 and the explanation provided, it can be inferred that debt instruments fall under this section. Hence, the applicable tax rate for LTCG under Section 112 is 10% without indexation benefit or 20% with indexation benefit, whichever is lower. For STCG, Section 111A is usually referred to, but as Section 111A only covers STCG arising on the sale of equity shares, anything other than these is taxed at a normal slab rate.[23] Hence, STCG on debt instruments on and off-market fall are taxable at applicable tax slab rates.

Given below is a concise explanation of the legal framework relevant to debt issues.

Capital Gains Tax on Debt Instruments of For-Profit Social Enterprise on SSE			
S. No.	**Description**	**On-market trade**	**Off-market trade**
1	Long-term capital gains tax	i. 20% after giving effect to indexation benefit if available (exclusive of applicable surcharge and cess); or ii. 10% before giving effect to the indexation benefit (exclusive of applicable surcharge and cess), whichever is lower.	--
2	Short-term capital gains tax[24]	Taxable at applicable slab rates.	Taxable at applicable slab rates.

Figure 16: Income Tax on Capital Gains of Debt Instruments Issued by For-Profit Social Enterprises

23 "Tax on Long-Term Capital Gains." Income Tax Department. 2023.

24 "Tax on Long-Term Capital Gains." Income Tax Department. 2023.

2. Goods and Services Tax

A. Is Goods and Services Tax chargeable on securities listed on the Social Stock Exchange?

Securities, including shares, will not be considered either goods or services under the Central Goods and Services Tax Act (CGST Act) as per a clarification issued by the Central Board of Indirect Taxes and Customs on 17th July 2023. Thus, Goods and Services Tax (GST) will not be applicable on the sale or purchase of securities listed on the SSE.

3. Alternate Investment Fund

A. How Are Social Impact Funds Different from Social Venture Funds?

In July 2022, SEBI amended the regulations on Alternative Investment Funds (AIFs) to rechristen Social Venture Funds as Social Impact Funds. Social Impact Funds fall under Alternative Investment Funds Category I. Previously, Social Venture Funds had to adhere to the same conditions as the rest of Category I funds. They could also only invest in social ventures, which limited their investment basket to non-profits and microfinance institutions. Following the amendments, specific conditions have been crafted for Social Impact Funds along with introducing allowing investment in social enterprises, which expands their investment ambit.

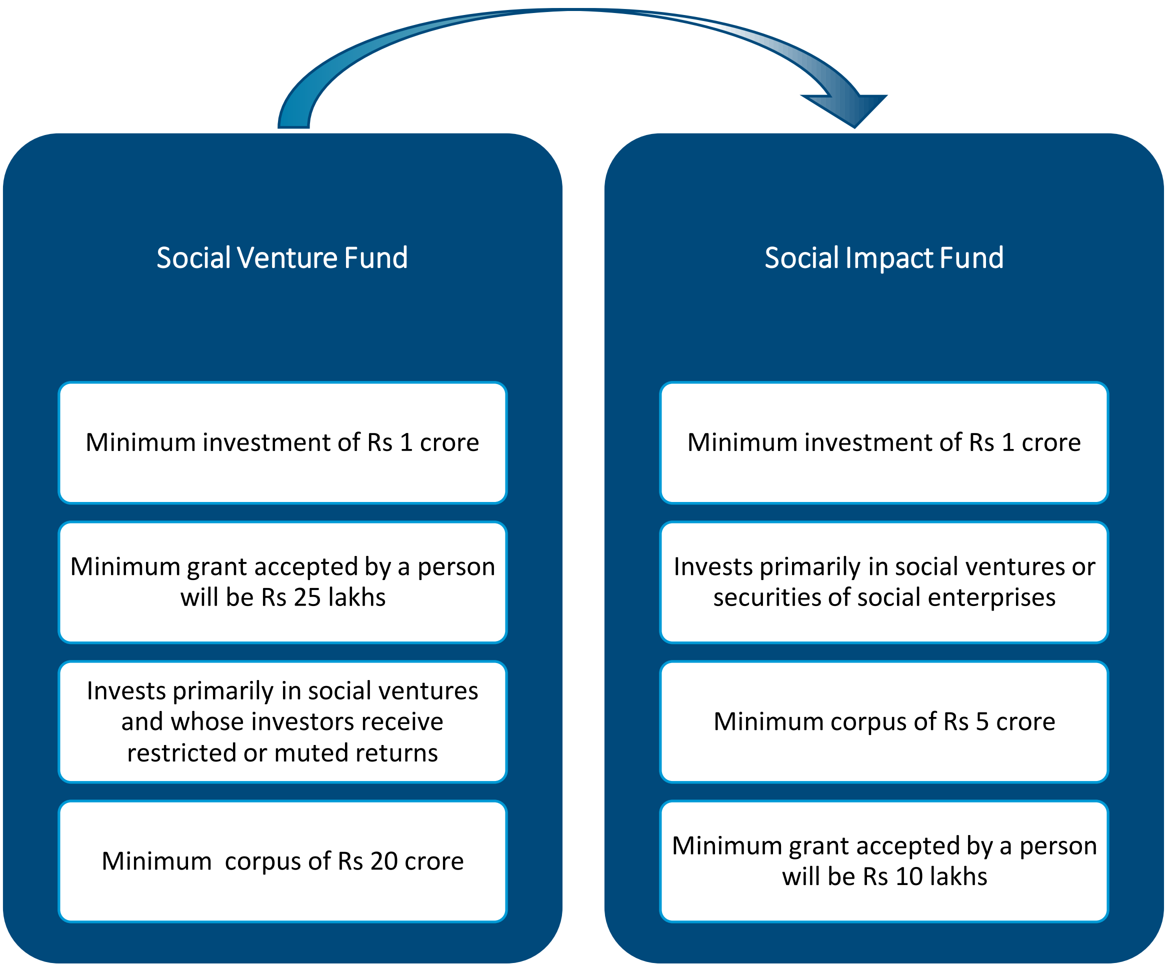


Figure 17: Difference between Social Venture Funds and Social Impact Funds under SEBI Regulations

B. What Are the Conditions for Social Impact Funds under AIF Category I requirements?

Conditions for Social Impact Funds under AIF Category I

Can invest in investee companies, venture capital undertakings, special purpose vehicles, limited liability partnerships and units of other Category I AIF of the same sub-category or units of Category II AIF.

Investors, other than accredited investors, must grant at least Rs 10 lakhs minimum

At least 75% will be invested in unlisted securities, partnership interest of social ventures, units of social ventures, or securities of social enterprises

What can SIFs (AIF-I) do?

- Can give grants to securities of social enterprises while making required disclosures in placement memorandum.
- Can engage in hedging and credit default swaps as per regulations.

What SIFs (AIF-I) not do?

- Cannot borrow funds or engage in leverage.
- Exception: for meeting temporary funding requirements and for not more than 30 days. This can happen only four times and amount to maximum 10% of investable funds.

Figure 18: Investment Conditions for Social Impact Funds under AIF-I norms.

4. Corporate Social Responsibility

A. Can Corporate Social Responsibility Money Go into For-Profit Social Enterprises?

No direct provision allows or disallows corporate social responsibility (CSR) spending to go to for-profit social enterprises. The law specifically mentions, in Section 8, that companies, trusts or societies are recipients of CSR grant money, thus giving it a narrow ambit.

B. Can Corporate Social Responsibility Money Be Used to Pay Interest to Risk Investors?

The legal position on whether CSR money can be used to pay risk investors is unclear. Moreover, there is a risk of negative market perception due to which such payments may not be allowed. The Ministry of Corporate Affairs (MCA) circular clarifies the purposes for which CSR funds can be utilized.[25] It excluded activities undertaken in the course of business activities or fulfilled under any statutory

[25] "Frequently Asked Questions (FAQs) on Corporate Social Responsibility" (General Circular No. 14/2021). Government of India, Ministry of Corporate Affairs. 2021.

law.[26] There is a likelihood that using CSR money as payment to a risk investor can be viewed as a business activity.

Moreover, CSR expenditure cannot be incurred on activities beyond Schedule VII. The activities undertaken in pursuance of the CSR policy must be relatable to Schedule VII of the Companies Act 2013. The items enlisted in Schedule VII of the Act are broad-based and are intended to cover a wide range of activities. The entries in the said Schedule VII must be interpreted liberally to capture the essence of the subjects enumerated in the said Schedule.

26 "Frequently Asked Questions (FAQs) on Corporate Social Responsibility" (General Circular No. 14/2021). Government of India, Ministry of Corporate Affairs. 2021.

CHAPTER 5: Policy Recommendations on the Social Stock Exchange

<table>
<tr><th>No.</th><th>Challenge</th><th>Recommendation</th></tr>
<tr><td>1</td><td colspan="2">Framework: SSE Regulations and SEBI Regulations</td></tr>
<tr><td></td><td>Non-profit organisations can raise funds on the SSE by issuing Zero Coupons Zero Principals (ZCZPs). For-profit social enterprises can do so by issuing equity shares/debt instruments. Presently available instruments like ZCZP are unsuitable for outcome funding models, which are the most prevalent in this space.

ZCZPs function like grants and cannot facilitate the flow of returns from the social enterprise to the risk investor. This renders the entire outcome funding model untenable.</td><td>Through an amendment to the SSE Regulations and SEBI Regulations, explicitly define the following phrases:
▪ <u>Outcome funder</u>: An institutional or government entity that releases funding to an agent, non-profit or otherwise, under a contract upon the latter's achievement of pre-defined social outcomes.
▪ <u>Risk investor</u>: An actor in an outcome funding model who provides upfront capital to an agent, non-profit or otherwise, to achieve agreed social outcomes for the term of the contract.
▪ <u>Impact bond</u>: An instrument that facilitates both non-profit and for-profit social enterprises to raise funds through one of the following models:
– Debt-based model: The bond shall allow the risk investor to provide debt financing to a registered entity, against which the investor shall be able to receive returns. A government entity shall act as an outcome funder in this tripartite model.
– Service-fee model: Through this bond structure, the risk investor shall pay a service fee to the registered entity for certain predefined outcomes. Once the outcomes are achieved, the investor will be eligible for a service fee from the outcome funder.

Explicitly defining these terms and creating an impact bond as a single listable instrument will aid the ecosystem that the SSE set out to enable. Models like the service-fee-based one will also reduce financial risks for the social enterprises, allowing them to better achieve outcomes.</td></tr>
<tr><td>2</td><td colspan="2">Corporate Social Responsibility</td></tr>
<tr><td></td><td>The current position of the law as to whether CSR funds can be utilised in outcome funding models is unclear. Due to this, the market perception has</td><td>▪ The MCA has recently outlined the need for CSR to be used to enhance corporate sustainability through a process that promotes transparency and accountability.[27] Infusing funds into non-profit or for-</td></tr>
</table>

[27] "Monthly Newsletter." *Ministry of Corporate Affairs.* 2023. Vol. 66.

No.	Challenge	Recommendation
	generally disallowed the use of these funds to say, for example, pay interests/ returns to risk investors on their capital.	profit social enterprises listed on the SSE is the ideal way to achieve this goal. The disclosure requirements that must be followed by any enterprise listed on the SSE enhance transparency and iron out communication between funders and social enterprises. ▪ Companies should be encouraged to prioritise investing in enterprises listed on the SSE when using CSR funds. This can be done through either a clarification by the MCA or an amendment to Schedule VII of the Companies Act of 2013, which lists the permissible goals for which CSR funds may be deployed.
3	**Goods and Services Tax**	
	In outcome funding models, there is a risk that the grants paid by outcome funders upon the achievement of certain milestones may be characterised as a service, thus attracting GST. Such characterisation also brings with it heavy reporting requirements, which is a huge compliance burden for the actors in this model. This can disincentivise organisations from opting for outcome funding contracts.	Previous circulars by the department have made it clear that donations that are philanthropic in nature and made without a quid pro quo element would not qualify as a 'supply of service'. Grants made by outcome funders are also meant to enhance social outcomes for public purposes. The Department of Revenue can release a circular clarifying that GST will not be applicable on grants made by these funders for the fulfilment of predefined social objectives.
4	**Foreign Contribution Regulation Act**	
	Most outcome funding models are heavily dependent on grants from foreign investors. The process for obtaining permission to receive such funds is tedious and, as a matter of practice, open only to non-profit social enterprises. For-profit entities are thus unable to participate in outcome funding models with foreign contributions despite operating as social enterprises.	Instead of following a prior permission route, foreign capital under outcome funding contracts channelled through the SSE should be allowed under the automatic approval route. This is especially important considering the transparency that funds routed through the SSE enjoy, given the regulatory oversight involved. Keeping in mind the concerns around the misuse of funds, such automatic approval should at least be provided in cases where a government or its agency acts as an outcome funder. Where a branch of the government is involved, possibly the risk of misuse is significantly lesser.

No.	Challenge	Recommendation
5	**Income Tax Act**	
	As per the Union Budget 2023, if a charitable institution donates a grant received by another registered trust/ institution, only 85% of such donations shall be exempt from tax. These changes were aimed at preventing any misuse of tax exemption provisions through chain donations. Such restrictions risk discouraging genuine sub-granting transactions, leading to increased obligations for all charities due to misuse by a few.	It must be ensured that genuine sub-granting transactions are not unduly affected by the newly imposed restrictions. The Central Board of Direct Taxes can issue circular/binding instructions excluding the applicability of such restrictions from legitimate sub-granting arrangements facilitated fully or in part through the SSE.

ANNEXURE-I

Annual Impact Report

The Annual Impact Report should at a minimum, cover the aspects described below.

a. Strategic Intent and Planning

i. What is the social or environmental challenge the organisation and/or the instrument listed is addressing? Has this changed in the last year?

ii. How is the organisation attending to the challenge or planning to attend to the challenge? Has this changed in the last year?

iii. Who is being impacted (target segment)? Has this changed in the last year?

iv. What will be the outcomes of the activities, intervention, programmes or project? Disclosure should include positive and potential unintended negative outcomes.

b. Approach

i. What is the baseline status/situation and analysis/context description at the start of the activity/intervention/programmes or project and at the end of the last reporting period?

ii. What has been the past performance trend (if relevant)?

iii. What is the solution implementation plan and what measures have been taken for the sustainability of the activity/intervention/program or project outcomes? Has there been any material change in your implementation model in the last year?

iv. Please briefly outline the alignment of solutions to the Sustainable Development Goals (SDGs)/national priorities/state priorities/developmental priorities.

v. How have you taken into consideration stakeholder feedback in this reporting period?

vi. In the last year, what have you seen as the biggest risks to the achievement of the desired impact? How are these being mitigated?

c. Impact Score Card

i. What are the matrices monitored, and what has been the trend?

ii. Briefly include narratives of impact on target segment(s) in the reporting period.

iii. Beneficiary/stakeholder validation through surveys and other feedback mechanisms.

ANNEXURE-II

Guidance Note for All Social Enterprises on the Annual Impact Report

a. Strategic Intent and Planning

i. What is the social or environmental challenge the organisation or the instrument listed is addressing? The problem statement is to be explained in detail. The challenge, its extent, causes and consequences, and the part of the problem statement the organisation and the instrument are trying to address shall be explained.

ii. How is the organisation planning to attend to the challenge or how is it attending to the challenge?

iii. The approach the organisation or the specific instrument will be using or is already using needs to be explained. The organisation shall also explain what change is resulting for the targeted beneficiaries and what proportion of the target group is experiencing the change.

iv. Who is being impacted (target segment)?

The target beneficiaries/stakeholders cover various kinds of target groups. Include the organisation's internal definition of the "target segments" it seeks to serve, usually along one or more of the three dimensions, namely:

- Income (driven by socio-demographic and/or behavioural characteristics);
- Geography (ecosystem or geographic characteristics driven by population density (urban/rural), administrative boundaries, terrain, etc.); and
- Thematic issue (gender, caste, community that places the target segment at a disadvantage that has economic and non-economic consequences).

Where the target segment is a specific geographic region in its entirety, state so. Thematic issues could be one or more of the following: conservation of resources, generation via renewable resources, reduction in waste, conservation (say of land, wildlife, historical monuments, etc.) and reduction in toxic substances. Also, bring out possible deviations that might have occurred in the reporting period.

v. What will be the outcomes of the solution/programme? Coverage should include positive and potential unintended negative outcomes.

Describe the theory of change/logic model framework (defining input(s), output(s) and outcome(s)) for the solution proposed. While identifying the targeted impact segment, both positive and potential unintended negative impacts need to be identified.

b. Approach

i. What is the baseline status/situation and analysis/context description at the start of the activity, intervention, programme or project?

The baseline measurement is done to establish the starting point in any activity, intervention, programme or project. The measurements give the depth of the challenge and/or the spread of the challenge. The organisation will establish the right kind of measurements, keeping the end or what the organisation or instrument wants to achieve since the baseline will be used to measure what actually changed due to the intervention. In the absence of a baseline study, a detailed situation analysis is to be mentioned.

ii. What has been the past performance trend?

For any ongoing activity, intervention, programme or project explain the key past performance trends; for a proposed activity, intervention, programme or project, the narrative should explain the experience of similar programmes in similar situations.

iii. What is the solution implementation plan and what measures have been taken for the sustainability of programme outcomes?

A detailed implementation plan is to be mentioned, capturing all the essential activities. The interventions can be either perennial support or time-bound support. In case of time-bound support, the organisation shall explain the exit strategy and how it ensures that the outcomes achieved will be sustained. In the case of perennial support, the organisation can also explain how it will ensure the sustainability of the project/programme. Also, bring out possible deviations that might have occurred in the reporting period.

iv. Please briefly outline the alignment of solutions to SDGs/national priorities/state priorities.

Explain the alignment of the activity, intervention, programme or project to respective SDGs and national/state priorities and schemes.

v. How have you taken into consideration stakeholder feedback in this reporting period?

The organisation to mention how they have mapped and prioritised the key stakeholders for the engagement. The reporting shall include the list of stakeholders engaged, their feedback and how the organisation used the feedback.

vi. In the last year, what have you seen as the biggest risks to the achievement of the desired impact? How are these being mitigated?

Mention the key potential risks pertaining to the organisation or the specific instrument that could hamper/hinder the achievements of desired intended outcomes in the last year and the steps or strategies taken by the organisation to mitigate the same.

c. Impact Scorecard

i. What are the matrices monitored, and what has been the trend?

The trend in performance shall be explained through the trend of the data across the output, outcome and impact matrices that are established by the organisation. The matrices will capture the reach of the activity, intervention, programme or project as well as the level of inclusiveness of the impact being generated (direct, indirect, extended). This shall help evaluate the delta change that has occurred in the lives of various target stakeholders (including the environment) due to the solution. The matrices monitored shall target to cover the reach, depth and inclusion.

Reach - Outreach metrics for the target segment(s) served:

- The proportion of the target segment(s) who have been reached in the reporting period
- The proportion of the target segment(s) who accepted the organisation`s solution

- What part of the planned activity, intervention, programme or project has been accomplished in the reporting period
- Cumulative reach (members of the target segment served since inception)
- Other suitable metrics in relation to the solution usually relate to people, institutions or activities (e.g., monthly active users of MAUs for an app/tech platform). These can be considered as needed, where the target segment is the specific geographic region.

Depth - The depth of impact on the median individual (of the target segment(s))

Surveys (1% of the customers/recipients or at least 200 respondents per organisation) asking respondents, 'Has your quality of life changed', with response options being: very much improved, slightly improved, no change, got slightly worse, got much worse.

Alternatively, social enterprises can compare themselves to different 'case studies' of high-, medium- and low-depth organisations.

Inclusion - The social enterprise must consider for itself how its approach intends to improve inclusion for its customers/recipients along one or more of the following themes.

- Theme 1: Net increase in income levels of customers/recipients among target segment(s) as decided by the organisation. The organisation can self-select 'low', 'medium' or 'high'.
- Theme 2: Diversity and inclusion: The social enterprise exhibits how it prioritises the inclusion of these disadvantaged groups or communities (either as owners, partners or customers) and empowers them in their relationship with the social enterprise over time.
- Theme 3: Social equity: The social enterprise exhibits how its approach has resulted in the disadvantaged group or community experiencing increased social equity. This can be through a survey as above or through qualitative criteria such as details of its strategy, processes and internal accountability/governance processes that have resulted in an internal culture that values and works towards achieving social equity for the disadvantaged group or community.

ii. What are the highlights or achievements in the reporting period?

The organisation should mention key highlights, achievements, challenges and/or disappointments during the reporting period.

iii. Beneficiary/stakeholder validation

It is of the utmost necessity to capture the perspectives of programme stakeholders to draw a holistic picture of the impact/change that has been achieved by the programme. Stakeholder voices also help in capturing information that will help validate the impact claims. This can establish a check and avoid over-claiming. The validation process shall answer the following questions:

- What would have happened in the absence of this activity, intervention, programme or project?
- How much did the activity, intervention, programme or project contribute to the changes that are evidenced?

- How many unintended negative impacts happened due to the activity, intervention, programme or project?

ASPEN NETWORK OF DEVELOPMENT ENTREPRENEURS

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