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REGULATORY

Bridging Corporate Social Responsibility and Capital Markets: An Analysis of MCA’s Recognition of ZCZP Instruments on the Social Stock Exchange

AUTHOR Rahul Sundaram, Akriti Singhal

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Introduction

The Ministry of Corporate Affairs (MCA), through Notifications G.S.R. 415(E) and G.S.R. 416(E) dated 27 May 2026, has introduced a significant development in India's Corporate Social Responsibility (CSR) framework. By recognizing subscriptions to Zero Coupon Zero Principal (ZCZP) Instruments issued by eligible Not-for-Profit Organisations (NPOs) on the Social Stock Exchange (SSE) as a valid mode of CSR implementation, the MCA has created a direct regulatory bridge between corporate philanthropy and capital market infrastructure.

While the amendments do not alter the mandatory CSR expenditure obligations under Section 135 of the Companies Act, 2013, they fundamentally expand the mechanisms through which CSR funds can be deployed. The reform reflects a broader policy objective of enhancing transparency, accountability, and efficiency in the utilization of CSR resources.

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Understanding the Regulatory Framework

The reform has been implemented through two complementary notifications.

First, G.S.R. 415(E) inserts Rule 4A into the Companies (Corporate Social Responsibility Policy) Rules, 2014, permitting companies to implement CSR projects by subscribing to ZCZP instruments listed on the Social Stock Exchange.

Secondly, G.S.R. 416(E) amends Schedule VII of the Companies Act, 2013 by inserting Item XIII, expressly recognizing subscription to ZCZP instruments on the SSE as a permissible CSR activity.

Together, these amendments eliminate the regulatory uncertainty that previously surrounded the treatment of ZCZP subscriptions as CSR expenditure.

Social Stock Exchange and ZCZP Instruments: The Concept

The Social Stock Exchange, established under the regulatory framework of the Securities and Exchange Board of India, functions as a dedicated segment of recognized stock exchanges for facilitating fundraising by social enterprises and not-for-profit organizations.

A Zero Coupon Zero Principal Instrument is a unique financial instrument characterized by two defining features:

- It carries no interest obligation.
- It does not provide repayment of principal.

Consequently, unlike traditional securities, a ZCZP instrument generates no financial return for the subscriber. The subscription amount effectively functions as a regulated donation routed through securities market infrastructure.

The instrument therefore combines philanthropic intent with market-based transparency and disclosure requirements.

Closing the Regulatory Gap

Before the 2026 amendments, the SSE framework already permitted eligible NPOs to issue ZCZP instruments. However, companies were uncertain whether subscriptions to such instruments could be treated as valid CSR expenditure under Section 135.

The absence of express statutory recognition created a disconnect between SEBI's social financing framework and the CSR regime under company law.

The MCA notifications have now resolved this issue by formally integrating both frameworks. Significantly, Rule 2(1)(ha) of the CSR Rules adopts SEBI's definition of a Not-for-Profit Organisation, thereby ensuring consistency between securities regulation and corporate law.

This harmonized approach enhances regulatory certainty while encouraging greater participation by both corporates and social enterprises.

The New Rule 4A: Structure and Safeguards

Voluntary Adoption

The use of ZCZP instruments remains entirely optional. Companies may continue implementing CSR projects through traditional methods such as direct implementation, registered implementing agencies, or collaborative arrangements.

The amendment merely introduces an additional route rather than replacing existing mechanisms.

The Ten Percent Ceiling

One of the most notable features of Rule 4A is the restriction that expenditure through ZCZP instruments cannot exceed ten percent of a company's annual CSR obligation.

This limitation serves several purposes:

- Preventing excessive reliance on passive funding mechanisms.
- Preserving direct corporate engagement with social development initiatives.
- Limiting exposure to a relatively new fundraising ecosystem.
- Allowing gradual market development within the SSE framework.

The cap indicates that the legislature views the SSE as a supplementary mechanism rather than the primary avenue for CSR implementation.

Time-Bound Project Execution

Rule 4A requires that projects financed through ZCZP instruments be completed within three succeeding financial years from the date of issuance.

This requirement introduces a structured timeline that promotes:

- Accountability,
- Timely utilization of funds,
- Measurable outcomes, and
- Prevention of indefinite project delays.

Unlike conventional grant arrangements, SSE-funded projects are therefore subject to stricter execution timelines.

Protection of Unspent Funds

Another noteworthy safeguard is the treatment of unspent funds.

Where the listing of a ZCZP instrument is terminated and any funds remain unutilized, the NPO must transfer the unspent amount to a fund specified under Schedule VII of the Companies Act and submit compliance reports to SEBI.

This provision ensures that CSR capital remains dedicated to public welfare purposes even if the original project fails or is discontinued.

Governance Implications for Companies

Contrary to some initial perceptions, the amendment does not eliminate corporate governance responsibilities.

The Board of Directors and the CSR Committee continue to bear ultimate responsibility for compliance under Section 135.

Compliance Relaxations

Rule 4A provides limited exemptions, including:

- Exemption from impact assessment requirements under Rule 8(3).
- Exemption from CFO utilization certification under Rule 4(5).
- Exemption from specific ongoing project monitoring obligations under Rule 4(6).

These relaxations recognize that SSE-listed projects are already subject to a robust disclosure and monitoring framework overseen by stock exchanges and SEBI.

Continuing Obligations

Despite these exemptions, companies must continue to:

- Obtain CSR Committee recommendations.
- Secure Board approval for ZCZP subscriptions.
- Ensure compliance with annual CSR reporting requirements.
- Verify that the issuing NPO satisfies SEBI's eligibility criteria.
- Maintain adherence to the 10% ceiling prescribed under Rule 4A.

Therefore, the amendment simplifies certain procedural requirements but does not diminish fiduciary oversight.

Accounting and Tax Considerations

The notifications operate solely within the framework of company law and do not amend tax legislation.

Accordingly, existing tax principles remain relevant.

Income Tax Implications

Expenditure incurred towards mandatory CSR obligations continues to be subject to Explanation 2 to Section 37(1) of the Income-tax Act, 1961, which generally disallows CSR expenditure as a business deduction.

Similarly, companies should not assume that subscriptions to ZCZP instruments would qualify for deductions under Section 80G merely because they are routed through the SSE.

Accounting Challenges

The MCA has not prescribed a specific accounting treatment for ZCZP subscriptions.

Questions remain regarding:

- Initial recognition,
- Measurement,
- Presentation in financial statements,
- Disclosure requirements under applicable accounting standards.

Further guidance from the Institute of Chartered Accountants of India may be necessary to ensure uniform accounting practices.

Remaining Areas of Uncertainty

Although the amendments establish the legal framework, several practical questions remain unanswered.

These include:

1. Whether CSR action plans must identify specific ZCZP issuances at the approval stage.
2. The manner in which CSR reporting formats will capture SSE-specific transaction details.
3. The evidentiary standards auditors should apply when verifying project completion.
4. The accounting classification of ZCZP subscriptions.
5. Additional guidance that may be issued by the MCA, SEBI, or ICAI.

As the framework evolves, these issues are likely to become the subject of professional and regulatory clarification.

Conclusion

The MCA's recognition of Zero Coupon Zero Principal Instruments as an eligible CSR implementation mechanism marks an important evolution in India's CSR ecosystem. By integrating the Social Stock Exchange with the statutory CSR framework, the amendment introduces a regulated, transparent, and disclosure-driven channel for deploying corporate social responsibility funds.

Although constrained by a 10% ceiling, the reform has the potential to strengthen accountability, standardize disclosures, and improve access to funding for credible not-for-profit organizations. More importantly, it signals a broader policy shift toward leveraging market institutions to advance social development objectives.

Whether the mechanism achieves widespread adoption will depend on the quality of projects listed on the Social Stock Exchange, the confidence of corporate boards in the regulatory framework, and the timely issuance of practical guidance by the MCA, SEBI, and ICAI. Nevertheless, the amendment represents a significant step toward aligning corporate philanthropy with modern financial infrastructure and may shape the future trajectory of social finance in India.

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