

A woman with long dark hair, wearing a blue ruffled-sleeve shirt, is seen from the side, looking at a wooden bookshelf filled with books. She has blue nail polish and is wearing a ring. Her left arm is raised, and she is wearing a watch and several colorful beaded bracelets. The background is a library setting with many books on shelves.

Changing Regulatory Paradigm of Corporate Social Responsibility

Adjusting to the changing
regulatory paradigm

April 2021

The EY logo consists of the letters 'EY' in a bold, white, sans-serif font. A yellow chevron shape is positioned above the 'Y'.

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Executive summary

In 2014, India became the second country in the world (after Mauritius) to mandate spend on Corporate Social Responsibility (CSR) by introducing specific provisions through Section 135 of the Companies Act, 2013 (CA 2013). The new law required companies to spend in a given financial year, at-least two percent of their average net profits earned over the preceding three financial years subject to satisfying certain qualifying conditions. The Board of Directors were required to explain reasons for underspend, if any, in the company's Annual Report. Over the years, these provisions underwent changes and more recently, with an objective to reinforce compliance, anti-abuse and strengthen governance, transparency and flexibility, the MCA has introduced significant changes through the Companies (Amendment) Act, 2020 and the Companies (Corporate Social Responsibility Policy) Amendment Rules, 2021 to amend the CA 2013 and its related rules.

The amended rules became effective from 22 January 2021 and require close review as they directly impact implementation of a company's CSR initiatives and also introduce new concepts like a specific negative list in the CSR definition, mandatory treatment of CSR underspend, mandatory impact assessment, mandatory registration by NGOs undertaking CSR activities, etc. These changes are likely to trigger impact across regulatory, accounting, finance and tax domains.

The key amendments in the CSR Rules are as follows:

- » Negative list introduced in the CSR definition; Obligation on the Board to ensure that disbursed funds are utilized as approved and monitor implementations (fund allocations / timelines) of ongoing projects;
- » CSR implementing NGOs are required to be registered for income tax and company law purposes;
- » Companies are required to mandatorily spend their CSR obligation;
- » Unspent CSR amounts at year end are required to be transferred out as prescribed depending on whether the underspend relates to an ongoing project or not to a Government notified funds within six months;
- » Penalty on company and Board members for failure to transfer unspent amounts as prescribed;
- » Creation/acquisition of CSR capital assets by companies is prohibited;
- » Ongoing project is defined as a multi-year project that shall not extend beyond three years excluding the year of commencement;
- » Amount spent in excess of CSR obligation can be carried forward and set-off in next three financial years;
- » Companies are required to carry out impact assessment mandatorily for CSR projects meeting specified thresholds;
- » Reporting format for disclosures is revamped.

Companies have to evaluate the following key considerations to comply with the amended CSR provisions and CSR rules:

1

Companies to re-assess whether their CSR expense policy is in compliance with newly defined CSR expense in light of detailed negative list.

2

Companies to assess their policy, procedures and controls around CSR spending to comply with revamped CSR rules which cast obligation on the Board collectively and members individually for ensuring CSR expenses are mandatorily incurred during the year, last mile spending is in compliance with CSR policy of Company, CSR vehicles are registered with the government, impact assessment has been carried out etc. Non-compliance shall result in penalty on the Company as well as officers of the Company.

3

Amended rules are likely to require strong processes to meet the requirements around accounting, taxation and Companies Act perspective. Companies need to align their compliance calendar, revamp controls around CSR spending, put in place policy & process for monitoring of the last mile CSR spending by CSR vehicles associated with the Company and ensure that any unspent amount is transferred to the Govt. mandated funds on timely basis.

4

The Companies need to put in place policy, process and control around impact assessment of the projects meeting the threshold limit.

5

Companies need to review their books of accounts for capital assets created in the past and put in place mechanism to transfer such assets in time bound manner. This shall require larger consideration from structuring of transaction, accounting, compliance and taxation perspective.

6

CSR rules requires companies to transfer the unspent amount to the Govt. mandated fund within 180 days from financial year end except for the fund allocated to an ongoing project. Companies need to review their financial closure process to understand the impact of this regulation to ensure compliance.

Notification No. G.S.R. 40(E) dated 22 January 2021
(http://www.mca.gov.in/Ministry/pdf/CSRAmendmentRules_23012021.pdf)

Background

The Government has amended Companies (Corporate Social Responsibility Policy) Rules, 2014 with an objective to increase accountability, transparency and flexibility.

The Ministry of Corporate Affairs had constituted a High-Level Committee (CSR HLC) in September 2018 to review of CSR framework and make recommendations to develop a more robust and coherent CSR regulatory and policy framework including underlying ecosystem. The HLC submitted its report on August 2019 and consequent amendments are in line with the recommendations made by CSR HLC. The recommendations such as registration of implementing agency, impact assessment, creation of capital assets through CSR spending, etc. form part of the amended rules.

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1. Definition of Corporate Social Responsibility (CSR)

CSR Rules have introduced the concept of negative list in the definition of CSR. Some of these ineligible CSR activities were mentioned earlier in the CSR Rules and certain circulars issued by the MCA. These activities have now been consolidated and listed in the CSR Rules. Following items are specifically excluded from the ambit of the CSR definition:

Activities in normal course of business	activities undertaken in pursuance of normal course of business of the company but does not include research and development activity of new vaccine, drugs and medical devices related to COVID-19 for financial years 2020-21, 2021-22, 2022-23, subject to conditions as specified in notification
Activities benefiting employees	activities benefitting employees of the company as defined in clause (k) of section 2 of the Code on Wages, 2019
Sponsorship	activities supported by the companies on sponsorship basis for deriving marketing benefits for its products or services
Statutory obligations	activities carried out for fulfilment of any other statutory obligations under any law in force in India
Sponsoring sports personnel	any activity undertaken by the company outside India except for trainings of Indian sports personnel representing any State or Union territory at national level or India at international level
Political donation	contribution of any amount directly or indirectly to any political party under section 182 of the CA Act, 2013

Points to ponder

- » The CSR Committee and Board should finalize the CSR projects/ programs as per the amended provisions
- » Spend by a company in relation to the specific exclusions mentioned in CSR rules shall not be considered as CSR expenses in financial statements and such amounts shall be charged out of the profits of the company.



Guiding Principles:

Guiding principle for CSR spend is to promote public good and spend should not be for activities which are specifically restricted e.g. statutory obligation or political donation. Any financial transaction, e.g. purchase of goods and services from social enterprises that directly benefit the employees of the company (such as gifts purchased from local NGO for employees, set up of a school for the benefit of

employees' children etc) or the Company is not to be treated as CSR spend. Financial benefit arising to the Company or its employees could be incidental e.g. school created for a village where children of employee's as well go for study. One needs to exercise judgement in terms of extent of benefit to employees vis-à-vis society at large.

Points to ponder



Companies to re-assess whether their CSR expense policy is in compliance with newly defined CSR expenses in light of detailed negative list.



When can an activity be treated as being in the 'normal course of business' and subject to disqualification?



Whether an activity incidentally benefiting 'employees' can also be disqualified?



When can a sponsorship be treated as deriving 'marketing benefits' for a company's products or services and be subject to disqualification?



1A. Administrative overheads

Rule 2(1)(b) defines “administrative overheads” as the expenses incurred by the company for ‘general management and administration’ of CSR functions. This shall not include the expenses directly incurred for designing, implementation, monitoring, and evaluation of a particular CSR project/ program.

Rule 7(1) mandates the Board to ensure that expenses falling within the ambit of ‘administrative overheads’ do not exceed 5% of the total CSR expenditure in a financial year.

- ▶ It is important to note that this limit of 5% is not intended to cover expenses directly linked to a particular CSR project/ program.
- ▶ Further, the amount incurred in excess of 5% of overall CSR spend on administrative overheads will not be treated as CSR spend and shall be borne by the Company from its profit. Tax deductibility of the excess spend on administrative overheads (beyond 5%) considering that the excess amount will not be treated as CSR spend.

Points to ponder



The Rules obligate the company’s Board to ensure that administrative overheads do not exceed 5% of the total CSR expenditure in a financial year. The Board therefore needs to evaluate and review their policy, procedure and controls to

- identify the items that may be treated as eligible and ineligible administrative overheads,
- ensure that eligible expenditure incurred is within limits and
- identify the excess spent, if any, including accounting considerations related to excess spend.

Such evaluation and review require revisiting of the significant policies of the Company and re-alignment of financial closure process for appropriate accounting and disclosures related to the excess spent.



Can payments to implementation agencies include a portion related to ‘administrative overheads’ incurred by such agencies on managing their CSR function? What about payments to implementation agencies for designing, monitoring and evaluating the Company’s CSR projects?



What is the tax deductibility of excess spend on administrative overheads (beyond 5%) considering that the excess amount will not be treated as CSR spend?



2. Mandatory registrations for CSR vehicles

CSR rules provides that the Board shall ensure that the CSR activities are undertaken by the company itself or through following legal vehicle:

 Vehicle	 Requirements
a) Sec 8 Company	1. Registered under section 12A and 80 G of the Income Tax Act, 1961 and established by the Company either singly or along with other company; or
b) Registered public trust	2. Established by Central Government or State Government; or
c) Registered Society	3. Any other Sec 8 company registered under Sec 12A and 80G of the Income Tax Act, 1961 and have a track record of three years in undertaking similar activities
d) Government formed entities	any entity established under an Act of Parliament or a State legislature

Every entity e.g. section 8 Company, registered society that intends to undertake any CSR activity, shall register itself with the Central Government by filing the form CSR-1 electronically with the Registrar, with effect from the April 1, 2021. It means that entities covered under Rule (4)(1) can only be appointed as implementing partners for CSR project implementation.

- ▶ This registration is to be automatically approved and the entity is to receive a unique CSR Registration Number on filing the form
- ▶ The Amendment has also clarified that this registration requirement will not affect CSR projects or programs approved prior to 01 April 2021 i.e. ongoing projects / programs as on 01 April 2021 may continue.

- ▶ There may be several implementation agencies that are risky to partner with, given any past, current or potential litigation, fraud, bankruptcy, media concerns or any non-compliant affiliations. These anomalies could have possible implications on the Company's program implementation and relatedly, its reputation and brand value. Hence, basis these registrations under the CA 2013 and the ITA 1961, the Government is looking to validate the bona fides of CSR implementation agencies.
- ▶ ICAI has recommended that wherever Companies undertakes the CSR activity through a third party / NGO, it is advised that all such companies should obtain an independent practitioner's report on utilization of such CSR funds from the auditor / Chartered Accountant in practice of the third party / NGO, to whom the funds are given by the Company for implementing CSR activity. **(Advisory-for-Independent-Practitioners-Report-on-Utilization-of-CSR-Funds_hosted.pdf (icai.org).**

Points to ponder

- ▶ Boards need to set-up a process to ensure that CSR agencies associated with the companies are registered as prescribed. Further, control should be placed around receiving and verifying the registration certificates at the time of disbursement of funds and such verification may be carried out at periodic intervals to ensure continued compliance by the CSR agencies.
- ▶ Should verification of registrations in case of step-down implementation agencies be considered?
- ▶ Should spend by unregistered implementation agencies during a financial year be disregarded in determining a company's overall CSR spend?
- ▶ There may be some implementation agencies that are registered under alternative tax exemption sections of the ITA 1961 for e.g. Section 10(23). Will such agencies be disregarded as eligible CSR vehicles?
- ▶ Has Company completed a legal and reputational check of the Implementation agency? Does Company have a well-defined due diligence policy and underlying procedures in place to identify any potential 'Red Flag', if any?



3. Recognition of CSR obligations

Section 135 (5) of the Company Act 2013 requires the Board of every company to 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.

- ▶ The CSR obligations should be recognized after preparation of annual financial statements. Also, if the amount as per annual financial statements is near the threshold, the accounts of each quarter/month should be analyzed to check the applicability of CSR expenditure.
- ▶ When to recognize the CSR expenses is a pertinent issue and should be an important agenda item. In this regard the following may be noted that-
- ▶ An obligating event arises when CSR activities (spend/incur) are undertaken during the financial year in accordance with the CSR Policy and CSR project approved by the Board of Directors of the Company. An obligating event for unspent amount arises as at the end of the financial year on its determination, whether it is related to an ongoing projects or not, after duly considering the requirements of Section 135 of the Company Act, 2013. Thus, the obligating events requiring recognition of CSR expenditure and a liability occur as follows:
 - ▶ during the financial year, when carrying on CSR activities (spending/incurred);
 - ▶ at the end of financial year, to the extent of the unspent amount relating to:
 - (i) ongoing projects; and
 - (ii) other than ongoing projects.
- ▶ Accordingly, any CSR expenditure shall be recognized as an expense in the statement of profit or loss when it is incurred on CSR activities undertaken as per Board approved CSR policy and CSR projects during the financial year.
- ▶ For any unspent amount, a legal obligation arises to transfer unspent amount to specified accounts depending upon the fact whether such unspent relates to an ongoing project. Therefore, the liability for such unspent amount needs to be recognized as at the end of a financial year by Companies.
- ▶ Further as per Ind AS 34, Interim Financial Statements, CSR obligations to be recognized based on the principles for recognition of the same in annual financial statements.

Points to ponder



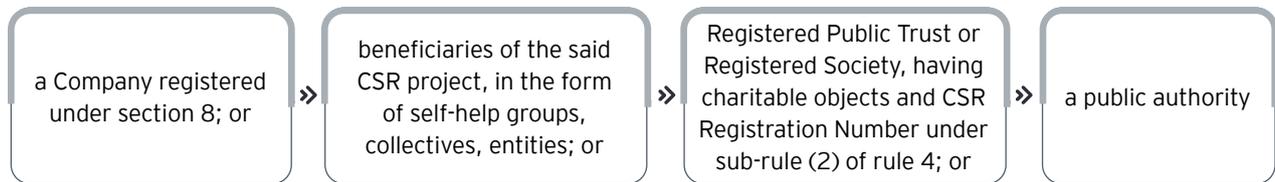
CSR provisions require compulsory spending of 2% of average profits of preceding three years towards CSR activities by a company.





4. Creation/acquisition of assets

CSR Rules provide that the CSR amount may be spent by the company for 'creation or acquisition' of a capital asset. This capital asset 'created or acquired' out of CSR funds cannot be held directly by the company. It can only be held by any of the entities prescribed i.e.



Provided that any capital asset created by a company prior to the commencement of the companies (Corporate Social Responsibility Policy) Amendment Rules, 2021, shall within a period of one hundred and eighty days from such commencement, comply with the requirement of this rule, which may be extended by a further period of not more than ninety days with the approval of the Board based on reasonable justification.

- ▶ The key terms used and not defined here are 'beneficiaries' and 'public authority'. While the definition of 'public authority' is defined under other laws such as Right to Information Act, 2005, the term 'beneficiaries' should be analyzed for each project and could only be in certain forms, as specified.
- ▶ The tax considerations associated with transfer to, and receipt of CSR assets by implementing agencies (by way of voluntary / corpus donations, etc.) will have to be evaluated.
- ▶ The amended CSR Rules provide restrictions on ownership of CSR capital assets by companies and mandated transfers of CSR assets created prior to 22 January 2021, to prescribed entities.
- ▶ Companies that had created capital assets as part of their CSR programs and had capitalized the same in their books in the past will not be able to continue with the past accounting treatment. Such companies shall have to revise their accounting policy and provide for expensing the amounts to be spent on creation of capital assets.
- ▶ Further, companies with capital assets in their books as on January 22, 2021, will have to de-recognize the carrying value of assets within stipulated time. Such de-recognition shall not be considered as CSR spend for the year.
- ▶ Companies shall have to evaluate the terms of the transfer and do appropriate accounting on transfer of assets in the income statement. However, if such assets are capitalized at nominal value, then there shall be no significant impact on the financial statement of the Company

Points to ponder

- ▶ Companies will need to review their significant accounting policies and past practices around capitalization of assets to meet the requirements of the CSR Rules. Further, Companies need to review their existing policies, procedures and controls around their CSR spends involving capital assets creation from a broader legal angle and from the perspective of compliance with the CA 2013 requirements i.e. appropriate handover of the assets to any of the prescribed transferee agencies.
- ▶ Companies need to establish a mechanism for structuring transfer of existing capital assets, accounting for transfer and income tax obligations. If a company requires extended time of two hundred and seventy days, it needs to bring such agenda to the Board meeting for its approval in a time bound manner. Companies should evaluate whether such transfers could be considered as current year spend and reduce their obligation for financial year ended 2022?
- ▶ Company will need to see tax implications associated with transfer of assets forming part of block of assets of the company to implementation agencies, beneficiaries or public authorities (i.e. the impact on past depreciation claims, trigger of capital gains/ losses, stamp duty implications etc) to be considered.



5. Unspent amounts, carry forward and set-off of excess spend and surplus

Revised CSR rules specifies detailed guidance on treatment of unspent CSR amount, excess amount spend and its carry forward, set-off and any surplus arising from the CSR activities.

5A. Unspent amounts in relation to 'ongoing' or other projects

Section 135(6) of the CA 2013 require a Company to open an Unspent CSR Account for unspent amount relating to Ongoing Projects and transfer unspent amounts to this account within 30 days from the end of a financial year.

In case of other projects, unspent CSR amount shall be transferred to the fund specified in Schedule VII within 6 months from the end of financial year. Further, a Company is required to transfer the unspent CSR amount relating to Ongoing Project from Unspent CSR Account to funds specified in Schedule VII, within 30 days of the completion of the 3 financial years, if the transferred amount still remains unspent at the end of this period.

CSR rules defines "Ongoing project" as a multi-year project undertaken by any Company in fulfilment of its CSR obligation which shall not exceed three financial years excluding the financial year in which the project was commenced. This shall also include such project that was initially not approved as a multi-year project but whose duration has been extended beyond one year by the board based on reasonable justification.

Relatedly, Rule 10 of the CSR Rules provides that until a fund is specified in Schedule VII for the purposes of sub-section (5) and (6) of section 135 of the Act, the unspent CSR amount, if any, shall be transferred by the company to any fund included in Schedule VII.

- ▶ The Company needs to create an obligation towards CSR relating to an ongoing project and amount transferred to unspent CSR account should be carried as an asset under 'Restricted cash and cash equivalents.
- ▶ A Company having unspent CSR amounts at year end related to projects other than ongoing projects needs to account for the prescribed transfer to a Fund by setting off the transfer against the CSR liability recognised in the books. The same treatment would apply in case of unspent CSR amounts related to ongoing projects that remain unspent at the end of three financial years and are transferred to a Fund. The monitoring requirement for identification of unspent amount to cover last mile e.g. If a Company provides fund to NGO for a specified project, then such company needs to monitor the spending to ensure that fund has been spent by NGO for specified project within the financial year. In case, NGO does not spend the money, it would be considered as unspent fund in the hands of such donor Company.
- ▶ Transfer of unspent amounts of CSR projects for consecutive years indicate/ communicate the need for better planning / monitoring CSR activities and spend.
- ▶ Details of unspent amounts reported in the Annual Reports are accessible to all stakeholders and periodic shortfalls could negatively impact the social value, brand value and reputation of the Company.

Points to ponder

- ▶ Has the company evaluated its existing policy, procedure and controls to closely monitor spending per the prescribed requirement either by itself or by its implementing agencies?
- ▶ Has the company evaluated the implications of underspend in relation to years prior to the year of commencement of the amended CSR Rules i.e. year ended March 31, 2021?
- ▶ In view of the introduction of the concept of 'ongoing projects', has the company identified the CSR projects that should fall within this category? Projects with a known duration exceeding 4 years (including year of commencement) cannot be treated as ongoing projects. Company should transfer unspent CSR amounts from Unspent CSR Account to funds specified in Schedule VII.
- ▶ What happens if an ongoing project extends beyond the prescribed period? How should related Unspent CSR amounts be treated? Do separate unspent CSR accounts need to be opened for each project?
- ▶ Has the company analyzed the treatment of the CSR expenditure transferred to implementing agencies but not entirely spent by such agencies within the relevant financial year?

5B. Carry forward and set-off of excess CSR spend

CSR Rules provide that CSR expenditure incurred in excess of the requirement under Sec 135(5) in financial year can be set-off in three succeeding years. CSR rules also prescribes two pre-conditions before the excess CSR amount is set off

- i) the excess CSR amount should not include any surplus generated out of CSR activities;
 - ii) the Board should pass a resolution permitting the set-off.
- ▶ Companies will have to ensure that the excess amounts spent are direct CSR expenses and not revenues/ surplus generated from CSR activities themselves, which in any event have to be tracked separately and ploughed back into the CSR activity or transferred to prescribed Funds or an Unspent CSR Account (to be spent subsequently).

- ▶ The Board approval should be preceded by an approval of the CSR Committee for better governance.
- ▶ The amount eligible for carry forward subject to the Board resolution is in the nature of a pre-paid expense and the company would be entitled to create a pre-paid asset in its books for the same, if it meets both the conditions provided in the Rules. This may be adjusted against the Company's future obligations in the immediate three succeeding years.

Points to ponder



CSR rules provides for the carry forward of excess CSR spend during a financial year and such excess can be set-off in next three years from its obligations provided a Board resolution has been passed approving the set-off. In light of this, has company put in place appropriate mechanisms to introduce a resolution for approval at the Board meeting at the appropriate time? Additionally, has the company reviewed its significant accounting policy for carry forward and set-off of excess spend and are processes and controls in place to identify the excess spend?



What happens to surplus CSR spend of years prior to the year in which the amended CSR Rules have been notified i.e. year ending March 31, 2021?

5C. Surplus arising out of CSR

Under Rule 7(2), any surplus arising out of CSR activities shall not form a part of the business profit of the company. The surplus can be utilized through either of the following options only:

- i) It shall be ploughed back to the same project;
- ii) transferred to the Unspent CSR Account and spent in pursuance of the CSR Policy;
- iii) transferred to any Fund specified in Schedule VII of the Act within a period of six months of the expiry of the financial year.
 - ▶ The Amendment acknowledges the fact that surplus may be generated while carrying out CSR activities and accordingly prescribes the usage of such surplus

- ▶ It would also strengthen the monitoring and application of the utilization of the surplus arising out of CSR activities of a company.
- ▶ The surplus arising out of CSR activities shall not be considered as business profit of the company. The rules require the same to be either ploughed back into the same project or transferred to a specified fund or an unspent CSR account.
- ▶ This would mean, any surplus arising out of CSR activities cannot be accounted as income and would be required to be reduced from the expense relating to the same project.

Points to ponder



CSR Rules provides that any surplus arising out CSR activities shall not be considered as income of a Company and shall be ploughed back to the same project. Company to put in place procedure and mechanism to identify such surplus and ensure that such surplus has been utilized for same project without being accounted as income of a Company. This may require review of the financial closure process.



Has the Company analyzed the implications of surplus if the project is already completed and closed?





6. Impact assessment (IA)

The amended Rules mandate Impact Assessment for qualifying companies (with average CSR obligation of INR 10 crores or more in last three financial years) with respect to projects of minimum INR 1 crore size and completed at least 1 year prior to the date of Impact Assessment. The Impact Assessment is required to be carried out through an independent agency. The impact assessment reports shall be placed before the Board and shall be annexed to the annual report on CSR.

This requirement has been introduced following the recommendations of the CSR HLC. The CSR HLC recommended that Impact Assessment should be undertaken for certain projects with large outlays, to identify areas where intervention is required for the benefit of marginalized communities.

CSR Rules place limits on the amount which can be spent towards the impact assessment to be considered as part of the CSR expenditure during a financial year at INR 50 lacs or five percent of total CSR expenditure for that financial year, whichever is lower.

Impact assessment report shall be placed before the Board and annexed to the annual report on CSR.

- ▶ The rules do not specify the period or number of projects to be covered for impact assessment i.e. whether all past projects completed at least 1 year prior to the impact assessment that meet the minimum threshold of INR 1 crore should be subjected to an impact assessment or would it be as per the Board's discretion.
- ▶ Companies that have identified multiple projects for Impact Assessment may incur expenses in excess of the prescribed limit. This will lead to the question around how this excess expense shall be recorded. Amount incurred in excess of the threshold should be borne by the Company from its profit and will not be treated as CSR spend
- ▶ The categorization/ boundaries of CSR projects are not clearly defined, as some projects are defined by the Memorandum of understanding, themes and geographical reach.
- ▶ Impact Assessments are to be executed based on viable and validated models such as Impact Reporting and Investment Standards (IRIS), Log frame approach (LFA), Social returns on Investment (SROI) and theory of change. These models help in assessing impact through tested approaches and scientific analysis.
- ▶ These Impact Assessment studies also aid in understanding the journey and effectiveness of a company's CSR agenda and goals and therefore, helps it take strategic decisions or corrective action where required.
- ▶ Board shall be taking cognizance of the Impact Assessment Studies and shall also be presenting such studies as part of the Annual Report in CSR section of the Company

Points to ponder

- ▶ The revised Rules provide that a Company shall mandatorily carry out Impact Assessment for projects having an outlay of more than one crore and completed at-least one year prior to the date of assessment. Has the Company put in place, a policy and process to identify the projects to be selected for the impact assessment? Do 100% of all qualifying projects completed at least 1 year prior to notification of the amended Rules need to be considered?
- ▶ Decision on choice of the specific agency to be appointed for carrying out the Impact Assessment. Whether a Board approval is required for such selection of projects and appointment of professional agencies?
- ▶ What should be the criteria adopted for concluding the Impact Assessment of the identified projects?
- ▶ Rules places a limit of five percent or rupee fifty lacs, whichever is lower, which can be spent towards impact assessment for being considered as part of the CSR spent. Companies need to evaluate and review their policy, procedure and controls to identify the excess spend, if any. Accounting considerations related to excess spend, if any, to be considered which will require revisiting the significant policies of the Company and re-alignment of financial closure process for appropriate accounting and disclosures.
- ▶ What is the next step for the Company after impact assessment i.e. what are the steps a Company should take if the desired results are not achieved from a CSR project? How can the Board or CSR Committee effectively use the impact assessment for remedial action?
- ▶ Tax deductibility of the excess spend on Impact Assessment (beyond 5%) considering that the excess amount will not be treated as CSR spend?



7. Increasing responsibility of Board, CSR committee and Chief Financial Officer

Amended CSR rules has cast enhanced obligation on the Board, CSR Committee and Chief Financial Officer of the Company for monitoring, evaluation and reporting of CSR activities of the Company.



Specific obligation of Board includes:

- » Rule 4(1) requires Board to ensure that CSR activities are undertaken by the Company itself or the implementing partners mentioned in the provisions e.g. Sec 8 Company;
- » Rule 4(5) requires Board to satisfy itself that the funds so disbursed have been utilized for the purposes and in the manner as approved by Board;
- » Rule 4(6) requires monitoring of the implementation of the project with reference to the approved timelines and year-wise allocation and shall be competent to make modifications, if any, for smooth implementation of the project within overall permissible time period;
- » Board is required in Rule 7(1) to ensure that the administrative overheads does not exceed five percent of total CSR expenditure of the company for the financial year;
- » Rule 4(3) provides that Board to pass a resolution for carry forward and set-off of the excess CSR spend by the Company;
- » Rule 7(4) requires Board to pass resolution for extension of the time period in which the Company shall transfer existing capital assets with reasonable justification;
- » Rule 8(1) provides that the Board's Report of a company covered under these rules pertaining to any financial year shall include an annual report on CSR containing particulars specified in Annexure I or Annexure II, as applicable;
- » Under rule 9 of revised CSR rules, the Board of Directors of the Company shall mandatorily disclose the composition of the CSR Committee, and CSR Policy and Projects approved by the Board on their website, if any, for public access.
- » Sec 135(4) of the Company Act, 2013 require Board to approve the Corporate Social Responsibility Policy for the company after taking into account the recommendations made by the Corporate Social Responsibility Committee and disclose contents of such Policy in its report and also place it on the company's website, if any, in such manner as may be prescribed; and ensure that the activities as are included in Corporate Social Responsibility Policy of the company are undertaken by the company
- » Sec 135(5) of the Company Act, 2013 provides that 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. Further, if the company fails to spend such amount, the Board shall, in its report made under clause (o) of sub-section (3) of section 134, specify the reasons for not spending the amount and, unless the unspent amount relates to any ongoing project referred to in sub-section (6), transfer such unspent amount to a Fund specified in Schedule VII, within a period of six months of the expiry of the financial year.



Specific obligation of Chief Financial Officer includes

- » Rule 4(5) of revised CSR rules requires Chief Financial officer to certify that the funds disbursed under CSR have been utilized for the purposes and in the manner as approved by the Board of Directors of the Company.



CSR Committee

- » Sec 135(1) of the Companies Act requires every Company having net worth of Rupees 500 crores or more, or turnover of Rupees one thousand crore or more or a net profit of Rupees five crores or more during the immediately preceding financial year to constitute a CSR committee.
- » CSR committee shall consist of three or more Directors, out of which at least one director shall be Independent Director of the Company. However, if a Company is not required to appoint an independent director under section 149 of the Company Act, 2013 then CSR committee shall have two or more directors who are not necessarily required to be independent.
- » With respect to a foreign company covered under these rules, the CSR Committee shall comprise of at least two persons of which one person shall be as specified under clause (d) of sub-section (1) of section 380 of the Act and another person shall be nominated by the foreign company.
- » CSR committee shall:
 - » formulate and recommend to the Board, a Corporate Social Responsibility Policy which shall indicate the activities to be undertaken by the company in areas or subject, specified in Schedule VII, namely:
 - (i) the list of CSR projects or programs that are approved to be undertaken in areas or subjects specified in Schedule VII of the Act;
 - (ii) the manner of execution of such projects or programs as specified in sub-rule (1) of rule 4;
 - (iii) the modalities of utilization of funds and implementation schedules for the projects or programs;
 - (iv) monitoring and reporting mechanism for the projects or programs; an
 - (v) details of need and impact assessment, if any, for the projects undertaken by the company;
 - » recommend the amount of expenditure to be incurred on the activities referred to in clause (a); and
 - » monitor the Corporate Social Responsibility Policy of the company from time to time.
 - » Board may alter the plan at any time during the financial year, as per the recommendation of its CSR Committee, based on the reasonable justification to that effect
- » Rule 5 of revised CSR rules provides that CSR Committee shall formulate and recommend to the Board, an annual action plan in pursuance of its CSR policy, which shall include the following, namely
 - (i) the list of CSR projects or program that are approved to be undertaken in areas or subjects specified in Schedule VII of the Act;
 - (ii) the manner of execution of such projects or programs;
 - (iii) the modalities of utilization of funds and implementation schedules for the projects or programs;
 - (iv) monitoring and reporting mechanism for the projects or programs; and
 - (v) details of need and impact assessment, if any, for the projects undertaken by the company

Provided that Board may alter such plan at any time during the financial year, as per the recommendation of its CSR Committee, based on the reasonable justification to that effect.



8. Penal provisions

Section 135, sub-section 7 has been amended to provide for a specific penalty on non-compliance with section 135 (5) or (6). Revised provisions provide penalties for Company and every officer of the Company as mentioned below:

Company

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.

Every officer

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.

- ▶ The payment of above-mentioned penalties do not extinguish the company's obligation to transfer unspent CSR amounts either to the Fund specified in Schedule VII or the Unspent Corporate Social Responsibility Account.
- ▶ It is to be noted that for other defaults under Section 135 (excluding Section 135(5) and 135 (6)) and the CSR Rules, penalties can still be levied under the residual provisions contained in Section 450 of the Companies Act, 2013
- ▶ The penal provisions reinforce the mandatory nature of CSR obligations.
- ▶ The penalties introduced for non-compliance are not compoundable.

Points to ponder

- » There are now both general and specific penalties leviable under the CA 2013 for non-compliance with the CSR provisions. The Board should prepare a detailed checklist of processes with owners and timelines, to monitor continued compliance of CSR regulations by the Company. The compliance agenda could be strengthened if the related monitoring could be undertaken by an independent agency on a periodic basis.
- » The Company needs to evaluate and review their policy, procedure and controls for compliance of the amended CSR requirements considering that both Company and officers of the Company are liable to penal provisions in case of non-compliance
- » The Company needs to put a framework in place to assist the CFO in certifying the funds spent on projects under CSR. The fund disbursement review must assess the existing control environment and address the risk of non-compliance, leakage and provide structured approach to ensure that the funds have been used for Board approved CSR activities.



9. Enhanced disclosures

CSR Rules enhance the disclosure requirements for Companies undertaking CSR activities or contributing towards CSR. CSR Rules prescribe formats to be adhered to while making disclosures related to the CSR policy, CSR spend etc. Further, the Ministry of Corporate Affairs, Government of India, issued notification dated 24th March, 2021 to amend Schedule III to the Companies Act, 2013 to enhance the disclosures required to be made by the Company in its Financial Statement and such notifications also mandates disclosure in relation to CSR for the Companies which are covered under the section 135 of the Companies Act. These new disclosures are applicable for financial year beginning on or after 01 April 2021. This is our initial and tentative view. We will await further clarification from ICAI/MCA in this regard.

Following are some of the key pieces of information required to be provided by the Company

- » Brief outline on CSR policy of the Company,
- » Composition of CSR Committee,
- » Provide web-link where composition of CSR committee, CSR policy and CSR projects approved by the Board are disclosed on the website of the Company,
- » Provide details of impact assessment of CSR projects carried out in pursuance of sub-rule (3) of rule 8 of Companies (Corporate Social responsibility policy) Rules 2014, if applicable (attach the report).
- » Details of amounts available for set-off in pursuance of sub-rule (3) of rule 7 of the CSR rules and amount required to be set off for financial year, if any
- » Average net profit as per section 135(5)
- » (a) Two percent of average net profit of the Company as per section 135(5), (b) surplus arising out of the CSR projects or programs or activities of the previous financial years; (c) amount required to be set-off for the financial year, (d) total CSR obligation during the financial year
- » (a) CSR amount spent or unspent for the financial year, (b) details of amount spent against the ongoing projects for the financial year, (c) details of amount spent against other than ongoing projects for the financial year, (d) amounts spent for administrative overheads, (e) amount spent on Impact Assessment, if applicable (f) total amount spent for the financial year, (g) excess amount for set off, if any.
- » (a) Details of unspent CSR amount for preceding three financial years, (b) details of amount spent in the financial year for ongoing projects of the preceding financial year
- » In case of creation or acquisition of capital asset, furnish the details relating to the asset so created or acquired through CSR spent in the financial year (asset-wise details): (a) date of creation or acquisition, (b) amount of CSR spent for creation or acquisition of capital asset, (c) details of the entity or public authority or beneficiary under whose name such Capital asset is registered, their addresses
- » Specify the reasons, if the Company has failed to spend two percent of the average net profit as per section 135(5).
- » Reasons why the company has failed to spend two percent of the average net profit as per section 135(5) the enhanced reporting requirements are likely to involve additional time and effort to fully comply with the same. Developing structured formats for enabling rereporting will help create a more efficient process for enabling transparency and clarity to any stakeholder accessing the information.
- » A well drafted CSR policy and detailed annual action plan will support stakeholders in understanding the vision, mission and road map for the CSR journey of the Company Such disclosures also aid partnerships, collaborations for enhancing impact and long-term outcomes.

Points to ponder

- » In light of the detailed requirements, a Company needs to assess and put in place, suitable mechanisms to collate the data required for disclosures. Also, an evaluation of the completeness of financial disclosures in the Annual Report is required
- » CSR Rules mandatorily require impact assessment report to be placed before the Board and the reports to be annexed to the Annual Report on CSR. Companies should evaluate whether the full impact assessment report should be annexed to the report or an abridged version could be appended, with a reference to the Company's website, if any, where the detailed report shall be hosted or provide details of a designated person who could be contacted for the full report, in case the Company does not maintain a website

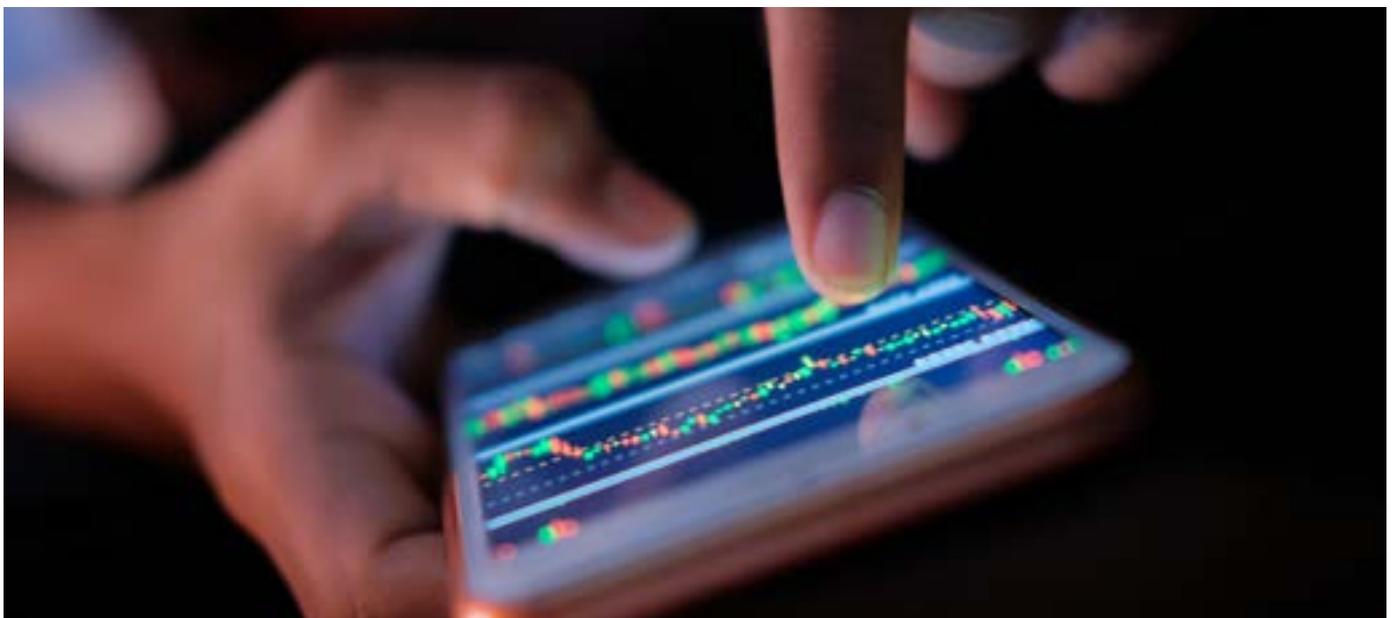
9A. Display of CSR activities on website

The Board of Directors of the Company shall mandatorily disclose the composition of the CSR Committee, CSR policy and projects approved by the Board on the website, if any, for public access.

- » The disclosure on the website is intended to enhance transparency and accountability with respect to the company's CSR agenda.

Points to ponder

- » Company to review their existing policy and process of disclosure to ensure compliance with the revised CSR rules.
- » If a Company has only a web page on the website and not an independent website, would it still need to comply with this requirement?
- » As a first time requirement, is the company required to publish details of all projects approved since the beginning of the financial year or all projects approved and under execution as at the date of notification of the Rules or only all projects approved after the date of notification of the Rules?





10. Next steps

Amended CSR rules makes compliance more onerous and specific penal provision for both Companies and officers of the Company make it imperative to review existing policies, procedures and controls around formulation, implementation, monitoring and reporting of CSR. Following "Next Steps" could assist companies in preparing for the compliance.





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