INDIA'S CORPORATE SOCIAL RESPONSIBILITY (CSR) REGIME SIMPLIFIED

75 Years
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General framework of CSR

- <u>Section 135 of Companies Act, 2013 (Act)</u>

  - Every company with a net worth of INR5 billion, revenue (turnover) of INR10 billion or net profit of INR50 million, during the preceding financial year, is required to spend a minimum of 2% of the average net profits in the 3 preceding financial years on CSR. In assessing whether CSR obligations apply, the net profit is to be computed as profit before tax and not profit after tax.

- CSR is specific to each company. It is applicable to a holding or subsidiary company only when such company fulfills the prescribed eligibility criteria.

- It is also applicable to a foreign company having a branch or project office in India.

- The government has no direct role in the implementation of CSR projects. It is a process driven by a company's Board of Directors (Board).

- Schedule VII of the Act includes a broad range of CSR activities. CSR expenditure cannot be incurred beyond the activities and funds listed in Schedule VII.

- In addition to Section 135 and Schedule VII of the Act, the Companies (CSR Policy) Rules, 2014, govern India's CSR regime.

Key changes to the CSR regime

- <u>CSR covers Covid-19 assistance</u>
  - As per the amendments and clarifications issued by the Indian government, CSR includes:
    - funds spent for Covid-19 in relation to promotion of health care, including preventive health care and sanitation, and disaster management;
    - contributions to the Prime Minister's National Relief Fund, the PM CARES Fund, and the state disaster management authority;
    - research and development activity of new vaccines, drugs and medical devices related to Covid-19 up to FY2023, but only in collaboration with a government organization;
    - awareness or public outreach campaigns on Covid-19 vaccination;
    - setting up makeshift hospitals and temporary Covid-care facilities; and
    - funds spent for Covid-19 vaccination of persons other than a company's employees and their families.

Key changes to the CSR regime

- <u>Tax issues in relation to Covid-19 assistance</u>

  - Generally, Covid-19 relief measures provided by employers to employees is not considered as a deductible CSR expenditure.

  - However, financial assistance received by an employee from the employer or any other person towards Covid-19 medical expenses, during the financial year 2019-20 and subsequent years, is not subject to income tax.

  - Ex-gratia payments received by family members of an employee from the employer or any other person on account of death from Covid-19, during the financial year 2019-20 and subsequent years, are exempt from income tax.

Key changes to the CSR regime

- <u>Transfer of unspent CSR amount</u>
  - Any unspent CSR amount is to be utilized for CSR purposes only and is required to be transferred, with effect from financial year 2020-21, as follows:
    - For ongoing projects:
      - ✓ to the ‘Unspent CSR Account,’ i.e., a separate bank account of the company created for each financial year but not for each ongoing project; and
      - ✓ within 30 days from the end of the financial year
    - For projects which are not ongoing:
      - ✓ to any fund included in Schedule VII of the Act; and
      - ✓ within 6 months from the end of the financial year. Companies cannot spend the unspent CSR amount during this intervening 6-month period for any CSR activity.
  - If the company is not able to meet its CSR obligations, transfer of the unspent CSR amount is considered as sufficient compliance.

Key changes to the CSR regime

- Set off
  - Excess of the prescribed CSR amount spent during a financial year can now be set off against CSR obligations during the next 3 financial years.
- Implementation of CSR activities
  - Three routes: (i) through the company itself; (ii) through certain specified intermediaries like section 8 companies, registered public trusts and registered societies; or (iii) through collaboration with other companies.
  - Intermediaries are required to register with the Central Government by filing form CSR-1 on the MCA portal, with effect from April 1, 2021.
  - The registration is not required when the company itself undertakes the CSR activities.
  - An international organization cannot act as an intermediary to implement the CSR activities.

Key changes to the CSR regime

- CSR expenditure

  - The Indian government has clarified that CSR expenditure:

    - cannot be utilized to fund government schemes;
    - cannot be deemed to be a business expenditure;
    - does not provide specific tax exemptions; and
    - includes amount spent towards acquisition of a capital asset, including stamp duty and registration charges, if such asset is held by certain prescribed entities like section 8 companies, registered public trusts, registered societies, self-help groups, or a public authority.

  - CSR contributions cannot be in kind. Involvement of the company’s employees in CSR projects cannot be monetized and shown as CSR expenditure.

  - Any surplus arising out of CSR activities, i.e., income generated from CSR activities, is to be used only for the purposes of CSR.

Key changes to the CSR regime

- Annual Report and Disclosure Requirements
  - An annual report on CSR is to be included in the Board's report in the prescribed format for each financial year.
  - The Board must disclose: (i) the composition of the CSR committee; (ii) the CSR Policy; and (iii) the projects approved by the Board, on its website.
- Impact Assessment
  - Every company having average CSR obligations of at least INR100 million in the preceding 3 financial years and any company with a CSR project of at least INR10 million is required to conduct an impact assessment of such CSR projects.
  - The rationale is to assess the social impact of a CSR project and encourage companies to make judicious decisions towards CSR spending.
  - The impact assessment report is to be annexed to the annual report on CSR. However, providing a web link to access the impact assessment report and its executive summary in an annual CSR report is also sufficient compliance.

Key changes to the CSR regime

- Decriminalization

    - Criminal penalties for non-fulfillment of CSR obligations have now been omitted.

    - Breach of CSR regulations is only a civil wrong now.

    - The applicable penalty is only in case of non-transfer of the unspent CSR amount in a financial year, as follows:

        - twice the unspent amount, or INR10 million, whichever is less, in case of a company; or

        - 1/10th of the unspent amount, or INR200,000, whichever is less, in case of every officer in default.

    - The penalty is over and above the unspent CSR amount required to be transferred.

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Key changes to the CSR regime

- Impact

  - A company can no longer just provide reasons in the Board's report for failing to spend the CSR amount.

  - A company will necessarily have to spend the prescribed amount for CSR purposes, or in the alternative, transfer the unspent CSR amount to the prescribed government funds.

  - The government has now made CSR mandatory and akin to a surcharge, which will have an impact on corporate balance sheets.

  - Companies will now be able to set off any excess spending against future CSR obligations.

  - Registration of intermediaries and conducting an impact assessment study for projects crossing a certain threshold are additional compliances. The government may be able to better monitor the CSR activities implemented by intermediaries.

  - Given the foregoing, companies should take a detailed look at their CSR policies to reassess their CSR obligations and plan their CSR expenditure appropriately.

Thank You

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