CS PREETI GROVER
(Company Secretaries)

REPORT OF THE HIGH LEVEL COMMITTEE ON CORPORATE SOCIAL RESPONSIBILITY(CSR) - PART II

In year 2018 a High Level Committee (HLC) was set up under the chairmanship of Mr. Injeti Srinivas, Secretary, Ministry of Corporate Affairs. The HLC submitted its final report to the Honourable Union Minister of Finance and Corporate Affairs in **August 2019.** The objective of the committee was to review the existing CSR framework and formulate the roadmap for future implementation to unlock the full potential of CSR.

CHAPTER III - SOME KEY ISSUES AND RECOMMENDATIONS MADE BY THE COMMITTTEE

APPLICABILITY

Section 135(1) of the Companies Act, 2013, defines the applicability of CSR . The HLC discussed that CSR provisions be made applicable to profit making entities not incorporated under Company law, but operating under the specific statutes on mutatis mutandis basis. The provision of CSR need to be applicable across all business entities and there should be a level playing field.

Final Recommendation

The scope of CSR applicability be extended to LLPs, Banks registered under Banking Regulation Act, 1949, and similarly placed entities not covered under Companies Act through amendments in Companies Act and if necessary, in their respective statues.

APPLICABILITY OF CSR PROVISIONS TO NEWLY INCORPORATED COMPANIES

Section 135(1) of the Companies Act, 2013 is applicable on newly incorporated Companies as well. The companies who are in existence for less than 3 years face difficulty in fulfilling the obligation of spending CSR amount, and adequate time needs to be given for a newly incorporated company to stabilize itself before mandatory spending obligations are imposed on it.

Final Recommendation

A clarification must be issued that for newly incorporated Companies, obligation under section 135 shall lie only after they have been in existence for 3 years.

CONSTITUTION OF CSR COMMITTEE

As per section 135(1) of the companies act, 2013, CSR eligible companies needs to constitute a CSR committee of the Board. As per schedule VII, the CSR committee has to formulate and recommend the CSR policy and needs to monitor the expenditure made on the CSR activities. The HLC felt that mandating such requirements for smaller companies having low prescribed CSR amount leads to increased operational costs for them .

Final Recommendation

Companies having prescribed CSR amount below 50 lakhs be exempt from forming a separate CSR committee. The Board itself would carry out the functions of the CSR Committee.

OBLIGATION TO CARRY OUT CSR AND CARRYING FORWARD OF UNSPENT CSR AMOUNT

As per section 135(5) of the Companies Act, 2013, every company eligible for CSR needs to explain the reasons for non spending the CSR amount in its Board Report. The HLC felt that mere statement of a reason for not spending is not sufficient , the justification for not spending CSR amount, despite being eligible to do so must be substantive.

Final Recommendation

The HLC recommended that unspent amount for a particular year should be transferred to a separate designated account, which should be spent within a period of 3 to 5 years failing which the same should be transferred to a fund specified by Central Government.

CREATION OF CAPITAL ASSETS THROUGH CSR SPENDING

The HLC discussed the reports revealing that CSR spending has been used for creation of assets like land, building etc. with the reasoning that such spending was a prerequisite for undertaking activities specified in schedule VII. According to the HLC, creating assets in the name of company would tantamount to non spending of CSR amount and CSR expense has to be revenue expense. Companies needs to be sensitized to contribute in social development with a focus on serving the unserved and not be profit-oriented and commercialise operations in the guise of CSR.

Final Recommendation

Disclosure on CSR should be made more enhanced and granular, to check that CSR expenditure is not being used for creation of capital assets .

UNDERTAKING CSR ACTIVITIES IN LOCAL AREAS

As per section 135(5) of the companies act, 2013, the companies shall give preference to the local area(s) around which it operates for spending the CSR amount. The HLC observed that there is skew in favour of industrialised states , and less developed states receive least funds. The HLC felt that the companies needs to balance CSR spending between local area(s) around where it operates and less developed regions as aspirational districts.

Final Recommendation

The emphasis in local area in the Act is only directory and not mandatory in nature. It is advisable for companies to engage in CSR activities by balancing local area preferences with national Priorities.

SCHEDULE VII OF THE ACT

Schedule VII of the Act specifies the areas/subject to be undertaken by the Company for CSR activities but doesn't recognize any area outside of it. The HLC felt that the Central Government may give specific directions when the situation warrants to align CSR expenditure with broader national priority or social inclusion.

Final Recommendation

Schedule VII be mapped to include some items such as promoting sports, senior citizen welfare, welfare of differently abled persons, disaster management, and heritage to develop an SDG+ framework.

CSR AUDIT

Companies are required to state the amount of expenditure incurred on CSR activities in the Board Report as per the prescribed format of CSR Rules. The HLC felt that it is required to assess the flow of CSR funds, its utilization and surplus generated from the use of CSR funds. The inclusion of CSR spending in financials of the company, along with showcasing of project on CSR exchange portal would make the CSR framework transparent and robust.

Final Recommendation

CSR may be brought in purview of statutory financial audit, by making details of CSR spending as a part of the financial statement of the company, and incorporated in schedule II of the Act.

ISSUES PERTAINING TO IMPEMENTING AGENCIES

As per Rule 4(2) of Companies (Corporate Social Responsibility Policy) Rule, 2014, a Company may decide to undertake its CSR activities either by a company established under section 8 of the Act/ registered trust/ registered society, established by a company, either singly or along with any other company; **OR** a company established under section 8 of the Act/ registered trust/ registered society, established by Central Government/state Government or any other entity established under an Act of parliament or state legislature. As per data analysis 34% of the CSR amount has been spent directly by the Companies which implies that a sizable percent of CSR funds is spent through Implementing Agencies (IAs). HLC noticed that mere disbursal of CSR funds to IAs is being constructed as CSR spending.

Final Recommendation

The Board of the Company to ensure that CSR funds are duly spent on CSR activities as specified under schedule VII and report on the modalities of utilization of funds.

REGISTRATION OF IMPLEMENTING AGENCIES (IAs)

One big issue companies face is to find suitable Implementing Agencies. Suggestions included registration of IAs with the MCA, with a reporting requirement so that there is an authentic and reliable list of Implementation agencies . The Ministry could maintain a register of IAs and assign a unique Identification Number to them along the lines of the registry of Independent Directors, to be quoted while reporting on any CSR activity.

Final Recommendation

The Board of the company to ascertain the credibility of IAs and carryout necessary due diligence. IAs to be registered with MCA to carryout CSR activities.

TAX BENEFIT FOR CSR ACTIVITIES

No tax Benefit are prescribed under Income tax Act, 1961 for expenses incurred by companies towards CSR as clarified by the Finance Act, 2014.

Final Recommendation

All activities mentioned in schedule VII should have tax benefit. CSR expenditure to be made deductible from the income earned for the purpose of taxation. IAs be treated as partners and not as service providers so as to address the variable incidence of indirect taxes on them.

CSR EXCHANGE PORTAL

As prescribed by the committee, all information reported by companies on CSR be compiled by MCA and placed in a public domain.

Final Recommendation

A CSR exchange portal be developed for creating an interactive platform for all stakeholders, including contributories, beneficiaries, IAs by leveraging the benefits of technology to maximize the potential and outcomes of CSR.

ADMINISTRATIVE OVERHEADS

The HLC deliberated enhancing the 5% limit on administrative overheads and recommends for maintenance of status quo in this regard.

Final Recommendation

For companies undertaking need & impact assessments, the limit may be extended by an additional 5 %.

****