

Social Sector Hotline

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SIGNIFICANT CHANGES INTRODUCED UNDER CSR RULES: IMPACT ON CSR PRACTICES

- Companies are now relaxed from all the Corporate Social Responsibility (“CSR”) compliances immediately upon ceasing to meet the statutory limits of applicability in the preceding financial year as against immediately three preceding financial years of non-applicability.
- Constitution of CSR Committee is mandated in case of any unspent CSR amount with the companies, irrespective of the limit of CSR expenditure.
- The category of entities functioning as implementing agencies is broadened.
- New format of CSR annual report has been introduced.

INTRODUCTION

In exercise of the powers conferred under Section 135 and sub-sections (1) and (2) of Section 469 of the Companies Act, 2013 (“Act”), the Central Government recently amended The Companies (Corporate Social Responsibility Policy) Rules, 2014¹ through the Companies (Corporate Social Responsibility Policy) Amendment Rules, 2022.² (“Amended CSR Rules”)

As per Section 135 of the Act, certain (profit-making) companies are expected to spend at least 2 per cent of their average net profit of the preceding three financial years on CSR activities in a particular financial year in accordance with its CSR Policy. The Board of Directors must ensure that the firm spends at least 2 per cent of its average net profit made during the three financial years immediately preceding the current one.

KEY AMENDMENTS AND THEIR IMPACT

RULE	AMENDMENTS	IMPACT
Rule 3(1) [new proviso inserted]	<i>“Provided further that a company having any amount in its Unspent Corporate Social Responsibility Account as per sub-section (6) of section 135 shall constitute a CSR Committee and comply with the provisions contained in sub-sections (2) to (6) of the said section.”;</i>	<p>In case of any unspent amount pertaining to an ongoing CSR project, the companies are required to open a separate Unspent CSR Account to keep such unspent CSR amount and the same should be spent within a maximum period of three financial years. If the companies fail to spend in said three financial years, the remaining unspent CSR amount be transferred to any of the funds specified in Schedule VII of the Act within 30 days from the end of third financial year.</p> <p>Amended CSR Rules now require the companies having unspent CSR amount to constitute CSR Committee. This condition applies irrespective of the CSR obligation and hence, the exemption granted under Section 135(9) of the Act from the constitution of CSR Committee will not apply in such cases.</p> <p>The rationale for this change could be that since the ongoing CSR projects involving unspent amount are relatively larger in size and requires constant monitoring by the</p>

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company till the entire amount is fully utilized and the role of CSR committee becomes very crucial in such cases.

However, notifying this amendment with immediate effect will make a lot of eligible companies to take immediate action to constitute the CSR Committee as soon as possible as there is no lead time given in the amendment to constitute such CSR Committee.

Any delay in constitution of CSR Committee *may* be viewed as non-compliance.

Rule 3(2)
[omitted]

"Every company which ceases to be a company covered under sub-section (1) of section 135 of the Act for three consecutive financial years shall not be required to - (a) constitute a CSR Committee; and (b) comply with the provisions contained in sub-section (2) to (6) sub-section (2) to (5) of the said section, till such time it meets the criteria specified in sub-section (1) of section 135."

[Omitted]

Prior to this amendment, even the companies which cease to be covered under Section 135(1) of the Act were required to comply with all the provisions under Section 135 of the Act for consecutive three financial years. Technically, this provision had become redundant when the expression '*immediately preceding financial year*' was first plugged in Section 135(1) of the Act. However, there was no official relaxation granted so far.

As a result, the companies had suffered and incurred costs in complying with this despite having business losses. This requirement has been now taken away which come as a greater relaxation.

Henceforth, the companies can enjoy immediate exemption from CSR compliance and expenditure obligations upon ceasing to meet the thresholds under Section 135(1) of the Act in the immediately preceding financial year.

Rule 4 (1)

"(1) The Board shall ensure that the CSR activities are undertaken by the company itself or through, - (a) a company established under section 8 of the Act, or a registered public trust or a registered society, exempted under sub-clauses (iv), (v), (vi) or (via) of clause (23C) of section 10 or registered under section 12A and approved under 80 G of the Income Tax Act, 1961 (43 of 1961), established by the company, either singly or along with any other company; or (b) a company established under section 8 of the Act or a registered trust or a registered society, established by the Central Government or State Government; or (c) any entity established under an Act of Parliament or a State legislature; or (d) a company established under section 8 of the Act, or a registered public trust or a registered society, exempted under sub-clauses (iv), (v), (vi) or (via) of clause (23C) of section 10 or registered under section 12A and approved under 80 G of the Income Tax Act, 1961, and having an established track record of at least three years in undertaking similar activities. Explanation.- For the purpose of clause (c), the term "entity" shall mean a statutory body constituted under an Act of Parliament or State legislature to undertake activities covered in Schedule VII of the Act."

The Amended CSR Rules have now widened the scope of implementing agencies by allowing the companies to undertake their CSR activities also through a section 8 company or registered public trust or registered society exempted under sub-clauses (iv), (v), (vi) or (via) of clause (23C) of section 10 of the Income Tax Act, 1961 ("**IT Act**"), in addition to the entities registered under section 12A and approved under 80G of the IT Act allowed earlier. These entities either created by the company itself or entities acting as implementing agency and fulfil the established track record of minimum 3 years can undertake the CSR activity on company's behalf.

Entities permitted under these sub-clauses of section 10 (23C) of the IT Act broadly include the funds and institutions formed for the purposes like charity, educational, medical treatment, rehabilitation solely for philanthropic purposes and including those formed for religious purposes. Here, the scope of activities covered under sub-clauses of section 10 (23C) of the IT

Act seems to be wider than the CSR activities recognised in Schedule VII of the Act. Considering this, in our view, only the entities permitted under section 10(23C) of IT Act and which are engaged in undertaking Schedule VII activities should be permitted to act as an implementing agency for undertaking CSR activities. For instance, the entity under clause (v) of section 10(23C) of IT Act is engaged exclusively in religious activities, which is not a Schedule VII activity and hence, such entity cannot be appointed as an implementing agency.

Rule 8(3)(c)	<p><i>“(i) for the words “five percent”, the words “two per cent.” shall be substituted; (ii) for the words “whichever is less”, the words “whichever is higher” shall be substituted.”</i></p>	<p>Prior to this change, the overall limit for expenditure towards impact assessment was allowed up to 5 per cent of total CSR expenditure subject to a maximum amount of fifty lakh rupees.</p> <p>Now, Amended CSR Rules has revised these limits to prescribe 2 per cent of total CSR expenditure or fifty lakh rupees, whichever is higher.</p> <p>Impetus on impact assessment will bring accountability on the organisation to ensure money is spend for the right cause in the right manner. With the revised limits, the larger companies generating higher profits and undertaking larger CSR expenditure will have proportionately higher amount to allocate towards assessing the impact of CSR projects undertaken.</p> <p>For example, if CSR obligation of a company is fifty crore rupees in a year, as per earlier limits, only up to fifty lakh rupees was allowed towards impact assessment. This is allowed up to one crore as per revised limits.</p> <p>.</p>
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Annexure II	<p>The government has announced a new format for the annual report on CSR activities that must be included in the report of the board for the financial year beginning on or after April 2020.</p>	<p>New format of annual report on CSR has been made more comprehensive and is in sync with the changes introduced in Amended CSR Rules. This has eliminated the obligation to provide each CSR project's specifics. Several further adjustments are also made to the order of the information required in the report. In accordance with the new format the composition of the CSR committee necessitates that companies give an executive summary and hyperlinks to impact assessments of CSR initiatives implemented.</p>
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Table 1: Denoting the 2022 amendments in the governing rules and their impact

CONCLUSION

To sum up, the said Amended CSR Rules have sought to rationalize certain existing key CSR requirements which includes constitution of CSR committee, CSR expenditure norms, scope of implementing agencies, ceiling on impact assessment cost and reporting format. Further, the pre-existing redundant requirement has been now dispensed with.

In accordance with the Companies (Corporate Social Responsibility Policy) Amendment Rules of 2021, the yearly

CSR annual report format has been amended and made more comprehensive. This has now been justified by eliminating the obligation to provide each project's specifics. Several further adjustments are made to the order of the information required in the report.

However, there appears to be a case of poor drafting by the Ministry of Corporate Affairs ("MCA") as far as applicability of new CSR annual report is concerned as the new format of CSR annual report has been made applicable for the financial year commencing on or after April 1, 2020 instead of financial year commencing on or after April 1, 2022.

As mentioned in the preceding paragraph, MCA, on January 21, 2021, amended the CSR Rules vide Companies (Corporate Social Responsibility Policy) Amendment Rules, 2021, CSR annual report was amended, and two formats were notified i.e. Annexure-I and Annexure-II. Annexure-I was made applicable for the financial year commencing prior to April 1, 2020 and Annexure-II was made applicable for the financial year commencing on or after April 1 2020 and this made sense as the new format was notified in January 2021 and eligible companies could follow the Annexure-II format for the financial year 2020-21 as the financial year was not concluded when the new format of Annexure-2 was introduced.

Notifying the new format of CSR annual report on September 20, 2022, when most of the companies would have got their Board's report approved along with CSR annual report, with retrospective effect saying the new format is applicable for the financial year commencing on or after April 1, 2020, may not be viewed as correct and would be questioned on implementation.

Though the current amendments are made effective from Sep 20, 2022, majority of the stakeholders could access the amendments only the next day, and in the meantime, many companies have approved their Board's report along with CSR annual report which may put them in a soup of non-compliances in literal terms of the law for following old format of the CSR annual report.

It is appropriate that MCA issues a clarification at the earliest on the above as well as provide a lead time to constitute the CSR Committee or clarify that constitution of CSR Committee anytime during the financial year should be valid compliance.

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(The authors would like to acknowledge Shreya Agarwal for her contribution.)

You can direct your queries or comments to the authors

¹ https://www.mca.gov.in/Ministry/pdf/CompaniesActNotification2_2014.pdf

² <https://www.mca.gov.in/bin/dms/getdocument?mds=1Wt3uUYzV0rGCr2Vxa8ztQ%253D%253D&type=open>

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