

# CSR: From Comply or Explain to a Stricter Regime

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***Presentation***

*for*

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# Disclaimer

All views expressed in this PPT  
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# Key topics for discussion

- CSR under Companies Act, 2013 ●
- CSR under Companies (CSR Policy) Rules 2014 ○
  - ① CSR and Sustainability ①
  - ② Utilisation Certificate ②
  - ③ Impact Assessment ③
  - ④ CSR Audit ④
  - ⑤ Penal Provisions ⑤
  - ⑥ Social Stock Exchange ⑥
  - ⑦ Social Audit ⑦
  - ⑧ Social Audit vis-à-vis CSR Audit ⑧
  - ⑨ Social Audit Standards ⑨
  - ⑩ CSR Rating ⑩

# **CSR under Companies Act, 2013**

## Legal Framework under Companies Act, 2013

- Sec 134(3)(o) – Disclosures in Board’s Report
- Sec 134(8) – Penalty
- Sec 135(1) - Companies that are required to comply with CSR provisions
- Sec 135(1) - Composition of CSR Committee
- Sec 135(2) - Disclosures about CSR Committee in Board’s report
- Sec 135(3) - Role of CSR Committee
- Sec 135(4) - CSR Policy
- Sec 135(5) - Mandatory CSR Spending [transfer to Sch VII if unspent]
- Sec 135(6) – Unspent amount in Ongoing Project
- Sec 135(7) – Penalty
- Sec 135(8) – Direction by Central Government
- Sec 135(9) – Non-requirement of CSR Committee in some cases
- Sec 166(2) - Duties of directors
- Schedule VII – CSR Activities

## The Companies Act, 2013

- Makes CSR mandatory for certain class of profitable undertakings
- As per section 135 of Companies Act 2013, mandatory CSR spending of 2% of net profit is required by the following companies:

Net worth > Rs 500 crores, or

Turnover > Rs 1000 crores, or

Net profit > Rs 5 crores, or

foreign company defined u/s 2(42) having its branch office or project office in India which fulfills the criteria under pts. (i), (ii) or (iii)

# Net Worth, Sec 2(57)

## It is the aggregate of

- paid-up share capital;
- all reserves created out of the profits; and
- Securities Premium Account.

## The following are the implied inclusions:

- any reserve created out of profits,
- (including statutory reserves); and
- does not matter whether or not dividend can be paid out of it;

## Deductions therefrom

- accumulated losses;
- deferred expenditure;
- miscellaneous expenditure not written off.

## The following shall be excluded in calculation on net worth

- reserves created out of revaluation of assets;
- reserves created out of write-back of depreciation; and
- reserves created out of amalgamation.

# Turnover, Sec 2(91)

~~Turnover is the aggregate value of realization made by the company during a financial year from:~~

- ~~• the sale, supply or distribution of goods or~~
- ~~• on account of services rendered or~~
- ~~• both of the above~~

Turnover is the gross amount of revenue recognised in the profit and loss account from the sale, supply, or distribution of goods or on account of services rendered, or both, by a company

The earlier definition looked very simple but practical difficulties arose for which ICAI had issued some guidelines



# Spending that do not qualify as CSR

- In project not related to activity in Schedule VII
- Spending in the ordinary course of business
- Spending outside the local area of operation of the company (this is marked as 'preferable')
- Spending outside India by a Foreign company to which this section applies (spending 'locally' here means in India)
- Spending that benefits only employees & their families
- Contribution given to any political party with objective of carrying out any such specified activity
- Any spending which a company is statutorily required to do under any other Act
- Spending in violation of any Act
- Spending beyond limit specified in CSR Policy
- Spending on One-off Events
- Spending on projects not specified in CSR Policy
- Spending on an ongoing project in the 5<sup>th</sup> year (MCA expected to clarify)

# Responsibility of the Board

- To compose a CSR Committee
- To disclose composition of CSR Committee in its reports.
- To ensure that CSR committee meetings are held properly
- To ensure at least 2% of average net profit of the preceding 3 years is spent on CSR activities every year.
- To approve the CSR Policy after considering recommendations of the CSR Committee and upload it on the website
- To ensure that activities laid down in CSR policy are actually undertaken as per the intent of the committee.
- To disclose CSR policy and initiatives towards implementation in its report and website.
- If spending up to 2% of net profits, as required, is not done, to report the reasons for failure in its report.
- Transfer Unspent amount to Unspent CSR A/c or Sch VII fund as case may be
- Draw up yearly Action Plans and upload in the website
- Ensure Administrative Overheads do not exceed 5% of CSR expenditure
- Monitor the implementation of the CSR projects (even when project implemented by Implementation Agency)
- Utilisation Certificate

# CSR Committee of the Board

- Board to constitute a CSR committee
- To consist of at least 3 directors of the company one of whom shall be an independent director.
- For companies that are not mandatorily required to appoint IDs, or companies that do not require three directors under the Companies Act 2013 but qualify for CSR spending the following applies:
- Private Company having only 2 directors may have only 2 directors in CSR committee
- Companies not required to have an independent directors (ID) may have CSR Committee without an ID
- In case of Foreign company, the authorized representative of the company in India and another person nominated by such company in this regard
- For Company whose CSR Budget is less than Rs. 50 Lakhs, CSR Committee is not required and the Board may perform its functions

# CSR Committee – Duties and Functions

- Review past and current CSR activities of the company, examine their alignment with Schedule VII
- Researching on national and local development priorities and setting up relevant CSR activities for the company.
- Studying the CSR practices of other companies and learning from their experiences.
- Formulate and recommend to BOD, a CSR Policy listing the activities to be undertaken by the company and to lay down what those policies would imply in terms of the company's vision, mission and its core business area.
- Recommend the amount of expenditure to be incurred
- Determine the mechanism for implementation
- Monitor and supervise the implementation of the CSR projects recommended
- Monitor the CSR Policy of the company from time to time.

# Salary vs. Employee Benefit

- Salary to employees of the CSR Department may be paid out of the CSR Fund, but
- The fund cannot be utilised for the objective of activities beneficial only to employees

# Schedule VII – Specified Activities

- CSR activities under the Companies Act, 2013 have to be undertaken in any of the areas mentioned in Schedule VII of the Act.
- While traditional CSR includes within its ambit activities directed towards Social and Environmental upliftment and upgradation, the Schedule VII of the Companies Act 2013 very specifically includes activities directed at overall national development also. This is in the right spirit for a developing country like India.

# Schedule VII – Social Projects

- Eradicating hunger, poverty & malnutrition promoting preventive health care and sanitation and **making available safe drinking water**;
- Promoting education, employment enhancing vocation skills among children, women, elderly, and the differently abled;
- Promoting gender equality, empowering women setting up homes and hostels for women, orphans or old age homes, day care centres etc. for the socially and economically backward classes
- Rural development projects.
- Setting up public libraries

# Schedule VII – Environmental Projects

- Environmental sustainability,
- Ecological balance,
- Protection of flora and fauna, animal welfare, agro forestry,
- Conservation of natural resources and
- Maintaining quality of soil, air and water;
- Clean Ganga Fund
- Swachh Bharat Kosh



# Schedule VII – Nationalistic Projects

- Protection of national heritage, art and culture,
- Restoration of buildings and sites of historical importance
- Promotion and development of traditional arts and handicrafts;
- Measures for the benefit of armed forces veterans, war widows and their dependents;
- Training to promote rural sports, nationally recognized sports, paralympic and Olympic sports;
- Contribution to PM National Relief Fund or any other fund set up by CG for socio-economic development, relief & welfare of SC, ST, OBC, other minorities and women;

# Schedule VII – Technology Projects

- This is the darker side of CA 2013
- CSR in India speaks very less of technology.
- The only place in the Schedule VII where we see specific mention of technology is - Contributions to technology incubators within academic institutions;
- For overall development of a country technological development and incentives for carrying on Research and Development is very important. This is lacking. But we can hope that in the coming days we will see some inclusion in this regard.

# **Companies (CSR Policy) Rules, 2014**

# Legal Framework under Companies (Corporate Social Responsibility Policy) Rules, 2014

- Rule 2(1)(d) - Definition of Corporate Social Responsibility
- Rule 2(1)(f) - Definition of CSR Policy
- Rule 2(1)(h) - Definition of 'Net Profit'
- Rule 3 - Companies to which CSR applies
- Rule 4 - CSR activities
- Rule 5 - CSR Committees
- Rule 6 - CSR Policy
- Rule 7 - CSR Expenditures
- Rule 8 - CSR Reporting
- Rule 9 - Display of CSR activities on the website.
- Annexure – Format for Annual Report on CSR Activities to be included in Board's Report

## **CSR Definition *Rule 2(1)(d)***

“Corporate Social Responsibility (CSR)” means the activities undertaken by a Company in pursuance of its statutory obligation laid down in section 135 of the Act in accordance with the provisions contained in these rules, but shall not include the following, namely:-

(i) activities undertaken in pursuance of normal course of business of the company:

Provided that any company engaged in research and development activity of new vaccine, drugs and medical devices in their normal course of business may undertake 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 the conditions that

(a) such research and development activities shall be carried out in collaboration with any of the institutes or organisations mentioned in item (ix) of Schedule VII to the Act;

(b) details of such activity shall be disclosed separately in the Annual report on CSR included in the Board’s Report;

## **CSR Definition *contd...***

- (ii) any activity undertaken by the company outside India except for training of Indian sports personnel representing any State or Union territory at national level or India at international level;
- (iii) contribution of any amount directly or indirectly to any political party under section 182 of the Act;
- (iv) activities benefitting employees of the company as defined in clause (k) of section 2 of the Code on Wages, 2019 (29 of 2019);
- (v) activities supported by the companies on sponsorship basis for deriving marketing benefits for its products or services;
- (vi) activities carried out for fulfilment of any other statutory obligations under any law in force in India;

## **CSR Policy – Definition, *rule 2(1)(f)***

"CSR Policy" means a statement containing the approach and direction given by the board of a company, taking into account the recommendations of its CSR Committee, and includes guiding principles for selection, implementation and monitoring of activities as well as formulation of the annual action plan;

## **Net Profit, Sec 2(1)(h)**

Rule 2(1)(f) "Net profit" means the net profit of a company as per its FS prepared in accordance with the applicable provisions of the Act, but shall not include the following, namely :—

- profit arising from any overseas branch or branches whether operated as a separate company or otherwise; and
- dividend received from other companies in India, which are covered under and complying with the provisions of sec 135
- The net profit in respect of a FY for which the relevant FS were prepared in accordance with the provisions of the Companies Act, 1956 shall not be required to be re-calculated in accordance with the provisions of the Act:
- In case of a foreign company net profit means the net profit of such company as per P & L A/c prepared in terms of Section 381(1)(a) read with section 198 of the Act.



## **Rule 4. CSR Implementation. –**

- (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, registered under section 12A and 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, registered under section 12A and 80G of the Income Tax Act, 1961, and having an established track record of at least three years in undertaking similar activities.

(2) (a) Every entity, covered under sub-rule (1), who 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 **01<sup>st</sup> day of April 2021**:

Provided that the provisions of this sub-rule shall not affect the CSR projects or programmes approved prior to the **01<sup>st</sup> day of April 2021**.

(b) Form CSR-1 shall be signed and submitted electronically by the entity and shall be verified digitally by a Chartered Accountant in practice or a Company Secretary in practice or a Cost Accountant in practice.

(c) On the submission of the Form CSR-1 on the portal, a unique CSR Registration Number shall be generated by the system automatically.

(3) A company may engage international organisations for designing, monitoring and evaluation of the CSR projects or programmes as per its CSR policy as well as for capacity building of their own personnel for CSR.

- (4) A company may also collaborate with other companies for undertaking projects or programmes or CSR activities in such a manner that the CSR committees of respective companies are in a position to report separately on such projects or programmes in accordance with these rules.
- (5) The Board of a company shall satisfy itself that the funds so disbursed have been utilised for the purposes and in the manner as approved by it and the Chief Financial Officer or the person responsible for financial management shall certify to the effect.
- (6) In case of ongoing project, the Board of a Company shall monitor 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 the overall permissible time period. ". This entire sub-rule has been substituted. Earlier it was named as 'CSR activities'.

## Rule 5. CSR Committee

(1) The companies mentioned in the rule 3 shall constitute CSR Committee as under:—

- (i) *a company* covered under sub-section (1) of section 135 which is not required to appoint an independent director pursuant to sub-section (4) of section 149 of the Act, shall have its CSR Committee without such director;
- (ii) a private company having only two directors on its Board shall constitute its CSR Committee with two such directors;
- (iii) 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.

~~(2) The CSR Committee shall institute a transparent monitoring mechanism for implementation of the CSR projects or programs or activities undertaken by the company.~~

(2) The 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:-

- (a) the list of CSR projects or programmes that are approved to be undertaken in areas or subjects specified in Schedule VII of the Act;
- (b) the manner of execution of such projects or programmes as specified in sub-rule (1) of rule 4;
- (c) the modalities of utilisation of funds and implementation schedules for the projects or programmes;
- (d) monitoring and reporting mechanism for the projects or programmes; and
- (e) 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.

## **~~Rule 6. CSR Policy~~**

Omitted by the Companies (CSR Policy) Amendment Rules, 2021

## Rule 7. CSR Expenditure

- (1) The board shall ensure that the administrative overheads shall not exceed five percent of total CSR expenditure of the company for the FY.
- (2) Any surplus arising out of the CSR activities shall not form part of the business profit of a company and shall be ploughed back into the same project or shall be transferred to the Unspent CSR Account and spent in pursuance of CSR policy and annual action plan of the company or transfer such surplus amount to a Fund specified in Schedule VII, within a period of six months of the expiry of the financial year.
- (3) Where a company spends an amount in excess of requirement provided under sub-section (5) of section 135 , such excess amount may be **set off** against the requirement to spend under sub-section (5) of section 135 up to immediate succeeding three financial years subject to the conditions that –
  - (i) the excess amount available for set off shall not include the surplus arising out of the CSR activities, if any, in pursuance of sub-rule (2) of this rule.
  - (ii) the Board of the company shall pass a resolution to that effect.

(4) The CSR amount may be spent by a company for creation or **acquisition of a capital asset**, which shall be held by -

(a) a company established under section 8 of the Act, or a Registered Public Trust or Registered Society, having charitable objects and CSR Registration Number under sub-rule (2) of rule 4; or

(b) beneficiaries of the said CSR project, in the form of self-help groups, collectives, entities; or

(c) a public authority:

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**. This entire section has been substituted for the earlier section by Companies (CSR Policy) Amendment Rules, 2021



## Rule 8. CSR Reporting .-

- (1) 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.
- (2) In case of a foreign company, the balance sheet filed under clause (b) of sub-section (1) of section 381 of the Act, shall contain an annual report on CSR containing particulars specified in Annexure I or Annexure II, as applicable.
- (3) (a) Every company having **average CSR obligation of ten crore** rupees or more in pursuance of subsection (5) of section 135 of the Act, in the **three immediately preceding financial years**, shall undertake impact assessment, through an independent agency, of their CSR projects having outlays of **one crore rupees or more**, and which have been **completed not less than one year** before undertaking the impact study.  
  
(b) The impact assessment reports shall be placed before the Board and shall be annexed to the annual report on CSR.

(c) A Company undertaking **impact assessment** may book the expenditure towards Corporate Social Responsibility for that financial year, which shall not exceed **five percent of the total** CSR expenditure for that financial year or fifty lakh rupees, whichever is less. This entire section has been substituted for the earlier section by Companies (CSR Policy) Amendment Rules, 2021

## **Rule 9. Display of CSR activities on its website. –**

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.

This entire section has been substituted for the earlier section by Companies (CSR Policy) Amendment Rules, 2021

## **Rule 10. Transfer of unspent CSR amount. –**

Until a fund is specified in Schedule VII for the purposes of subsection (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 of the Act.

This section has been inserted by Companies (CSR Policy) Amendment Rules, 2021

## **Form CSR 2**

Every company covered u/s 135(1) shall furnish a report on CSR activities undertaken by it in Form CSR 2 to the Registrar for the preceeding FY 2020-21 and onwards as an addendum to Form AOC-4 / AOC-4 XBRL / AOC-4 NBFC as the case may be.

Provided that for preceeding FY 2020-21, Form CSR-2 shall be filed separately at any time on or before 31<sup>st</sup> March 2022

\*Notified by MCA on 11.02.2022

## **Legal Framework under Companies (Accounts) Rules, 2014 and others**

- **Rule 9: Disclosures about CSR Policy.**

The disclosure of contents of Corporate Social Responsibility Policy in the Board's report and on the company's website, if any, shall be as per annexure attached to the Companies (Corporate Social Responsibility Policy) Rules, 2014.

- **DPE Guidelines on Corporate Social Responsibility and Sustainability for Central Public Sector Enterprises**

# CSR and Sustainability

“Businesses cannot be successful when the society around them fails”

Concept of CSR arises from concerns for sustainability. The UN Brundtland Commission defined sustainability as :-

“development that meets the needs of the present without compromising the ability of future generations to meet their own needs”.

CSR is an inter-disciplinary subject which combines social, ethical and moral responsibility by complying with legal and voluntary requirements. It is based on the management of corporate responsibility activities for producing a positive effect on society.

- Commission of the European Communities, 2003

*"CSR is the concept that an enterprise is accountable for its impact on all relevant stakeholders. It is the continuing commitment by business to behave fairly and responsibly and contribute to economic development while improving the quality of life of the work force and their families as well as of the local community and society at large."*

- Businesses are integral part of society, with a critical role in sustenance and improvement of healthy ecosystems, fostering social inclusiveness and equity, and upholding essentials of ethical practices and good governance.
- As per Business for Social Responsibility (BSR)

*"Corporate Social Responsibility is operating a business in a manner which meets or excels the ethical, legal, commercial and public expectations that a society has from the business."*



# Utilisation Certificate

## **Legal Provision**

Rule 4(5) of the Companies (CSR Policy) Rules, 2014 provides as follows:

*The Board of a company shall satisfy itself that the funds so disbursed have been utilised for the purposes and in the manner as approved by it and the Chief Financial Officer or the person responsible for financial management shall certify to the effect.*

## **ICAI has issued an Advisory to its members on Issuance of Utilization Certificate**

- A company may undertake its CSR activity, either:
  - by itself or
  - through a Third Party (Trust/Society or Section 8 Company)
- When the company undertakes the CSR activity through a third party or NGO, it is advisable for companies to obtain an Independent Practitioner's Report on Utilisation of such CSR Funds from the auditor / CA in practice of the third party or NGO, to whom the funds are given by the Company for implementing CSR activity.
- It is the duty of the Auditor or CA in practice to submit the Report on Utilization of CSR Funds after verifying that the third party has spent the funds on CSR activities as per Section 135 of the Companies Act, 2013, read with Schedule VII to the Act and related regulations and keeping in view the directions given to it by the company. Also the Guidance Note on Reports or Certificates for Special Purposes issued by the ICAI shall be kept in mind.

# CSR Audit

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## **Importance of CSR Audit**

- Social responsibility has gained importance after many corporate scams in the late 20th and early 21st century. The government has issued more accounting and transparency regulations. Stakeholders have demanded that companies be more responsible side by side with earning profits for their shareholders.

- Not Mandatory now
- There may be CSR Audit
- Audit of welfare projects already talked about with teams headed by eminent persons
- CSR Audit helps measure company's actual social performance against the social objectives it had set for itself. It would measure the social return on CSR spend
- Not clear as to type of audit ... may be by third party agencies or social audit in the form of projects rating by society
- CSR Audit vs. CSR Compliance Audit
- Various provisions of Companies (CSR Policy) Rules, 2014 talk about the following which imply recommendation of MCA for some kind of Audit
  - monitoring
  - reporting
  - impact assessment

- CSR Audit is in the nature of **Social Audit**
- Social Audit has been defined as *"a process in which, details of the resource, both financial and non - financial, used by public agencies for development initiatives are shared with the people, often through a public platform. Social Audit allows people to enforce accountability and transparency, providing the ultimate users an opportunity to scrutinize development initiatives"* [in a report submitted by Vision Foundation to the Planning Commission of India]
- But it may also incorporate financial and legal elements to expand the role of CAs and CSs
- The Social Audit Framework of the Organization for Economic Co-operation and Development (**OECD**) forms the basis for most Social Audits today

## Parameters for CSR Audit

- Community development
- fair working conditions
- concern for environment
- international relationships
- marketplace practices
- fiscal responsibilities and
- transparent accounting and financial practices
- regular monitoring



Sl. No.	Provision	Detailed Requirement
1	Sub-rule (3) of Rule 4	(3) A company may engage international <u>organisations</u> for designing, monitoring and <u>evaluation</u> of the CSR <u>projects</u> or <u>programmes</u> as per its CSR policy as well as for capacity building of their own personnel for CSR.
2	Sub-rule (5) of Rule 4	(5) The Board of a company shall satisfy itself that the funds so disbursed have been <u>utilised</u> for the purposes and in the manner as approved by it and the Chief Financial Officer or the person responsible for financial management shall certify to the effect.
3	Sub-rule (6) of Rule 4	(6) In case of ongoing project, the Board of a Company shall monitor 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 the overall permissible time period.

4	Sub-Rule (2) of Rule 5	<p>(2) The 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:-</p> <p>(a) the list of CSR projects or <u>programmes</u> that are approved to be undertaken in areas or subjects specified in Schedule VII of the Act;</p> <p>(b) the manner of execution of such projects or <u>programmes</u> as specified in sub-rule (1) of rule 4;</p> <p>(c) the modalities of <u>utilisation</u> of funds and implementation schedules for the projects or <u>programmes</u>;</p> <p>(d) monitoring and reporting mechanism for the projects or <u>programmes</u>; and</p> <p>(e) details of need and impact assessment, if any, for the projects undertaken by the company:</p> <p>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.”</p>
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5	Sub-Rule (3) of Rule 8	<p>(a) Every company having average CSR obligation of ten crore rupees or more in pursuance of subsection (5) of section 135 of the Act, in the three immediately preceding financial years, shall undertake impact assessment, through an independent agency, of their CSR projects having outlays of one crore rupees or more, and which have been completed not less than one year before undertaking the impact study.</p> <p>(b) The impact assessment reports shall be placed before the Board and shall be annexed to the annual report on CSR.</p> <p>(c) A Company undertaking impact assessment may book the expenditure towards Corporate Social Responsibility for that financial year, which shall not exceed five percent of the total CSR expenditure for that financial year or fifty lakh rupees, whichever is less.</p>
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\*[as amended by the Companies (CSR Policy) Amendment Rules, 2021]

## Reporting Requirement under CARO 2020

- Companies (Auditor's Report) Order (CARO) 2020 was notified on 25<sup>th</sup> February 2020 vide S.O. S49(E), and was to be applicable for the financial years commencing on or after the 1st April, 2019. However, the same was extended by a year by Ministry of Corporate Affairs vide Order dated 24<sup>th</sup> March 2020, to be applicable for the financial years commencing on or after the 1st April, 2020.
- Clause xx has been inserted in the CARO which specifically requires reporting on CSR. The same is read as under:
- *"(xx) (a) whether, in respect of other than ongoing projects, the company has transferred unspent amount to a Fund specified in Schedule VII to the Companies Act within a period of six months of the expiry of the financial year in compliance with second proviso to subsection (5) of Section 135 of the said Act;*
- *(b) whether any amount remaining unspent under sub-section (5) of section 135 of the Companies Act, pursuant to any ongoing project, has been transferred to special account in compliance with the provision of subsection (6) of Section 135 of the said Act"*
- A detailed Guidance Note to Auditors have also been issued by ICAI for reporting under CARO 2020.

## **Advisory issued by the ICAI**

### ***Responsibility of Auditors***

Wherever a Company undertakes CSR activity itself, the auditor of the company should ensure that:

- The activity/project undertaken is within the purview of Sch VII of the Act
- If mere contribution/donation is given, then the same is specifically allowed as per Schedule VII of the Act.
- Separate disclosure of CSR expenditure is made as per Sch III of the Act.
- Expenditure on the project is made as per Companies (CSR Policy) Rules 2014.
- The company has complied with applicable Accounting Standards in accounting, recognition and disclosure related to CSR spend.
- Auditor has complied with relevant Standards on Auditing for audit of CSR spend including:
  - SA 250 - Consideration of Laws and Regulations in an Audit of Financial Statements.
  - SA 720 (Revised) - The Auditor's Responsibilities Relating to Other Information

- He has complied with the Guidance note on Audit of Expenses. Wherever a Company undertakes CSR activity through a Third Party being eligible Section 8 Company / Registered Trust / Registered Society, the company should obtain an Independent Practitioner's Report on Utilisation of such CSR Funds from the auditor / CA in practice of the third party, to whom the funds are given by the Company for implementing CSR activity. The auditor / CA in practice of the third party before issuing the Independent Practitioner's Report on Utilization of CSR Funds should ensure that:
  - The third party has spent the funds on CSR activities as per Section 135 of the Companies Act, 2013, read with Schedule VII to the Act and related regulations.
  - Verification of the CSR spend has been done as per Guidance Note on Audit of Expenses issued by ICAI.
  - The utilization of CSR Funds report is issued in accordance with the Guidance Note on Reports or Certificates for Special Purposes issued by the Institute of Chartered Accountants of India.

# CSR Audit Stages

## Walk the Talk

- Definition of the depth & scope of the audit assignment
- Launching the assignment
- Interviews
- The analysis
- Delivery
- Does Your Company “Walk-the-Talk?”

# CSR Stakeholders

- **Government** - Adherence to legislations, Information Disclosure, & Environment Protection
- **Employees** - Safety, Health & Environment
- **Customers** - Quality control & Customer satisfaction
- **Shareholders** - Proactive communication & Information disclosure
- **Suppliers** - market information exchange (valued business partners)
- **Community** – social development, beneficiary
- **Professionals** – (In case of Audit/Assessment) Professional services



# Penal Provisions

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# Penalty for non-compliance

- **U/s 134(8)** – A company is required to attach with its report *the details about the policy developed and implemented by the company on CSR initiatives taken during the year [sec 134(3)(o)]*. In case of default, the company shall be liable to a penalty of Rs. 3,00,000 and every officer of the company who is in default shall be liable to a penalty of Rs. 50,000.
- **U/s 135(7)** - If a company is in default in complying with the provisions of sub-section (5) [spending 2% of average net profit, transfer of unspent amount to Sch VII fund etc] or sub-section (6) [transfer of unspent amount in ongoing project to special account], the company shall be liable to a penalty of **2X** the amount required to be transferred by the company to the Schedule VII Fund or the Unspent CSR Account, as the case may be, or Rs. **1 Crore**, whichever is less, and every officer of the company who is in default shall be liable to a penalty of **1/10<sup>th</sup>** of the amount required to be so transferred by the company, or **Rs. 2 Lakhs**, whichever is less.

# CSR Impact Assessment

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# Why Impact Assessment?

- Companies are required to understand what tangible and intangible changes have been brought about in the lives of the communities where its CSR projects were implemented. It also has to communicate this to the relevant stakeholders.
- In order to understand the overall outcome and impact of the project from the point of view of the beneficiaries an Impact Assessment is essential.

- As per the amendments brought by Companies (CSR Policy) Amendment Rules, 2021 Impact Assessment of CSR projects in some cases is **mandatory**
- Companies with an average CSR obligation of Rs. **10 crores** or more in **3 immediately preceding FYs** are mandatorily required to undertake impact assessment (IA) through an independent agency of their CSR projects.
- Impact assessment, where applicable, has to be done for:
  - Every project with an outlay of more than **INR 1 Cr**
  - Which has completed **1 year** of completion
- The IA report has to be **placed before the Board** and annexed to the annual report on CSR.
- Impact Assessment companies/firms can claim up to **5%** of total CSR expenditure or Rs. 50 lakh, whichever is less. for impact assessment
- Social Impact assessment in India has its roots in Government programmes to understand the impact of public initiatives. Some organisations undertake Impact Assessment. For certain specific sectors, standards for assessment have also been laid.

# Difficulties in IA

- Measuring the effects of one's CSR activities is very important.
- But measuring the impact may be difficult as some benefits like customer loyalty, better reputation etc are hard to quantify.
- Further measurement shows only the immediate impact of CSR.

# How to measure the impact of CSR?

In one of the following ways:

- By benchmarking one's business against others
- By employing a firm of professionals for Impact Assessment
- By measuring Social Return on Investment
- By seeking recognition for CSR best practices like CSR awards
- By using Key Performance Indicators (KPIs) to measure one's environmental performance
- Getting ISO 26000 certification (Guidance on operating businesses in a socially responsible way)

# Types of Impact Assessment

## Mandatory Impact Assessment

- IA is now mandatory for certain categories of companies in India.

## Voluntary Impact Assessment

- IA can also be done for future projects to understand the potential changes they might bring in the lives of the communities. This will help set up an action plan that will mitigate any possible damages to the community and environment.



# Component of Social Impact Assessment

- analyzing,
- monitoring,
- evaluating and
- managing social outcomes, both positive and negative.

# The benefits of Impact Assessment

- Helps the company get expert opinion and advice
- Helps generating local knowhow
- Helps analyze the concerns of interested and affected parties
- Helps disclose the importance of a company's activities to its stakeholders
- Helps monitor the planned intervention
- Helps improve decision-making process
- Helps analyze the alternatives
- Helps involve all stakeholders
- Helps understand the change in the lives of direct beneficiaries of the project.

...contd

...contd

- Helps in understanding the impact on the lives of indirect beneficiaries
- Helps align the company's CSR activities with corporate goals like reduce employee turnover, develop staff skills etc.
- Helps analysing the efficiency & effectiveness of the project
- Helps understand the Sustainability aspects of the projects
- Helps in setting up a feedback system for possible improvement
- Helps keep track of the progress in case of multi-year projects and thus ensure better implementation
- Helps decide which projects not to take up in future
- Helps plan more future projects

# How to do IA?

- Measuring the level of community support for the CSR projects
- Measuring the impact of CSR programs on the target groups, i.e. the beneficiaries
- Measuring the effect of CSR programs on the target geographical area, i.e the project location
- Measuring the effect of CSR programs on the type of activity taken up e.g. education, health, sanitation programmes etc.
- Matching the parameters as laid down by the CSR Committee w.r.t. the projects.
- Measuring the progress of the project as per the implementation schedule
- In case of an agency involved, measuring the diligence level of the agency

...contd

...contd

- Regularity of formal and informal dialogue between the company and the stakeholders.
- Frequency of collection of stakeholders' feedback
- Importance attached to stakeholders' feedback and whether the same is placed before committee meetings
- Whether correctional measures are taken on the basis of complaints received.
- Measuring the impact of the CSR projects on its goodwill and brand.
- Listing out the media comments on the company's CSR activities, both positive and negative
- Measuring the level of employee motivation and employee involvement
- Checking the initiatives of employees through volunteering

# Social Stock Exchange

(for discussion)

# Social Audit

(for discussion)

# Social Audit vis-à-vis CSR Audit

(for discussion)



# Social Audit Standards

(for discussion)

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# Other CSR Assessment Tools

- Corporate Responsibility Index (CRI)
- Social Return on Investment (SRoI)
- CSR Rating

# Corporate Responsibility Index (CRI)

- CRI is a management and benchmarking tool developed by UK's Business in the Community (BITC), a charitable organisation
- The idea behind is to assist management in improving their CSR performance and to allow benchmarking of companies on various aspects of CSR
- BITC recommends incorporation of a 'Corporate Responsibility Index' in Annual Financial Statements
- BITC publishes a Corporate Responsibility Index, which measures the performance of companies in terms of how well they apply CSR values to their business.
- BITC claims a membership of over 850 of the UK's top companies "committed to improving their positive impact on society".
- Can we have something like CRI in India?

# Social Return on Investment (SRoI)

- Social Return on Investment (SRoI) is an organisational method of accounting for value creation, w.r.t. social and environmental parameters. It helps organizations measure the value of its activities on the society. So SRoI is the social value generated for every rupee invested in developmental activities by the company
- SRoI helps companies to calculate a cost-benefit ratio for its investment.
- It helps communicate the social value generated by a project in the form of a number that can be easily understood by all stakeholders.

# CSR Rating

- The **ISO 26000:2010 – Guidance on Social Responsibility** was released by International Organization for Standardization in 2010. The idea was to help companies to contribute towards global sustainable development.
- Based on the above the Bureau of Indian Standard (BIS) has developed the standard **IS 26001:2020 – Corporate Social Responsibility** which compliments the compliance requirements u/s 135 of the Companies Act, 2013. It contains parameters to help a company get the Star Rating for CSR Performance. It has a Basic Level Certification and an Advanced Level Certification to help companies improve their CSR performance. The standards are applicable to all types of companies and supplements the CSR Legislations contained in the Companies Act, 2013 and the Companies (CSR Policy) Rules, 2014 and does not override/nullify it in any way.

# CSR Rating ...contd

## Principles and Parameters

This standard has a set of **5 Principles** supported by **9 parameters** that are distributed across the respective cycle(s) in the form of a PDCA (Plan, Do, Check, Act) Matrix.

Cycle	Principles	Parameter(s)
PLAN	1) CSR Governance	a) Parameter 1 – Functions and responsibilities of the board b) Parameter 2 – Composition and constitution of the CSR committee c) Parameter 3 – CSR policy, functions and responsibilities of the CSR committee
	2) CSR Planning	a) Parameter 4 – CSR projects b) Parameter 5 – Identification of credible implementing agencies
DO	3) Funds and Resources for Implementing CSR Projects	a) Parameter 6 – Provision of funds and resources
CHECK	4) Monitoring, Evaluation and Impact	a) Parameter 7 – Process for monitoring of CSR projects and activities; b) Parameter 8 – Evaluation and impact of CSR projects
ACT	5) CSR Reporting	a) Parameter 9 – CSR reporting

# CSR Rating ...contd

## Criteria for Basic Level CSR and Advanced Level CSR

- Basic Level Certification (BLC) – 1 star
- Advanced Level Certification (ALC) – 2 to 5 stars
- To get the certification a company must comply with all legal performance criteria mentioned in the Annexure to the IS 26001:2020. The criteria for BLC are mainly based on mandatory compliance. The criteria for ALC mainly outline the principles of moving beyond compliance and provide the provisions of getting the “CSR Star Rating Certification” based on performance.
- Appropriate documented information has to be maintained for BLC and ALC certification
- Company seeking the certifications shall ensure compliance with all applicable legal requirements w.r.t CSR in the *Companies Act, 2013* and CSR Rules.

**Thank You**

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