

Clarification on CSR after MCA FAQs dated August 25, 2021

1. Calculation of Net Profit Before Tax

Explanation under Section 135 (5) for Net Profit read as follows:

For the purposes of this section “**net profit**” shall not include such sums as may be prescribed, and shall be calculated in accordance with the provisions of section 198.

Net Profit as per CSR Rules, 2021 read as follows:

Net profit of a company as per its financial statement prepared in accordance with the applicable provisions of the Act, but shall not including profit arising from any overseas branch(es) or company, any dividend received from any other company in India which are covered under and complying with provisions of Section 135 of the Act.

Our Comments:

There is anomaly in definition of Net Profit and hence the Company need to calculate Net Profit in accordance with Section 198 of the Companies Act, 2013.

2. Applicability of CSR

Section 135 (1) read as follows:

Every company having Net Worth of Rs.500 Cr or more, or Turnover of Rs.1000 Cr. or more or Net profit of Rs.5 Cr or more, during the **immediately preceding financial year** shall constitute a Corporate Social Responsibility Committee of the Board consisting of 3 or more Directors, out of which at least 1 director shall be an Independent Director.

CSR Rule 3 (2) read as follows:

Every company which ceases to be a company covered under subsection (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 of CSR under sub-section (2) to (6) of the section 135, till such time it meets the threshold limits of Net Worth, Turnover or Net profit as specified u/s 135(1) of the Act.

Our Comments:

The Company shall be out of obligation of CSR Spend u/s 135 only if three consecutive financial years it has less than the threshold limits of Net Worth, Turnover or Net profit. Until this anomaly is not clarified by MCA or rules are amended in sync with section 135 (1) of the Act.

3. Formulation of CSR Committee

Section 135 (9) read as follows:

Where the amount to be spent by a company on **CSR does not exceed Rs.50 Lac**, the company is not required to constitute CSR Committee and the functions of CSR Committee shall be discharged by the Board of Directors of such company.

CSR Rule 3 (2) read as follows:

Every company which ceases to be a company covered under subsection (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 of CSR under sub-section (2) to (6) of the section 135, till such time it meets the threshold limits of Net Worth, Turnover or Net profit as specified u/s 135(1) of the Act.

Our Comments:

The Company may continue to have CSR Committee or may dissolve the same if the CSR spent is less than Rs.50 Lacs.

4. Section 8 Company also to comply with Section 135

Section 135 (1) reads that every company exceeding or equal to the threshold criteria of Net Worth or Turnover or Net profit shall comply with section 135 and Rules.

According to Section 8 (1) (b), Section 8 Company intends to apply its profit, if any, or other income in promoting its objects. Arguments are made that Section 8 Company applies its profit or income for promotion of its main object which is primarily not for profit. Further provisions of Section 2 (40) read with Schedule III, financial statements cover not just Profit & Loss Account but also Income and Expenditure account.

Our Comments:

As per MCA FAQs dt 25.08.2021, Section 135 (1) applies to all companies that includes section 8 companies also.

5. Expenses for Administrative overheads and Expenses of Implementing Agency

Rule 7 of CSR Rules states that the Board shall ensure that the administrative overheads shall not exceed **5% of total CSR expenditure** of the company for the financial year.

Rule 2 (b) defines “Administrative overheads” means the expenses incurred by the company for ‘general management and administration’ of CSR functions in the company but shall not

include the **expenses directly incurred** for the designing, implementation, monitoring, and evaluation of a particular CSR project.

Our Comments:

Any expenses made by Implementing Agency for CSR project is expenses incurred in designing, implementing, monitoring or evaluation of project, which is not part of Administrative Expenses. The Company and the Implementing Agency are two separate entity and expenses incurred by one cannot be claimed by other.

6. On –Going Project? When it can be regarded as “Commenced”

Rule 2(i)-“Ongoing Project” means a multi-year project undertaken by a Company in fulfilment of its CSR obligation having timelines not exceeding three years excluding the financial year in which it was **commenced**, and shall 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;

MCA has clarified in FAQs dated 25.08.2021 that an Ongoing Project is considered to be commenced , when the company has either **issued the work order** pertaining to the project or **awarded the contract** for execution of the project.

Our Comments:

The Board may with the reasonable justification, can approve the Project before 31.03.2021 as on-Going Project that was initially not approved as multi-year project. The Board may either **issue the work order or award the contract** prior to 31.03.2021 so that it can be considered that on-Going project was commenced in FY 2020-21. In next three FY that is FY 2021-22 to 2023-24 the CSR spend to be made on the said Project.

7. Funds disbursed or used is considered as compliance

Mere disbursement of funds for implementation of a project does not amount to spending unless the implementing agency utilizes the whole amount. It is the duty of the Board to satisfy itself that the funds of the company disbursed to implementing agency have been utilized for the purpose and in the manner as approved. CFO or person responsible for financial management also to certify to the effect.

Our Comments:

Can company reimburse / replenish the funds to implementing agency , which implementing agency had spent on the similar project from the available funds with them. Can IA give utilization certificate by doing so?

8. Excess amount spent in FY 2019-20 can be taken as set off

MCA vide circular dated 20th May 2021, said that where a Company has contributed any amount to “PM CARES FUND” on March 31, 2020, which is over and above the minimum amount as prescribed under Section 135 (5) of the Companies Act 2013 for FY 2019–20, such excess amount (or part thereof) can be set off against the requirement of CSR obligations for FY 2020-21, subject to the fulfilment of the following three conditions;

1. The amount offset as such shall have factored the unspent CSR amount for previous financial years, if any;
2. The Chief Financial Officer shall certify that the contribution to “PM CARES Fund” was indeed made on 31st March 2020 in pursuance of the appeal and the same shall also be so certified by the statutory auditor of the company; and
3. The details of such contribution shall be disclosed separately in the Annual Report on CSR as well as in the Board’s Report for FY 2020-21 in terms of section 134 (3) (o) of the Act.

Our Comments:

The Company need to satisfy all the three conditions mentioned above, before it takes set off of spent in FY 2019-20.

9. Other clarifications

- a. What is spent/ unspent/ when to transfer to separate bank account?
- b. What amount to be set off or carry forward?
- c. Foreign Company & CSR Obligation.
- d. Contribution to Corpus is not CSR.
- e. Capital Assets- Stamp duty / Registration fees shall qualify as CSR expenditure.
- f. CSR spend cannot be in kind?
- g. If company is carrying CSR activities on its own, no Form CSR-1 is required to be filed.
- h. International Organization cannot be used for implementation. It can be used for Designing, Monitoring, Evaluating and capacity building.
- i. On-Going project to be multiyear project (1+3 years).
- j. Funds earmarked for one project can be used for other subject to approval of the Board and CSR Committee with proper justification.
- k. Any spend benefitting exclusively to employees is not CSR.
- l. Any one off activity or sponsorship is not CSR.
- m. Registered Public Trust includes Trust Registered under Income Tax Act, 1961 in such State where Registration of Trust is not mandatory.
- n. Filing of Form CSR-1 Registration is to develop CSR Eco-System.
- o. Separate Bank Account to be opened for Unspent Amount for each FY, not for each on-going project.
- p. Funds in such Separate Bank account cannot be used by the company for collateral or creating charge or for any business activity.
- q. Earlier period projects cannot be considered as On-Going Project.

- r. Any violation is civil wrong and monetary penalties to be levied.
- s. Impact Assessment is for project completed on or after 22 January 2021.
- t. All CSR Project approved by the Board need to be disclosed on the website of the Company, if any.

Conclusions:

MCA has introduced this unique concept of CSR in 2014, initially as voluntary responsibility of Corporate. However it failed and hence MCA mandated it with more prescriptive rules to bring transparency, uniformity, clarity in the compliance of CSR obligations. Private –Public partnership plays an inordinate role in Nation building. It is a welcome move of MCA , however in the same breadth, we say that the new FAQs issued by MCA on 25.08.2021 created more confusion than the clarity.

Be that as it may, we need to see efficacy of stringent prescriptive rules and compliance regime around CSR in a year, when the new format of Report on CSR will be available for FY 2020-21. Days are also not far that we may see a separate Code only on CSR with more uniformity, accountability and implementation. Social Stock Exchanges (SSE) will also be playing imperative role for supporting, nurturing and scaling up the social initiative, social entrepreneurship and eco system for social impact investment. SSE will help various entities in social initiative to raise the funds and bridge the gap between the donor and beneficiaries.

Personally, I find it very interesting and soul fulfilling activity. This space is absolutely NishkamSewa (without any reason or greed of reward) which brings clarity of living and purpose of life.
