After studying this chapter, you would be able to

- Comprehend corporate social responsibility (CSR).
- Examine the various terminologies used in applying the provisions of CSR.
- Analyse the various situations under which CSR shall be implemented as per the statute.
- Deal with the Accounting and Reporting aspects of CSR.
1. INTRODUCTION

Corporate Social Responsibility (‘CSR’) is corporate initiative to assess and take responsibility for the company's effects on the environment and its impact on social welfare. It can be conceptualized as the corporations’ obligation to take necessary action to reduce the negative externalities and enhance the positive externalities associated with their business. In doing so, the corporations could protect and promote the interests of their stakeholders and society as a whole.

The origin of CSR can be traced to philanthropic activities of corporations, viz., donations and charity. Over the years, the concept of CSR has evolved and it now includes within its scope, triple bottom line approach (achieving a balance of economic, environmental and social imperatives), corporate sustainability, improving and developing skills for sustainability, to name a few.

CSR is the process by which an organization thinks about and evolves its relationships with stakeholders for the common good, and demonstrates its commitment in this regard by adoption of appropriate business processes and strategies. Thus, CSR is not charity or mere donations. CSR is a way of conducting business, by which corporate entities visibly contribute to the social good.

Socially responsible companies do not limit themselves to using resources to engage in activities that increase only their profits. They use CSR to integrate economic, environmental and social objectives with the company's operations and growth.
2. CORPORATE SOCIAL RESPONSIBILITY (CSR)

"Corporate Social Responsibility (CSR)" means and includes but is not limited to:

1. Projects or programs relating to activities specified in Schedule VII or

2. Projects or programs relating to activities undertaken by the board of directors of a company (Board) in pursuance of recommendations of the CSR Committee of the Board as per declared CSR Policy of the company

3. WHICH COMPANY TO PERFORM CORPORATE SOCIAL RESPONSIBILITY?

Every company including its holding or subsidiary, and a foreign company defined under clause (42) of section 2 of the Act having its branch office or project office in India which fulfils the criteria specified in sub-section (l) of section 135 of the Act shall comply with the provisions of section 135 of the Act and these rules:

Provided that net worth, turnover or net profit of a foreign company of the Act shall be computed in accordance with balance sheet and profit and loss account of such company prepared in accordance with the provisions of clause (a) of sub-section (1) of section 381 and section 198 of the Act.

Illustration 1

ABC Ltd. is a company which is formed with charitable objects under Section 8 of the Companies Act, 2013. As a result, the management of the company believes that as all the activities of the company will be with the intent of charity, the CSR provisions are not applicable to ABC Ltd. as these activities are activities in normal course of business.

Whether the provisions of CSR are applicable to ABC Ltd. provided it fulfils the criteria of Section 135 of the Act?

Solution

Section 135 of the Companies Act is applicable to every company meeting the specified criteria. As per section 2(20) of the Companies Act, ‘company’ means a company incorporated under the Companies Act or under any other previous company law. This would imply that companies set up for the purposes of CSR/public welfare are also required to comply with the provisions of CSR.
4. STATUTORY PROVISIONS

In India, the Companies Act, 2013 has statutorily recognised the concept of CSR. Section 135 of the Companies Act, 2013 read with Schedule VII thereto and Companies (Corporate Social Responsibility Policy) Rules, 2014 are the special provisions under the new company law regime imposing mandatory CSR obligations.

4.1 Important Definitions

(a) **Any financial year:** “Any financial year” referred under sub-section (1) of Section 135 of the Act read with Rule 3(2) of Companies CSR Rule, 2014, implies ‘any of the three preceding financial years’. *(Clarification vide MCA General Circular No. 21/2014)*

(b) **Average Net Profit:** “Average Net Profit” is the amount as calculated in accordance with the provisions of Section 198 of the Companies Act, 2013.

(c) **Financial Year:** “Financial Year”, in relation to any company or body corporate, means the period ending on the 31st day of March every year, and where it has been incorporated on or after the 1st day of January of a year, the period ending on the 31st day of March of the following year, in respect whereof financial statement of the company or body corporate is made up.

If a holding company or a subsidiary of a company incorporated outside India follows a different financial year for consolidation of its accounts outside India, the Tribunal may allow (on application) any period as its financial year, whether or not that period is a year, provided it align its financial year as per the Act, within a period of two years.

(d) **Net Profit:** “Net Profit” means the net profit of a company as per its financial statement prepared in accordance with the applicable provisions of the Act, but shall not include the following, namely:

(i) any profit arising from any overseas branch or branches of the company, whether operated as a separate company or otherwise; and

(ii) any dividend received from other companies in India, which are covered under and complying with the provisions of section 135 of the Act:

(e) **Net worth:** “Net worth” means the aggregate value of the paid-up share capital and all reserves created out of the profits and securities premium account, after deducting the aggregate value of the accumulated losses, deferred expenditure and miscellaneous expenditure not written off, as per the audited balance sheet, but does not include reserves created out of revaluation of assets, write-back of depreciation and amalgamation.

(f) **Turnover:** “Turnover” means the aggregate value of the realisation of amount made from the
sale, supply or distribution of goods or on account of services rendered, or both, by the company during a financial year;

(g) **Spend:** The term 'spend' in accounting parlance generally means the liabilities incurred during the relevant accounting period.

### 4.2 The Companies Act, 2013

**A. As per section 135 of the Companies Act 2013**

Every company having either

- net worth of ₹ 500 crore or more, or
- turnover of ₹ 1,000 crore or more or
- a net profit of ₹ 5 crore or more

**during any financial year** shall constitute a Corporate Social Responsibility (CSR) Committee of the Board consisting of three or more directors (including at least one independent director).

#### Illustration 2

ABC Ltd. is a company which has a net worth of INR 200 crores, it manufactures rubber parts for automobiles. The sales of the company are affected due to low demand of its products. The previous year's financials state:

<table>
<thead>
<tr>
<th>(INR in Crores)</th>
<th>March 31, 20X4 (Current year)</th>
<th>March 31, 20X3</th>
<th>March 31, 20X2</th>
<th>March 31, 20X1</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net Profit</td>
<td>3.00</td>
<td>8.50</td>
<td>4.00</td>
<td>3.00</td>
</tr>
<tr>
<td>Sales (turnover)</td>
<td>850</td>
<td>950</td>
<td>900</td>
<td>800</td>
</tr>
</tbody>
</table>

**Required**

*Does the Company have an obligation to form a CSR committee since the applicability criteria is not satisfied in the current financial year?*

**Solution**

It has been clarified that ‘any financial year’ referred to under sub-section (1) of section 135 of the Act read with Rule 3(2) of Companies CSR Rule, 2014, implies ‘any of the three preceding financial years’.

A company which meets the net worth, turnover or net profits criteria in any of the preceding three financial years, but which does not meet the criteria in the relevant financial year, will still need to constitute a CSR Committee and comply with provisions of sections 135 (2) to (5) read with the CSR Rules.
As per the criteria to constitute CSR committee -

1) Net worth greater than or equal to INR 500 Crores: This criterion is not satisfied.

2) Sales greater than or equal to INR 1000 Crores: This criterion is not satisfied.

3) Net Profit greater than or equal to INR 5 Crores: This criterion is satisfied in financial year ended March 31, 20X3.

Hence, the Company will be required to form a CSR committee.

B. Role of Corporate Social Responsibility (CSR) Committee

The CSR Committee shall—

(a) formulate and recommend to Board-
   a. a CSR Policy indicating the activities to be undertaken by the company as specified in Schedule VII;
   b. the amount of expenditure to be incurred on the above activities and

(b) monitor the CSR Policy of the company from time to time.

C. Role of Board

Board shall disclose-

(a) The composition of CSR Committee in its report
(b) Approve the recommended CSR Policy for the company
(c) Disclose the contents of such Policy in its report and place it on the company’s website
(d) Ensure that the activities included in CSR Policy of the company are duly executed by the company
(e) Ensure that the **company spends, in every financial year, at least two per cent** of the **average net profits** of the company made **during the three immediately preceding financial years** by giving preference to the local area and areas around it where it operates
(f) In case the company fails to spend such amount, the Board shall specify the reasons for not spending the amount.
Section 135

During any financial year

Net worth ≥ ₹ 500 crore

Yes

Form a CSR Committee and Report to Board

No

Turnover ≥ ₹ 1000 crore

Yes

Formulate & Recommend CSR Policy to Board

No

 Recommend amount of expenditure for CSR activities

Monitor CSR Policy

Net profit ≥ ₹ 5 Crore

Yes

Do not form a CSR Committee

No

Role of Board

Approve & Disclose CSR Policy

Ensure undertaking of CSR activities and spending of amount

Turnover ≥ ₹ 1000 crore

No

Net worth ≥ ₹ 500 crore

No

Formulate & Recommend CSR Policy to Board

Net profit ≥ ₹ 5 Crore

No

Role of Board

Approve & Disclose CSR Policy

Ensure undertaking of CSR activities and spending of amount

° The Institute of Chartered Accountants of India
Illustration 3

ABC Ltd. manufactures consumable goods like bath soap, tooth brushes, soap cases etc. As part of its CSR policy, it has decided to that for every pack of these goods sold, INR 0.80 will go towards the 'Save trees foundation' which will qualify as a CSR spend as per Schedule VII. Consequently, at the year end, the company sold 25,000 such packs and a total of INR 20,000 was recognised as CSR expenditure. However, this amount was not paid to the foundation at the end of the financial year.

Required

Will the amount of INR 20,000 qualify to be a CSR expenditure?

Solution

By earmarking the amount from such sale for CSR expenditure, the company cannot show it as CSR expenditure. To qualify the amount to be CSR expenditure, it has to be spent. Hence, INR 20,000 will not be automatically considered as CSR expenditure until and unless it is spending on CSR activities.

4.3 Calculation of “Net Profit” as per Section 198

(1) In computing the net profits of a company in any financial year,

(a) credit shall be given for the sums specified in sub-section (2), and credit shall not be given for those specified in sub-section (3); and

(b) the sums specified in sub-section (4) shall be deducted, and those specified in sub-section (5) shall not be deducted.

(2) In making the computation aforesaid, credit shall be given for the bounties and subsidies received from any Government, or any public authority constituted or authorised in this behalf, by any Government, unless and except in so far as the Central Government otherwise directs.

(3) In making the computation aforesaid, credit shall not be given for the following sums, namely:

(a) profits, by way of premium on shares or debentures of the company, which are issued or sold by the company;

(b) profits on sales by the company of forfeited shares;

(c) profits of a capital nature including profits from the sale of the undertaking or any of the undertakings of the company or of any part thereof;

(d) profits from the sale of any immovable property or fixed assets of a capital nature comprised in the undertaking or any of the undertakings of the company, unless the business of the company consists, whether wholly or partly, of buying and selling any such
property or assets:

Provided that where the amount for which any fixed asset is sold exceeds the written-down value thereof, credit shall be given for so much of the excess as is not higher than the difference between the original cost of that fixed asset and its written down value;

(e) any change in carrying amount of an asset or of a liability recognised in equity reserves including surplus in profit and loss account on measurement of the asset or the liability at fair value.

(4) In making the computation aforesaid, the following sums shall be deducted, namely:

(a) all the usual working charges;

(b) directors’ remuneration;

(c) bonus or commission paid or payable to any member of the company’s staff, or to any engineer, technician or person employed or engaged by the company, whether on a whole-time or on a part-time basis;

(d) any tax notified by the Central Government as being in the nature of a tax on excess or abnormal profits;

(e) any tax on business profits imposed for special reasons or in special circumstances and notified by the Central Government in this behalf;

(f) interest on debentures issued by the company;

(g) interest on mortgages executed by the company and on loans and advances secured by a charge on its fixed or floating assets;

(h) interest on unsecured loans and advances;

(i) expenses on repairs, whether to immovable or to movable property, provided the repairs are not of a capital nature;

(j) outgoings inclusive of contributions made under section 181;

(k) depreciation to the extent specified in section 123;

(l) the excess of expenditure over income, which had arisen in computing the net profits in accordance with this section in any year which begins at or after the commencement of this Act, in so far as such excess has not been deducted in any subsequent year preceding the year in respect of which the net profits have to be ascertained;

(m) any compensation or damages to be paid in virtue of any legal liability including a liability arising from a breach of contract;

(n) any sum paid by way of insurance against the risk of meeting any liability such as is referred to in clause (m);
(o) debts considered bad and written off or adjusted during the year of account.

(5) In making the computation aforesaid, the following sums shall not be deducted, namely:

(a) income-tax and super-tax payable by the company under the Income-tax Act, 1961, or any other tax on the income of the company not falling under clauses (d) and (e) of sub-section (4);

(b) any compensation, damages or payments made voluntarily, that is to say, otherwise than in virtue of a liability such as is referred to in clause (m) of sub-section (4);

(c) loss of a capital nature including loss on sale of the undertaking or any of the undertakings of the company or of any part thereof not including any excess of the written-down value of any asset which is sold, discarded, demolished or destroyed over its sale proceeds or its scrap value;

(d) any change in carrying amount of an asset or of a liability recognised in equity reserves including surplus in profit and loss account on measurement of the asset or the liability at fair value.

4.4 Important Points on CSR Activities

1. The CSR activities undertaken by the company shall exclude activities undertaken in pursuance of its normal course of business.

2. A company may collaborate with other companies for undertaking projects or programs 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 programs in accordance with these rules.

Illustration 4

*How can companies with small CSR funds take up CSR activities in a project/program mode?*

**Solution**

It has been clarified that companies can combine their CSR programs with other similar companies by pooling their CSR resources.

As per Rule 4 of the CSR Rules, a company may collaborate with other companies for undertaking projects or for CSR activities in such a manner that the CSR committees of the relevant companies are in a position to report separately on such projects in accordance with the prescribed Rules.

3. The CSR projects or programs or activities undertaken in India only shall amount to CSR expenditure.
Illustration 5

Due to immense loss to Nepal in the recent earthquake, one FMCG Company undertakes various commercial activities with considerable discounts and concessions at the related affected areas of Nepal for a continuous period of 3 months after earthquake. In the Financial Statements for the year 20X1-2X2, the Management has shown the expenditure incurred on such activity as expenditure incurred to discharge Corporate Social Responsibility.

Required

State whether the treatment done by the management of management is correct. Explain with reasons.

Solution

The Companies Act, 2013 mandated the corporate entities that the expenditure incurred for Corporate Social Responsibility (CSR) should not be the expenditure incurred for the activities in the ordinary course of business. If expenditure incurred is for the activities in the ordinary course of business, then it will not be qualified as expenditure incurred on CSR activities.

The statutory guidelines relating to CSR also require the deployment of funds for the benefit of the local area of the Company. Since Nepal is another country the expenditure done there i.e. in Nepal shall not qualify to be accounted as CSR expenditure.

Further, it is presumed that the commercial activities performed at concessional rates are the activities done in the ordinary course of business of the company. Therefore, the treatment done by the Management by showing the expenditure incurred on such commercial activities in its financial statements as the expenditure incurred on activities undertaken to discharge CSR, is not correct.

4. The CSR projects or programs or activities that benefit only the employees of the company and their Families shall not be considered as CSR activities in accordance with section 135 of the Act.

5. Companies may build CSR capacities of their own personnel as well as those of their Implementing agencies through Institutions with established track records of at least three financial years but such expenditure (including expenditure on administrative overheads) shall not exceed five percent of total CSR expenditure of the company in one financial year.

6. Contribution of any amount directly or indirectly to any political party, shall not be considered as CSR activity.

7. The surplus arising out of the CSR projects or programs or activities shall not form part of the business profit of a company.

8. CSR expenditure shall include all expenditure including contribution to corpus, for projects or programs relating to CSR activities approved by the Board on the recommendation of its CSR
Committee, but does not include any expenditure on an item not in conformity or not in line with activities which fall within the purview of Schedule VII of the Act.

9. The Board’s Report of a company shall include an annual report on CSR containing particulars as specified.

Illustration 6

ABC Ltd. is a company which comes under the ambit of Section 135 and CSR Rules. The Board of ABC Ltd did not appropriate the CSR funds and as a result there was no annual report on CSR in the Board’s report for financial year ended March 31, 20X1.

Required

Is this a non-compliance as per the Act?

Solution

It has been clarified that as per Rule 9 of the CSR Rules, the Board’s Report of a company qualifying under section 135 shall include an annual report on CSR, containing particulars specified in Annexure to CSR Rules. Reporting of CSR policy of the company in the Board’s Report is a mandatory requirement. If the disclosure requirements are not fulfilled, penal consequences may be attracted under section 134(8) of the Companies Act.

4.5 Permissible Activities under Corporate Social Responsibility Policies: Schedule VII

As per Schedule VII of Companies Act 2013, following activities may be included by companies in their Corporate Social Responsibility Policies Activities relating to:

1. eradicating hunger, poverty and malnutrition, promoting health care including preventive health care and sanitation including contribution to the Swach Bharat Kosh set-up by the Central Government for the promotion of sanitation and making available safe drinking water.

2. promoting education, including special education and employment enhancing vocation skills especially among children, women, elderly and the differently abled and livelihood enhancement projects.

3. promoting gender equality, empowering women, setting up homes and hostels for women and orphans; setting up old age homes, day care centres and such other facilities for senior citizens and measures for reducing inequalities faced by socially and economically backward groups;

4. ensuring environmental sustainability, ecological balance, protection of flora and fauna, animal welfare, agroforestry, conservation of natural resources and maintaining quality of soil, air and water including contribution to the Clean Ganga Fund set-up by the Central Government for rejuvenation of river Ganga;
5. protection of national heritage, art and culture including restoration of buildings and sites of historical importance and works of art; setting up public libraries; promotion and development of traditional arts and handicrafts;

6. measures for the benefit of armed forces veteran, war widows and their dependents;

7. training to promote rural sports nationally recognized sports and Olympic sports;

8. contribution to the Prime Minister's National Relief Fund or any other fund set up by the Central Government for socio-economic development and relief and welfare of the Scheduled Castes, the Scheduled Tribes, other backward classes, minorities and women; and

9. contributions or funds provided to technology incubators located within academic institutions which are approved by the Central Government;

10. rural development projects.

11. slum area development.

Note: Additional items included in Schedule VII or clarified as already being covered under Schedule VII of the Act is given as Appendix II of the chapter.

## 5. ACCOUNTING FOR CSR TRANSACTIONS

### 5.1 Revenue Expenditure made in the Current Financial Year

<table>
<thead>
<tr>
<th>Debit (INR)</th>
<th>Credit (INR)</th>
</tr>
</thead>
<tbody>
<tr>
<td>CSR Expenditure (Profit and loss statement)</td>
<td>XXX</td>
</tr>
<tr>
<td>To Cash/Vendor</td>
<td>XXX</td>
</tr>
</tbody>
</table>

CSR Expenditure is an item of profit and loss statement.

Item 5 (A)(k) of the General Instructions for Preparation of Statement of Profit and Loss under Schedule III to the Companies Act, 2013, requires that in case of companies covered under Section 135, the amount of expenditure incurred on ‘Corporate Social Responsibility Activities’ shall be disclosed by way of a note to the statement of profit and loss.

The treatment of revenue expenditure will be the same under AS and Ind AS.

### 5.2 CSR Expenditure made towards a Capital Asset

In case the expenditure incurred by the company is of such a nature that give rise to an ‘asset’, it should be recognised by the company in its balance sheet, provided the control over the asset is
with the Company and future economic benefits are expected to flow to the company.

Example
A school building is transferred to a Gram Panchayat for running and maintaining the school, it should not be recognised as ‘an asset’ in its books and such expenditure would need to be charged to the statement of profit and loss as and when incurred.

1. Accounting treatment as per AS

Where any CSR asset is recognized in its balance sheet, the same may be classified under natural head (e.g. Tangible assets or Intangible assets) with specific subhead of ‘CSR Asset’ if the expenditure satisfies the recognition criteria of ‘asset’.

<table>
<thead>
<tr>
<th>Debit (INR)</th>
<th>Credit(INR)</th>
</tr>
</thead>
<tbody>
<tr>
<td>CSR Asset (Balance Sheet)</td>
<td>XXX</td>
</tr>
<tr>
<td>To Cash/Vendor</td>
<td>XXX</td>
</tr>
</tbody>
</table>

2. Accounting treatment as per Ind AS

The accounting entry as given above remains the same. However, there is a difference in the classification of Non-current asset under Ind AS.

Where any CSR asset is recognized in its balance sheet, the same may be classified under natural head (e.g. Property plant and equipment, Intangible assets or Investment property) with specific sub-head of ‘CSR Asset’ if the expenditure satisfies the recognition criteria of ‘asset’.

The recognition criteria for asset under Ind AS i.e.,

- Ind AS 16 : Property, plant and equipment,
- Ind AS 40 : Investment Property
- Ind AS 38 : Intangible assets

is to be satisfied.

Illustration 7

A building is used for CSR activities of the company. The same is capitalised as ‘an asset’ in the books and depreciation is charged on the same as per the Companies Act, 2013. The Company claims the cost of the building as ‘CSR expenditure’ and also the depreciation thereon.

Required

Is this the correct treatment as per the Act?
Solution

In case the expenditure incurred by the company is of such nature which may give rise to an ‘Asset’, it should be recognised by the company in its balance sheet, provided the control over the asset is with the Company and future economic benefits are expected to flow to the company. Where any CSR asset is recognized in its balance sheet, the same may be classified under natural head (e.g. Building, Plant & Machinery etc.) with specific sub-head of ‘CSR Asset’ if the expenditure satisfies the definition of ‘asset’.

For example, a building used for CSR activities where the beneficial interest has not been relinquished for lifetime by a company and from which any economic benefits flow to a company, may be recognised as ‘CSR Building’ for the purpose of reflecting the same in the balance sheet.

If an amount spent on an asset has been shown as CSR spend, then the depreciation on such asset cannot be claimed as CSR spend again. Once cost of the asset is included for CSR spend, then the depreciation on such asset will not be included for CSR spend even if the asset is capitalized in the books of accounts and depreciation charged thereon.

5.3 Whether any Unspent Amount of CSR Expenditure is to be Provided for?

Facts

- **Section 135 (5) of the Companies Act, 2013**, requires that the Board of every eligible company, “shall ensure that the company spends, in every financial year, at least 2% of the average net profits of the company made during the three immediately preceding financial years, in pursuance of its Corporate Social Responsibility Policy”. A proviso to this Section states that “if the company fails to spend such amount, the Board shall, in its report specify the reasons for not spending the amount”.

- Further, **Rule 8(1) of the Companies (Corporate Social Responsibility Policy) Rules, 2014**, prescribes that the Board Report of a company under these Rules shall include an Annual Report on CSR, in the prescribed format.

Analysis

- The above provisions of the Act/Rules clearly lay down that the **expenditure on CSR activities is to be disclosed only in the Board’s Report** in accordance with the Rules made thereunder.

- In view of this, **no provision for the amount which is not spent**, (i.e., any shortfall in the amount that was expected to be spent as per the provisions of the Act on CSR activities and the amount actually spent at the end of a reporting period) may be made in the financial statements.
The proviso to section 135 (5) of the Act, makes it clear that if the specified amount is not spent by the company during the year, the Directors’ Report should disclose the reasons for not spending the amount.

However, if a company has already undertaken certain CSR activity for which a liability has been incurred by entering into a contractual obligation, then in accordance with the generally accepted principles of accounting, a provision for the amount representing the extent to which the CSR activity was completed during the year, needs to be recognised in the financial statements.

5.4 Whether the Excess Amount can be Carry Forward to set off against Future CSR Expenditure?

Where a company spends more than that required under law, a question arises as to whether the excess amount ‘spent’ can be carried forward to be adjusted against amounts to be spent on CSR activities in future period.

**Facts**

As per Section 135 (5) of the Companies Act, the Board shall ensure that the company spends, in every financial year, **at least two per cent of the average net profits** of the company made during the three immediately preceding financial years, in pursuance of its Corporate Social Responsibility Policy.

**Analysis**

Since 2% of average net profits of immediately preceding three years is the minimum amount which is required to be spent under section 135 (5) of the Act, the excess amount cannot be carried forward for set off against the CSR expenditure required to be spent in future.

**Conclusion under various Indian GAAP**

1. **Accounting treatment as per AS**

   It has been clarified that the Board is free to decide whether any unspent amount is to be carried forward to the next year, and the same shall be over and above the next year’s CSR allocation equivalent to at least 2% of average net profits of the company. Any shortfall in spending in CSR shall be explained in the directors’ report and the Board of Directors shall state the amount unspent and reasons for not spending that amount. Any shortfall is not required to be provided for in the books of accounts.

2. **Accounting treatment as per Ind AS**

   The query raised to the ITFG was to clarify whether a provision for unspent CSR expenditure is required to be made under Ind AS. The ITFG considered the principles mentioned in
Ind AS 37, Provisions, Contingent Liabilities and Contingent Assets. Under Ind AS 37, a provision would be recognised when all of the following conditions are satisfied:

- An entity has a present obligation (legal or constructive) as a result of a past event
- It is probable that an outflow of resources embodying economic benefits will be required to settle the obligation
- A reliable estimate can be made of the amount of the obligation.
- No provision is required to be made in case the above mentioned conditions are not met.

Considering the requirements of the Companies Act, 2013 (Section 135(5)) and Ind AS 37, the ITFG clarified that the provision for any shortfall in the amount that was expected to be spent on the CSR activities as per the Companies Act, 2013 on CSR activities and the amount actually spent at the end of a reporting period, may not be required in the Ind AS financial statements.

However, if a company has already undertaken certain CSR activity for which an obligation has been created, for example, by entering into a contractual obligation, or either a constructive obligation has arisen during the year, then in accordance with Ind AS 37, a provision for the amount of such CSR obligation, should be recognised in the Ind AS financial statements.

**Illustration 8**

ABC Ltd is a Company which is covered under the ambit of CSR rules. As part of its CSR contribution an amount of INR 15,00,000 was spent as CSR expense towards the education of girl child. The average net profit of the company for the past three years was INR 70,00,000. As the Company incurred a CSR expense in excess of what is required by the rules, it decided to utilise this expense as a carry forward to the next year and reduce next year’s CSR spend by INR 1,00,000.

**Required**

Can the excess expenditure towards CSR be carried forward to next financial year?

**Solution**

There is no provision for carrying forward the excess CSR expenditure spent in a particular year. Any expenditure over 2% could be considered as voluntary higher CSR spend for that year.

**5.5 Supply of Manufactured Goods/ Services by an Entity**

In some cases, a company may supply goods manufactured by it or render services as CSR activities. In such cases, the expenditure incurred should be recognised when the control on the goods manufactured by it is transferred or the allowable services are rendered by the employees.
• The goods manufactured by the company should be valued in accordance with the principles prescribed in Accounting Standard (AS) 2, Valuation of Inventories.

• The services rendered should be measured at cost. Indirect taxes (like excise duty, service tax, VAT or other applicable taxes) on the goods and services so contributed will also form part of the CSR expenditure.

• Where a company receives a grant from others for carrying out CSR activities, the CSR expenditure should be measured net of the grant.

Illustration 9

After the havoc caused by flood in Jammu and Kashmir, a group of companies undertakes during the period from October, 20X1 to December, 20X1 various commercial activities, with considerable concessions/discounts, along the related affected areas. The management intends to highlight the expenditure incurred on such activities as expenditure incurred on activities undertaken to discharge corporate social responsibility, while publishing its financial statements for the year 20X1-20X2.

Required

State whether the management’s intention is correct or not and why?

Solution

Corporate Social Responsibility (CSR) Reporting is an information communiqué with respect to discharge of social responsibilities of corporate entity. Through ‘CSR Report’ the corporate enterprises disclose the manner in which they are discharging their social responsibilities. More specifically, it is addressed to the public or society at large, although it can be squarely used by other user groups also.

Section 135 of the Companies Act, 2013 mandated the companies fulfilling the criteria mentioned in the said section to spend certain amount of their profit on activities as specified in the Schedule VII to the Act. Companies not falling within that criteria can also spend on CSR activities voluntarily. However, besides the requirements of constitution of a CSR committee and a CSR policy, the corporate entities should also take care that expenditure incurred for CSR should not be the expenditure incurred for the activities in the ordinary course of business. If expenditure incurred is for the activities in the ordinary course of business, then it will not be qualified as expenditure incurred on CSR activities.

Here, it is assumed that the commercial activities performed at concessional rates are the activities done in the ordinary course of business of the companies. Therefore, the intention of the management to highlight the expenditure incurred on such commercial activities in its financial statements as the expenditure incurred on activities undertaken to discharge CSR, is not correct.
5.6 Recognition of Income Earned from CSR Projects/ Programmes or During the Course of Conduct of CSR Activities

Facts

Rule 6 (2) of the Companies (Corporate Social Responsibility Policy) Rules, 2014, requires that “the surplus arising out of the CSR projects or programs or activities shall not form part of the business profit of a company”.

Analysis

• The term ‘surplus’ ordinarily means excess of income over expenditure pertaining to an entity or an activity. Thus, in respect of a CSR project or programme or activity, it needs to be determined whether any surplus is arising therefrom.

• A question would arise as to whether such surplus should be recognised in the statement of profit and loss of the company. It may be noted that paragraph 5 of Accounting Standard (AS) 5, Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies, inter alia, requires that all items of income which are recognised in a period should be included in the determination of net profit or loss for the period unless an Accounting Standard requires or permits otherwise. As to whether the surplus from CSR activities can be considered as ‘income’, the Framework for Preparation and Presentation of Financial Statements issued by the Institute of Chartered Accountants of India, defines ‘income’ as “increase in economic benefits during the accounting period in the form of inflows or enhancements of assets or decreases of liabilities that result in increases in equity, other than those relating to contributions from equity participants”.

• Since the surplus arising from CSR activities is not arising from a transaction with the owners, it would be considered as ‘income’ for accounting purposes.

• In view of the aforesaid requirement any surplus arising out of CSR project or programme or activities shall be recognised in the statement of profit and loss and since this surplus cannot be a part of business profits of the company, the same should immediately be recognised as liability for CSR expenditure in the balance sheet and recognised as a charge to the statement of profit and loss.

• Accordingly, such surplus would not form part of the minimum ‘2% of the average net profits of the company made during the three immediately preceding financial years in pursuance of its Corporate Social Responsibility Policy’.
6. CSR EXPENDITURE IN THE INCOME TAX SCENARIO

1. CSR expenditure, being an application of income, is not incurred wholly and exclusively for the purposes of carrying on business. As the application of income is not allowed as deduction for the purposes of computing taxable income of a company, amount spent on CSR cannot be allowed as deduction for computing the taxable income of the company.

2. Based on the Explanatory Memorandum to the Bill, the CSR expenditure which is of the nature described in section 30 to section 36 of the Income-tax Act shall be allowed as deduction under those sections subject to fulfilment of conditions, if any, specified therein. If the nature of CSR expenditure incurred is not covered under the aforesaid sections of the Act and is covered under section 37(1) of the Act, being a general deduction, the same is proposed to be disallowed by the Bill.

Illustration 10

ABC Ltd. carries out CSR activities from rented premises in Pune. The rent paid for such premises is disclosed as CSR expenditure and subsequently ABC Ltd. also claimed deduction of the same under the Income-tax Act. Is this permissible?

Solution

Based on the Explanatory Memorandum to the Bill, CSR expenditure which is of the nature described under the section 30 to 36 of the Income-tax Act shall be allowed as a deduction. Rent expenses can be claimed under section 30 of the Act and hence it can be claimed as a deduction.

7. REPORTING OF CSR: PRESENTATION AND DISCLOSURE IN THE FINANCIAL STATEMENTS

1. Item 5 (A)(k) of the General Instructions for Preparation of Statement of Profit and Loss under Schedule III to the Companies Act, 2013, requires that in case of companies covered under Section 135, the amount of expenditure incurred on ‘Corporate Social Responsibility Activities’ shall be disclosed by way of a note to the statement of profit and loss.

2. From the perspective of better financial reporting and still be in line with the requirements of Schedule III in this regard, it is recommended that all expenditure on CSR activities, that qualify to be recognised as expense in accordance with the relevant provisions as discussed above should be recognised as a separate line item as ‘CSR expenditure’ in the statement of profit and loss.
3. Further, the relevant note should disclose the break-up of various heads of expenses included in the line item ‘CSR expenditure’.

4. The notes to accounts relating to CSR expenditure should also contain the following:
   a) Gross amount required to be spent by the company during the year.
   b) Amount spent during the year on:

<table>
<thead>
<tr>
<th>In cash</th>
<th>Yet to be paid in cash</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>i)</td>
<td>Construction/acquisition of any asset</td>
<td></td>
</tr>
<tr>
<td>ii)</td>
<td>On purposes other than (i) above</td>
<td></td>
</tr>
</tbody>
</table>

   The above disclosure, to the extent relevant, may also be made in the notes to the cash flow statement, where applicable.

c) Details of related party transactions, e.g., contribution to a trust controlled by the company in relation to CSR expenditure as per Accounting Standard (AS) 18, Related Party Disclosures.

d) Where a provision is made in accordance with paragraph 8 above the same should be presented as per the requirements of Schedule III to the Companies Act, 2013. Further, movements in the provision during the year should be shown separately.

5. For the format of Annual report on CSR which is to be included in the Board’s Report, Refer Appendix I

8. CESSATION FROM COMPLIANCE OF CSR

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 (5) of the said section’ till such time it meets the criteria specified in sub-section (1) of section 135.

Analysis

Four year lock-in period for a company fulfilling a CSR criterion in one year It may be noted that once a company has fulfilled the net worth / turnover / net profit criterion for one year it has to fulfil its CSR obligations for the subsequent three financial years, even if it does not fulfil any of
these criteria in those years.

For example, if ABC Ltd. fulfils the turnover criterion under section 135(1) in the financial year 20X1-X2, it would continue to be within the scope of section 135(1) for the three financial years from 20X2-X3 to 20X3-X4, irrespective of fulfilment or otherwise of any criterion in those years. If it has not fulfilled any of the three criteria in the three subsequent financial years, it would be outside the scope of CSR in the financial year 20X5-X6. If in any of the three intermittent years, its average net profit figure is negative, it need not comply with the CSR requirement for that year.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>F.Y. 20X1-X2</th>
<th>F.Y. 20X2-X3</th>
<th>F.Y. 20X3-X4</th>
<th>F.Y. 20X4-X5</th>
<th>F.Y. 20X5-X6</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net Worth / Turnover / Net Profit Criterion</td>
<td>✓</td>
<td>×</td>
<td>×</td>
<td>×</td>
<td>×</td>
</tr>
<tr>
<td>Situation I</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Average Net Profits</td>
<td>Positive</td>
<td>Positive</td>
<td>Positive</td>
<td>Positive</td>
<td>Positive</td>
</tr>
<tr>
<td>CSR Obligation</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>×</td>
</tr>
<tr>
<td>Situation II</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Average Net Profits</td>
<td>Positive</td>
<td>Positive</td>
<td>Positive</td>
<td>Negative</td>
<td>Positive</td>
</tr>
<tr>
<td>CSR Obligation</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>×</td>
<td>×</td>
</tr>
</tbody>
</table>
TEST YOUR KNOWLEDGE

Questions

1. A property is being constructed to operate CSR activities by a company. At the balance sheet date, the cost of construction is treated as revenue expenditure. Are there any additional disclosures required in the financials regarding this?

2. In the year 20X1, XYZ Ltd. falls within the purview of CSR provisions as per the Companies Act, 2013 since its net profit for the financial year exceeded ₹ 5 crore. The company discharged CSR obligations in the year 20X2. However, the net profit of the year 20X2 was less than ₹ 5 crores. Also, it was also not satisfying the other two criteria of the section 135 for CSR compliance. Therefore, the company stopped performing CSR activities from the year 20X3 onwards. Comment on the company’s accountability for CSR.

Answers

1. Item 5 (a) of the General Instructions for Preparation of Statement of Profit and Loss under Schedule III to the Companies Act, 2013, requires that in case of companies covered under Section 135, the amount of expenditure incurred on ‘Corporate Social Responsibility Activities’ shall be disclosed by way of a note to the statement of profit and loss. The note should also disclose the details with regard to the expenditure incurred in construction of a capital asset under a CSR project.

2. Once a company has fulfilled the net worth / turnover / net profit criterion for one year it has to fulfil its CSR obligations for the subsequent three financial years, even if it does not fulfil any of these criteria in those years.

In the given case XYZ Ltd. falls in the ambit of CSR obligations by fulfilling the criteria of net profit exceeding ₹ 5 crores in the year 20X1. So it has to discharge its CSR obligations by spending two percent of its average profit every year starting from 20X2 till 20X4. It cannot stop spending on CSR activities as per the Act after 20X2.
Appendix I

FORMAT FOR THE ANNUAL REPORT ON CSR ACTIVITIES TO BE INCLUDED IN THE BOARD’S REPORT

1. A brief outline of the company’s CSR policy, including overview of projects or programs proposed to be undertaken and a reference to the web-link to the CSR policy and projects or programs.

2. The Composition of the CSR Committee.

3. Average net profit of the company for last three financial years.

4. Prescribed CSR Expenditure (two per cent. Of the amount as in item 3 above)

5. Details of CSR spent during the financial year.
   (a) Total amount to be spent for the financial year;
   (b) Amount unspent, if any;
   (c) Manner in which the amount spent during the financial year is detailed below.

<table>
<thead>
<tr>
<th>(1)</th>
<th>(2)</th>
<th>(3)</th>
<th>(4)</th>
<th>(5)</th>
<th>(6)</th>
<th>(7)</th>
<th>(8)</th>
</tr>
</thead>
<tbody>
<tr>
<td>S. No.</td>
<td>CSR Project or activity identified</td>
<td>Sector in which the Project is covered</td>
<td>Projects or programs (1) Local area or other (2) Specify the State and district where projects or programs was undertaken</td>
<td>Amount outlay (budget) project or programs wise</td>
<td>Sub-heads: (1) Direct expenditure on projects or programs. 2. Overheads:</td>
<td>Cumulative expenditure upto the reporting period</td>
<td>Amount spent: Direct or through implementing agency</td>
</tr>
<tr>
<td>1</td>
<td></td>
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<td>TOTAL</td>
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</tbody>
</table>
Give details of implementing agency:

6. In case the company has failed to spend the two per cent of the average net profit of the last three financial years or any part thereof, the company shall provide the reasons for not spending the amount in its Board report.

7. A responsibility statement of the CSR Committee that the implementation and monitoring of CSR Policy, is in compliance with CSR objectives and Policy of the company.

<table>
<thead>
<tr>
<th>Sd/-</th>
<th>Sd/-</th>
<th>Sd/-</th>
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<tbody>
<tr>
<td>(Chief Executive Officer or Managing Director or Director)</td>
<td>(Chairman CSR Committee)</td>
<td>(Person specified under clause (d) of sub-section (1) of section 380 of the Act)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(wherever applicable)</td>
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</tbody>
</table>
## ANNEXURE REFERRED TO AT PARA (i) OF GENERAL CIRCULAR NO. 21/2014 DATED 18.06.2014

<table>
<thead>
<tr>
<th>Sl. No.</th>
<th>Additional items requested to be included in Schedule VII or to be clarified as already being covered under Schedule VII of the Act</th>
<th>Whether covered under Schedule VII of the Act</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Promotion of Road Safety through CSR: (i) (a) Promotions of Education, &quot;Educating the Masses and Promotion of Road Safety awareness in all facets of road usage. (b) Drivers' training. (c) Training to enforcement personnel. (d) Safety traffic engineering and awareness through print, audio and visual media&quot; should be included. (ii) Social Business Projects: &quot;giving medical and Legal aid, treatment to road accident victims&quot; should be included.</td>
<td>(a) Schedule VII (ii) under &quot;promoting education&quot;. (b) For drivers training etc. Schedule VII (ii) under &quot;vocational skills&quot;. (c) It is establishment functions of Government (cannot be covered). (d) Schedule VII (ii) under &quot;promoting education&quot;. (ii) Schedule VII (i) under 'promoting health care including preventive health care.'</td>
</tr>
<tr>
<td>2.</td>
<td>Provisions for aids and appliances to the differently-able persons. 'Request for inclusion'</td>
<td>Schedule VII (i) under 'promoting health care including preventive health care.'</td>
</tr>
<tr>
<td>3.</td>
<td>The company contemplates of setting up ARTIC (Applied Research Training and Innovation Centre) at Nasik. Centre will cover the following aspects as CSR initiatives for the benefit of the predominately rural farming</td>
<td>Item no. (ii) of Schedule VII under the head of &quot;promoting education&quot; and &quot;vocational skills&quot; and &quot;rural development&quot;. (a) &quot;Vocational skill&quot; livelihood enhancement projects.</td>
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<tr>
<td>Community:</td>
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<td></td>
<td></td>
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<tr>
<td>(a) Capacity building for farmers covering best sustainable farm management practices.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(b) Training Agriculture Labour on skill development.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(c) Doing our own research on the field for individual crops to find out the most cost optimum and Agri-ecological sustainable farm practices. (Applied research) with a focus on water management.</td>
<td></td>
<td></td>
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<tr>
<td>(d) To do Product Life Cycle analysis from the soil conservation point of view.</td>
<td></td>
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<tbody>
<tr>
<td>(b) &quot;Vocational skill&quot;</td>
</tr>
<tr>
<td>(c) 'Ecological balance', 'maintaining quality of soil, air and water'.</td>
</tr>
<tr>
<td>(d) &quot;Conservation of natural resource&quot; and 'maintaining quality of soil, air and water'.</td>
</tr>
</tbody>
</table>

4. **To make "Consumer Protection Services" eligible under CSR.** (Reference received by Dr. V.G. Patel, Chairman of Consumer Education and Research Centre).

   (i) Providing effective consumer grievance redressal mechanism.
   (ii) Protecting consumer's health and safety, sustainable consumption, consumer service, support and complaint resolution.
   (iii) Consumer protection activities.
   (iv) Consumer Rights to be mandated.
   (v) all consumer protection programs and activities" on the same lines as Rural Development, Education etc.

Consumer education and awareness can be covered under Schedule VII (ii) "promoting education".
<p>| | | |</p>
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<tbody>
<tr>
<td>5.</td>
<td>(a) Donations to IIM [A] for conservation of buildings and renovation of classrooms would qualify as &quot;promoting education&quot; and hence eligible for compliance of companies with Corporate Social Responsibility.</td>
<td>Conservation and renovation of school buildings and classrooms relates to CSR activities under Schedule VII as &quot;promoting education&quot;.</td>
</tr>
<tr>
<td></td>
<td>(b) Donations to IIMA for conservation of buildings and renovation of classrooms would qualify as &quot;protection of national heritage, art and culture, including restoration of buildings and sites of historical importance&quot; and hence eligible for compliance of companies with CSR.</td>
<td></td>
</tr>
<tr>
<td>6.</td>
<td>Non Academic Technopark TBI not located within an academic Institution but approved and supported by Department of Science and Technology.</td>
<td>Schedule VII (ii) under &quot;promoting education&quot;, if approved by Department of Science and Technology.</td>
</tr>
<tr>
<td>7.</td>
<td>Disaster Relief</td>
<td>Disaster relief can cover wide range of activities that can be appropriately shown under various items listed in Schedule VII. For example,</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(i) medical aid can be covered under 'promoting health care including preventive health care.'</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(ii) food supply can be covered under eradicating hunger, poverty and malnutrition.</td>
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</tbody>
</table>
|   |   | (iii) supply of clean water can be covered under 'sanitation and
<table>
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<tr>
<th></th>
<th>making available safe drinking water.</th>
</tr>
</thead>
<tbody>
<tr>
<td>8.</td>
<td>Trauma care around highways in case of road accidents.</td>
</tr>
<tr>
<td>9.</td>
<td>Clarity on &quot;rural development projects&quot;</td>
</tr>
<tr>
<td>10.</td>
<td>Supplementing of Govt. schemes like mid-day meal by corporates through additional nutrition would qualify under Schedule VII.</td>
</tr>
<tr>
<td>11.</td>
<td>Research and Studies in the areas specified in Schedule VII.</td>
</tr>
<tr>
<td>12.</td>
<td>Capacity building of government officials and elected representatives - both in the area of PPPs and urban infrastructure.</td>
</tr>
<tr>
<td>13.</td>
<td>Sustainable urban development and urban public transport systems</td>
</tr>
<tr>
<td>14.</td>
<td>Enabling access to, or improving the delivery of, public health systems be considered under the head &quot;preventive healthcare&quot; or &quot;measures for reducing inequalities faced by socially &amp; economically backward groups&quot;?</td>
</tr>
<tr>
<td>15.</td>
<td>Likewise, could slum redevelopment or EWS housing be covered under “measures for reducing inequalities faced by socially &amp; economically backward groups”?</td>
</tr>
<tr>
<td></td>
<td>Renewable energy projects</td>
</tr>
<tr>
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</tr>
<tr>
<td>16.</td>
<td>(i) Are the initiatives mentioned in Schedule VII exhaustive?</td>
</tr>
<tr>
<td></td>
<td>(ii) In case a company wants to undertake initiatives for the beneficiaries mentioned in Schedule VII, but the activity is not included in Schedule VII, then will it count (as per 2(c)(ii) of the Final Rules, they will count)?</td>
</tr>
<tr>
<td>17.</td>
<td>(i) &amp; (ii) Schedule VII is to be liberally interpreted so as to capture the essence of subjects enumerated in the schedule.</td>
</tr>
<tr>
<td>18.</td>
<td>US-India Physicians Exchange Program-broadly speaking, this would be program that provides for the professional exchange of physicians between India and the United States.</td>
</tr>
</tbody>
</table>