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Govt's decision to tighten CSR spending rules makes sense: Here is why

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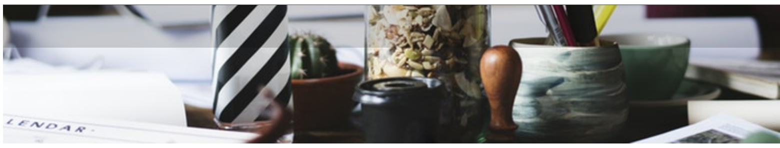
- While the total expenditure on CSR activities is on rise, spending as a percentage of the net profit is showing a consistent downward trend.



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Share

The Companies (Amendment) Act 2019 (Amendment Act) received presidential assent on July 31, 2019. The key change implemented in the amendment act is that the corporate social responsibility (CSR) spends are now mandatory in the case of eligible companies. Not meeting the CSR requirements hitherto only warranted a disclosure in the directors' report. However, it will now carry penal consequences including imprisonment of officials in certain instances.

Amendments

Pursuant to the amended Section 135 of the Companies Act 2013 (Companies Act), if there are any unspent CSR funds during a financial year (in respect of an ongoing CSR project), in accordance with its CSR policy, the company must transfer such unspent CSR funds into a special account within a period of 30 days from the end of financial year. Such account, to be opened with a scheduled bank by the company, will b called an Unspent Corporate Social Responsibility Account (Unspent CSR Account) and the proceeds of the Unspent CSR Account will have to be spent by the company towards the CSF projects (under its CSR policy) within three financial years from the date of such transfer. If the company is unable to spend the sum in the Unspent CSR Account within the prescribed period three financial years, then, such unsp

amount should be transferred to a fund specified under Schedule VII of the Companies Act (Schedule VII Fund)[1 within six months from the end of the relevant financial year.

However, if there are any unspent CSR funds at the end of a financial year and there are no ongoing CSR projects, the funds should be directly transferred to the Schedule VII Fund, within six months from the end of the relevant financial year.

If a company fails to comply with above mentioned obligations, the Amendment Act provides for imposition of penalty of not be less than Rs 50,000, which may extend to Rs 2.5 million. Additionally, the Amendment Act also provides for imprisonment of every officer of the company who is in default for up to three years and a fine of not be less than Rs 50,000 but which may extend up to Rs 500,000 or with both. Additionally, separate penalty for continuing offences has also been prescribed.

Under the Amendment Act, the central government has been empowered to make rules and issue directions to ensure compliance.

What statistics say

As making CSR (non-) spending subject to penal consequences has received industry criticism, it may be worthwhile to look at some statistics.

Out of 1,913 companies who met the eligibility criteria prescribed under the Companies Act, 667 were unable to spend for a variety of reasons. Even though the CSR expenditure amounts by listed companies has been growing, about 35 percent of the companies who met the eligibility criteria for CSR prescribed under the Companies Act, did not spend on CSR activities.

While the total expenditure on CSR activities is on rise, total expenditure on CSR activities as a percentage of the net profit is showing a consistent downward trend. The CSR spends as a percentage to net profit has come down from 2.28 percent in FY 16 to 2.05 percent in FY 17 to 2.00 percent in FY 18.[2] Moreover, a meagre 0.11 percent of the active companies spend on CSR activities.

The government's case for introduction of the Amendment Act is that this has been done to bring in more effectiveness to the CSR regime.

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[1]*Schedule VII Fund means, 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 / tribes, other backword classes, minorities and women.*

[2] *CRISIL CSR Yearbook 2019.*