

Notification of provisions relating to corporate social responsibility under the Companies Act, 2013

28 February 2014



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Immediately

**Within the next
3 months**

Post 3 months but
within 6 months

Post 6 months

Introduction

The Ministry of Corporate Affairs (MCA) has vide its notification dated 27 February 2014, and in exercise of powers conferred by section 1(3) of the Companies Act, 2013 ('the Act'), notified 1 April 2014 as the date on which the provisions of section 135 and Schedule VII of the Act shall come into force.

Section 135 covers the following:

Applicability

It covers all companies in India meeting any one or more of the following conditions:

- Turnover of INR 1,000 crores or more
- Networth of INR 500 crores or more
- Net Profit of INR 5 crores or more

The corporate social responsibility (CSR) contribution would have to be at least two per cent of the average net profit, made during the three immediately preceding financial years.

Administration and reporting

- The Board would appoint a three member CSR committee including one Independent Director.
- The CSR committee would be responsible to formulate CSR policy, recommend CSR initiatives and monitor CSR expenditure.
- The Board would be required to mandatorily report on CSR in the Board's report. In case of failure to spend the prescribed amount, reasons would have to be disclosed in the Board's report.

Implementation

- CSR committee is to develop CSR policy which shall indicate the activities to be undertaken by the company as specified in Schedule VII.
- The company shall give preference to the local area and areas around it where it operates for spending.

Companies (Corporate Social responsibility Policy) Rules, 2014

The MCA has also notified the Companies (Corporate Social Responsibility Policy) Rules, 2014 ('the Rules') to be effective from 1 April 2014.

The Rules have just released and as these are evaluated in detail, further areas requiring clarity may emerge. The salient features of the Rules are as follows:

Net profit to exclude dividends from other Indian companies and profits generated outside India

Net profit means net profit as per the financial statements of the Company and excludes profits generated outside India through overseas branches or subsidiaries and any dividend received from other companies in India that are complying with the CSR provisions. This could provide relief to companies by avoiding any cascading effect of CSR spending on up-streaming of dividends.

A private company or an unlisted public company exempted from the requirement of having independent directors for CSR committee

A private company or unlisted public company, which are otherwise not required to have an independent director, is exempted from the requirement of having an independent director on their CSR committee. This is a constructive development, and provides relief to a number of private companies who would have had to get independent directors on their boards. This may also ease the demand for independent directors at a time when there already may be a demand-supply mis-match for high quality independent directors.

CSR expenditure to be in line with the amended Schedule VII of the Companies Act 2013

CSR to include activities undertaken by the Board pursuant to policy developed by the Company, as long as the policy covers areas included in Schedule VII. This seems to indicate that the Board policy can cover other areas as well. However, it is also clarified that expenditure on any item not in conformity with Schedule VII will not be considered as eligible CSR expenditure. Therefore, companies will have to draw up the policy and action plan to ensure that they spend the required 2 per cent amount on the activities included in Schedule VII.

CSR expenditure to exclude those incurred in the normal course of business

CSR expenditure would also exclude those on activities undertaken in the normal course of business of a company. Companies would need to clearly distinguish those activities which are undertaken in the normal course of business and those that are done incrementally as part of the CSR initiatives.

Foreign companies covered under CSR provisions

Foreign companies to contribute to CSR based on the profits of their Indian business operations.

Indian branches and project offices of foreign companies covered under CSR provisions

Indian branches and project offices of foreign companies are covered under CSR provisions. This will also require such foreign companies to set up a CSR committee, CSR policy etc. to comply with these requirements.

Three years of non-applicability required to exit CSR compliance requirements

Once covered under CSR provisions, companies will need to have 3 consecutive years, where the provisions do not apply to them, before they can stop complying with the requirements relating to

CSR.

Group CSR projects or joint CSR projects permitted

Companies belonging to the same group can set up a registered trust or a registered society or a company established under section 8 of the Act, to undertake CSR activities. Companies can also join hands with other companies to undertake CSR projects jointly, in such a manner that such companies can report separately on such projects. This is a positive development as it would allow groups and companies operating in an area to come together and undertake projects of a larger scale.

CSR expenditure on projects or activities in India only

Only expenditure incurred on projects or activities in India to qualify as CSR expenditure.

Capacity building costs of own personnel or those of implementation agencies to qualify as CSR expenditure; capped at 5% of total CSR expenditure

Companies may build CSR capacity through their own personnel or through their implementation agencies. However, the total expenditure should not exceed 5% of the total CSR expenditure in that year.

Political contribution excluded from CSR expenditure

Contribution, directly or indirectly, to any political party shall not be considered as CSR expenditure.

Surplus from CSR activities not business profits of company

The CSR policy shall specify that the surplus arising from CSR activities are not to be considered as business profits of the company. Such surplus may therefore need to be ploughed back into CSR activities.

CSR policy and activities to be displayed on website

Companies will be required to display the CSR policy and projects undertaken and amount spent in the Board Report and on the Company's website.

Schedule VII of the Act

The comparison of the Schedule VII, as enacted, and the Schedule VII, as amended, is as shown in the table below. Essentially, some of the activities permitted as per the earlier schedule have been elaborated and widened in scope, a few activities have been added and some have been deleted.

Sr. No.	Schedule VII as enacted	Schedule VII as amended
1	Eradicating extreme hunger and poverty	Eradicating hunger and poverty and malnutrition, promoting preventive healthcare and sanitation and making available safe drinking water.
2	Promotion of education	Promoting education; including special education and employment enhancing vocation skills especially among children, woman, elderly and the differently abled and livelihood enhancement projects.
3	Promoting gender equality and empowering women	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	Reducing child mortality and improving maternal health	Deleted
5	Combating human immunodeficiency virus, acquired immune deficiency syndrome, malaria and other diseases	Deleted
6	Ensuring environmental sustainability	Ensuring environmental sustainability, ecological balance, protection of flora and fauna, animal welfare, agroforestry, conservation of natural resources and maintaining of quality of soil, air and water
7	Employment enhancing vocational skills	Integrated with Sr. No. 2 above
8	Social business projects	Deleted
9	Contribution to the Prime Minister's National Relief Fund or any other fund set up by the Central Government or the State Governments for socio-economic development and relief and funds for the welfare of the Scheduled Castes, the Scheduled Tribes, other backward classes, minorities and women	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.
10	Such other matters as may be prescribed	<p>Following new activities are added in the amended Schedule VII:</p> <ul style="list-style-type: none"> • Protection of national heritage, art and culture including restoration of buildings and sites of historical importance and works of art; setting up of public libraries; 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 recognised sports, and Paralympics sports and Olympic sports. • Contributions or funds provided to technology incubators located within academic institutions which are approved by the Central Government. • Rural development projects.

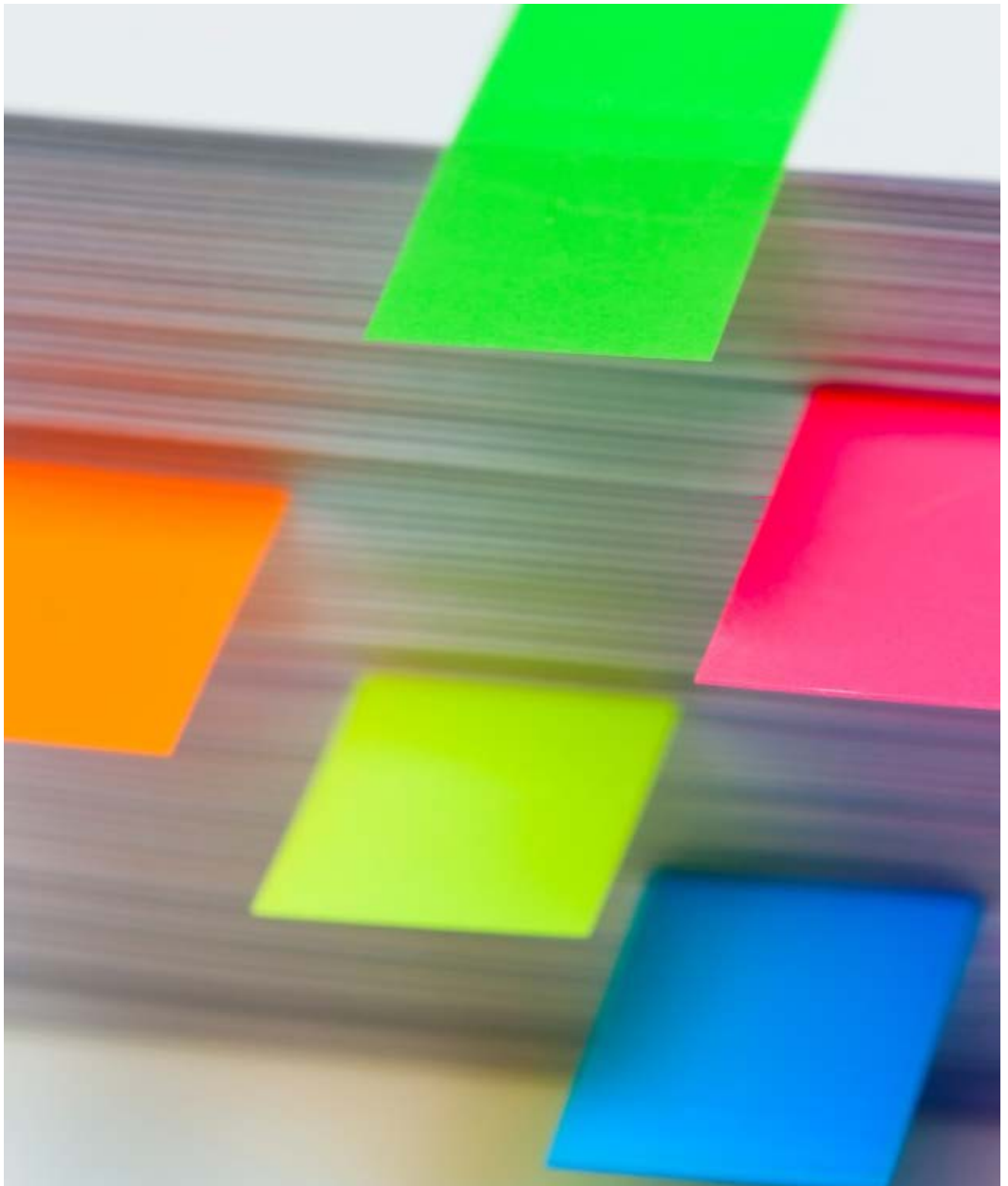
Our comments

The release of the Companies (Corporate Social Responsibility Policy) Rules, 2014, is a welcome development which aims to provide clarifications that were needed and signals the strong intent of the Ministry of Corporate Affairs to make the Companies Act, 2013, fully operational at the earliest.

This is the first set of rules that have been released by the MCA after the consultation on the draft rules late last year. It is also heartening to note that several of the representations made by the industry have been taken into account, as the MCA has finalised these rules and made amendments to Schedule VII of the Companies Act, 2013.

The bottom line

- Companies should aim to assess the changes made in the Rules and move to implement their corporate social responsibilities under the Companies Act, 2013, swiftly.



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