

CSR : ACCOUNTING & TAXATION

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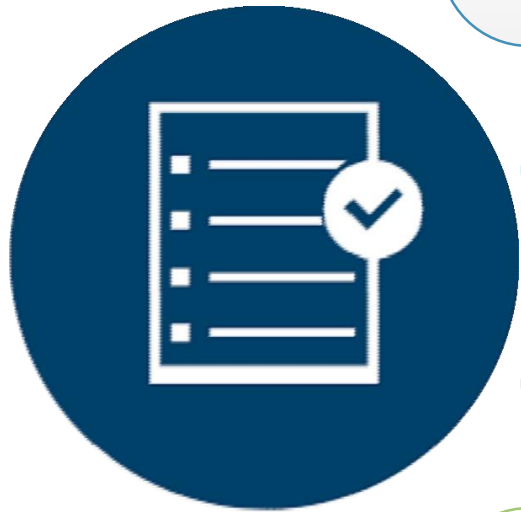
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Our Organization's Credo:

Focus on capabilities; opportunities follow



Agenda



CSR – Summary of Provisions

CSR Accounting

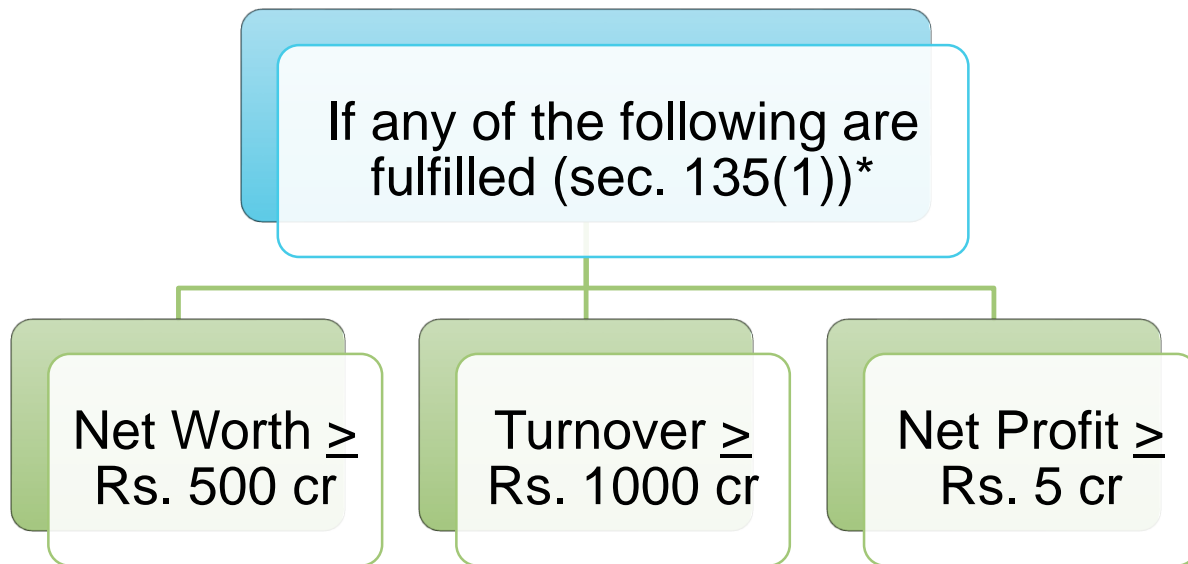
Taxation aspects of CSR

CSR Disclosures



SUMMARY OF PROVISIONS – CA, 2013

Applicability



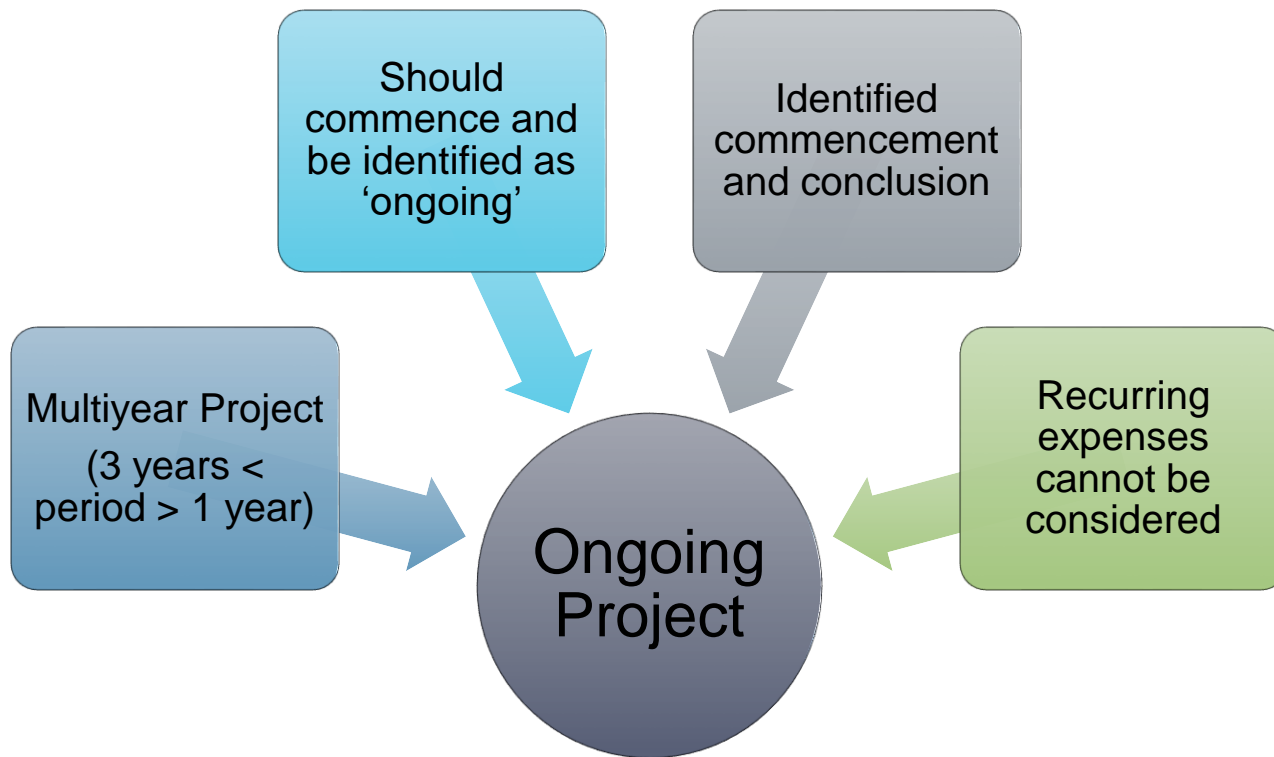
*during the immediately preceding financial year

- If any of the given criteria are met, the Company shall –
 - Constitute a CSR Committee;
 - Approve a CSR Policy;
 - Spend, in every FY, **at least 2% of the avg. net profits made during 3 immediately preceding FY**
- Where amount to be spent \leq Rs. 50 lakhs, no CSR Committee required (Sec. 135 (9))
- If Company does not meet any criteria set out in 135 (1) **for 3 consecutive FYs**, the Co. shall not be required to –
 - Constitute a CSR Committee;
 - Comply with provisions set out in sec. 135 (2) to (6)

Spending mandate and consequences of not spending

- Second proviso to sec. 135 (5), read with sec. 135 (6), elaborates the mandatory spending requirement
- Second proviso to sec. 135 (5):
 - If the company fails to spend the CSR target:
 - The board shall still explain the reasons for the same; and
 - Analyse the “unspent” amount:
 - If and to the extent it pertains to “ongoing project” – retain the money in a separate bank account [unspent CSR account] – **within 30 days of the end of FY**
 - Or else, transfer unspent money or money not retained for ongoing project to National Unspent Fund, within 6 months of the end of the financial year
- While the time for transferring the money to Unspent Fund is 6 months, but companies will have to take a board decision on retention, disclose reasons for not spending etc.
 - Hence, the analysis of what may actually be retained by the Company will have to be done before approval of board report

Analysis of Unspent amount and Ongoing Projects (1/2)



- To regard it as an “ongoing project”, is it necessary that some spending must have been during the financial year?
- If there is a binding commitment on the part of the company during the financial year, the fact that nothing has been spent during the year should not preclude it from “ongoing” status
- The idea of retention of money is for something which would need to be spent based on committed funds
- The essence of the retention is - Rolling the expense to the next year, and claim it to be expense of this year.

Analysis of Unspent amount and Ongoing Projects (2/2)

■ So, what is the Company expected to do end-of-year:

- The CSR Target is based on average of 3 preceding years – hence, that is unimpacted by the current year's accounts
- However, aggregation of all that is spent (Spending) during the FY needs to be done
- $\text{Total Shortfall} = \text{Target} - \text{Spending}$
- Identification of “Ongoing Projects”
- Identification of further outlay required for Ongoing Projects upto the expected completion date (Ongoing Project Outlay)
- $\text{Transferable Shortfall} = \text{Total Shortfall} - \text{Ongoing Project Outlay}$
- Transfer Transferable Shortfall within 6 months of EoY

■ Whose responsibility is it to identify Ongoing Project and Ongoing Project Outlay?

- Going by Rule 4 (6), the identification of Ongoing Project, Ongoing Project implementation schedule, as well as Ongoing Project Outlay are board responsibilities
- Non-compliance of sec. 135 (5) and (6) attract the penal provisions of sec. 135 (7)

■ What happens to money retained for Ongoing Projects, but not spent there?

- Transfer to Unspent Fund within 30 days from the end of third financial year
- Assuming that the implementation schedule stretches only to the next financial year, can the Company still retain unspent funds for 3 years?
 - Does not seem logical

Characteristics of Unspent money on Ongoing Projects

- It must be a “project”, and not merely a spending
- The project should have been a part of the CSR plan for FY 20-21
 - The idea of unspent money on ongoing project is that there was something which was expected to be completed in the financial year, but could not be completed
- The project should have been commenced, and it not yet completed
- If a project was originally a multi-year project, and the cash outlay was originally scheduled to be spent in subsequent years, can it be called unspent money for FY 20-21?
 - Does not seem logical
- Does the project have to be completed within 3 years?
 - The idea is not to rule out long-term projects. Several developmental projects may, by definition, be long-term projects
 - The idea is to limit the dragging of unspent money to a time-bound frame

Leading Unspent Funds for Ongoing Projects

- Unspent Funds that go to National Unspent CSR Fund go irretrievably
- Hence, there may be a strong motivation on the part of companies to retain the Funds for Ongoing Projects
 - Timely identification of Ongoing Projects
 - Do Ongoing Projects have to be part of a pre-approved CSR “Action Plan”?
 - In reality, in most companies, it is not possible to identify all CSR projects at the start of the year. Spending opportunities keep arising through the year and the CSR Committee continues to approve the same
- Presumably, a Company may retain Unspent Funds, within 3 years of retention
- However, given the penal implications of sec. 135 (7), it should not be a good idea to have an ambitious retention plan
- Board disclosures in case of retention:
 - If funds have been retained for Ongoing Projects, is that itself an explanation for Unspent Funds?
 - Target Spending pertains to the financial year, and therefore, should have been expected to be spent during the year
 - Not spending during the year, and spilling over for Ongoing Project, itself should require explanation
- Comprehensive disclosure requirements for Ongoing Projects

Scope of CSR Expenditure, and exclusions

- Definition of CSR in Rule 2 (1) (d) seeks to exclude several items from CSR spending
- Earlier definition defined what CSR includes, viz., by reference to Schedule VII, but revised definition has a list of exclusions.
- Further, the expression “statutory obligation” is notable
- 6 exclusions specified in Rules
- However, in any case, Schedule VII still remains the list of activities/subjects
- Contribution to corpus will not be considered to be CSR expenditure
 - The erstwhile Rule 7 allowed contribution to the corpus of implementing agencies to be included in the CSR expenditure.

Exclusions



Carry backward of CSR shortfall

- Concept of carry backward:
 - Shortfall of CSR spending in any year can be adjusted against excess spending in any previous year
- 3rd proviso to sec 135 (5) provides
 - if the company spends an amount in excess of the requirements provided under this sub-section, such company may set off such excess amount against the requirement to spend under this sub-section for such number of succeeding financial years and in such manner, as may be prescribed
- Rule 7 (3) provides for a time frame of 3 immediately succeeding years for adjusting that excess spending
 - The set off need not be spaced out – it may be in any of the 3 years
- However, puts conditions:
 - The excess shall not include surplus arising from CSR activities
 - The Board shall pass a resolution to this effect
- Board resolution to what effect? And in which year?
 - In author's view, excess spending in any year is a matter of fact – that is not something that requires a decision
 - However, the decision to adjust the surplus is a decision, and that should require a board resolution

Implementing agencies

- Rule 4 provides of carrying of CSR activities either by the company itself, or through the specified implementing agencies
- CSR activities have 2 ends:
 - The Company as the principal
 - The end beneficiary(ies) as the destination
- Implementing agencies are the intermediaries, typically carrying the following functions:
 - Aggregation of spending by several group companies
 - Identification of CSR opportunities
 - Coordination with the end beneficiaries
 - Monitoring of CSR implementation
- Implementing agencies essentially save the company from the drudgery and let the company focus on strategizing, deciding and spending
- Three modes of implementation
 - Self implementation
 - Joint implementation with one or more companies [Rule 4 (4)]
 - Implementation through agencies
- 4 types of agencies – Rule 4 (1)
 - Captives – sec 8 company, public trust, society
 - Govt agencies – sec 8 company, trust or society
 - Statutory bodies – entity under Act of Parliament or state legislature
 - Public agencies – sec 8 company, public trust or society
- These implementing agencies will need 2 registrations
 - MCA registration – in all cases
 - Income-tax registration – in case of 1, and 4
- Trusts have to be registered with Registrar of Assurances

Impact assessment

- Rule 8 (3) brings in the requirement of impact assessment
 - If the CSR target of the company, in each of the 3 preceding financial years, is Rs 10 crores or more
 - The activity or the project has an outlay of Rs 1 crore or more
 - Since the requirement applies immediately, the CSR target for FY 2017-18, 18-19 and 19-20 will be relevant, to see the impact assessment requirement for FY 20-21
- Impact assessment to be carried by an independent agency
- Several questions remain unanswered
 - Who is the independent impact assessment agency?
 - What exactly will be the scope and the format of the impact assessment
 - By what time is the impact assessment to be done?
 - To whom is the impact assessment report addressed?
 - This has to be placed before the Board [Rule 8(3)(b)]
 - This has to form part of CSR Annual Report



CSR ACCOUNTING

Key Terms

Net Profit		
Particulars	Amt (Rs.)	Amt (Rs.)
Net Profit as per S. 198		xx
Less:		
a. any profit arising from any overseas branch or branches of the company, whether operated as a separate company or otherwise	xx	
b. any dividend received from other companies in India, which are covered under and complying with the provisions of section 135 of the Act	xx	
Net Profit for ascertaining CSR obligation		XX

Net Worth	
Includes	Excludes
<ul style="list-style-type: none"> ▪ Paid-up share capital ▪ All reserves created out of the profits ▪ Securities Premium A/c ▪ P/L Balance (Dr/ Cr) after deducting the aggregate value of the accumulated losses ▪ Deferred Expenditure and Miscellaneous Expenditure not written off 	<ul style="list-style-type: none"> ▪ Reserves created out of revaluation of assets ▪ write-back of depreciation and amalgamation;

Note that for companies falling under specific statute (ex: IRDAI), profits shall be computed as per the respective law unless otherwise mentioned.

Liabilities - Ind AS *vis-à-vis* IGAAP

Meaning of 'Liability'	
Ind AS (37)	Indian GAAP
A liability is a <ul style="list-style-type: none">▪ present obligation of the entity▪ arising from past events,▪ the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits	Defines liability as – <ul style="list-style-type: none">▪ A present obligation▪ As a result of past obligations▪ Considered probably and can be reliably estimated

- **Principal features of a liability –**
 - **Present obligation** - must be payable in the same FY
 - **Arising from past events** – based on previous transactions/ business done in the same FY or previous FYs
 - **Identified liability** – the sum payable shall be ascertained with reasonable certainty
 - **Identified payee** – the person/ entity to whom such payment is to be made must be identified
 - **Outflow of resources** – the payment of a liability must lead to an actual outflow of resources

Provisions & Contingent Liability - Ind AS *vis-à-vis* IGAAP

Meaning of 'Provision'	
Ind AS (37)	Indian GAAP
<p>A provision is a liability of</p> <ul style="list-style-type: none"> ▪ uncertain timing; or ▪ uncertain amount 	<p>A provision is a liability which can be measured only by using a substantial degree of estimation.</p>

Meaning of 'Contingent Liability'	
Ind AS (37)	Indian GAAP
<p>Means –</p> <ul style="list-style-type: none"> ▪ a possible obligation ▪ that arises from past events and ▪ whose existence is subject to happening of an event (certain or uncertain) <p>or</p> <ul style="list-style-type: none"> ▪ a present obligation ▪ that arises from past events but is not recognised because: <ul style="list-style-type: none"> ▪ it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation; or ▪ the amount of the obligation cannot be measured reliably 	<p>Means –</p> <ul style="list-style-type: none"> ▪ a possible obligation ▪ that arises from past events and ▪ whose existence is subject to happening of an event (certain or uncertain) <p>or</p> <ul style="list-style-type: none"> ▪ a present obligation ▪ that arises from past events but is not recognised because: <ul style="list-style-type: none"> ▪ it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation; or ▪ the amount of the obligation cannot be measured reliably

Recognition and Measurement of Unspent CSR

- As per section 135 (5), where amount = 2% of the Avg. Profit of last 3 FYs is not spent –
 - The Board shall in its Report explain reasons for not spending such amount; and
 - Except in case of an 'On going Project' - **Transfer the unspent amount to a specified Fund within 6 months of the end of FY**
- **Is this Transferrable Amount**
 - A liability;
 - A provision; or
 - A contingent liability?

Unspent CSR – Liability or Provision or Contingent Liability

Recognition as	Features of CSR	Y/N
Liability	<ul style="list-style-type: none">▪ Identified amount exists;▪ Obligation created by the law▪ Is payable to an identified person/ entity;▪ Within a definite time period	Yes
Provision	<ul style="list-style-type: none">▪ Identified amount exists;▪ Obligation created by the law;▪ Within a definite time period – exact timing may not be sure▪ Is payable to an identified person/ entity	Yes
Contingent Liability	Amount of CSR Payable is always certain + Not subject to happening of any event	No

- Hence, Unspent CSR can **never** be recognised as a contingent liability – either under Ind AS or I-GAAP
 - There is no contingency. Amount of CSR payable is calculated from past profits – hence, there is no uncertainty
- The definition is inclined towards “liability”. In such case, it will be straight expensed out
- However, if it is treated as a provision, the actual payment, whenever done will be settled with the provision.

Accounting for Unspent CSR – Other than Ongoing Project (1/2)

- The amount spent on CSR – Expenditure under P/L
- If any amount remains unspent – create a liability to transfer the unspent amount to the Fund
 - Within 6 months from end of FY

■ Illustration

Particular	Details
Amount to be spent on CSR Activities	Rs. 2 crores
Nature of the Project	Other than ongoing project
Amount actually spent during F.Y. 2020-21	Rs. 1.75 crores
Unspent Amount	Rs. 0.25 crores

- In the given Illustration

- Unspent Amount of Rs. 2 crores should be transferred to the National Unspent CSR Fund, or any other Fund as prescribed in Sch. VII

■ Accounting Treatment –

The unspent amount shall be treated as

- “**liability**” if the Fund in which the unspent amount shall be transferred is **identified**
- “**provision**” if the Fund is not identified

Accounting for Unspent CSR – Other than Ongoing Project (2/2)

Recognized as Liability

- i. Identification of Liability**
- | | | <u>Amount (in Cr.)</u> |
|---------------------|----|------------------------|
| CSR for 2020-21 A/c | Dr | 0.25 / |
| To PM Cares Fund | | 0.25 |
- ii. Paid to PM Cares Fund**
- | | | |
|---------------|----|--------|
| PM Cares Fund | Dr | 0.25 / |
| To Bank | | 0.25 |

Recognized as Provision

- i. Provisioning**
- | | | <u>Amount (in Rs.)</u> |
|----------------------------------|----|------------------------|
| CSR for 2020-21 A/c | Dr | 0.25 / |
| To Provision for CSR for 2020-21 | | 0.25 |
- ii. Identification of Fund**
- | | | |
|-------------------------------|----|--------|
| Provision for CSR for 2020-21 | Dr | 0.25 / |
| To PM Cares Fund | | 0.25 |

iii. Paid to PM Cares Fund

PM Cares Fund A/c	Dr	0.25 /
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Accounting for Unspent CSR –Ongoing Project (1/2)

- The amount spent on CSR – Expenditure under P/L
- If any amount remains unspent –
 - Transfer to ‘Unspent CSR’ Account within 30 days from end of FY

Illustration Particular	Details
Amount to be spent on CSR Activities	Rs. 5 crores
Nature of the Project	Ongoing Project
Amount actually spent during F.Y. 2020-21	Rs. 4 crores
Unspent Amount	Rs. 1 crore
F.Y till which the unspent CSR for FY 2020-21 be rolled over	2023-24

- In the given Illustration
 - Unspent Amount of Rs. 1 crores should be transferred to the ‘Unspent CSR for F.Y. 2020-21’
 - Within 30 days from end of F.Y. 2020-21
 - Can be rolled over till 2023-2024
 - If till F.Y. 2023-24 is not used, then the remaining unspent amount should be transferred to Fund mentioned in Sch. VII
- **Accounting Treatment –**
The unspent amount shall be treated as
 - **“liability”** when required to be deposited to ‘Unspent CSR’ and if at the end of F.Y. 2023-24 the Fund is identified
 - **“provision”** if at the end of F.Y. 2023-24 the Fund is not identified

Accounting for Unspent CSR –Ongoing Project (2/2)

When transferred to the Unspent CSR Account

i.	<u>Amount to be transferred</u>	<u>Amount (in Cr.)</u>
	CSR expenditure for 2020-21	Dr 1
	To Unspent CSR for 2020-21	1

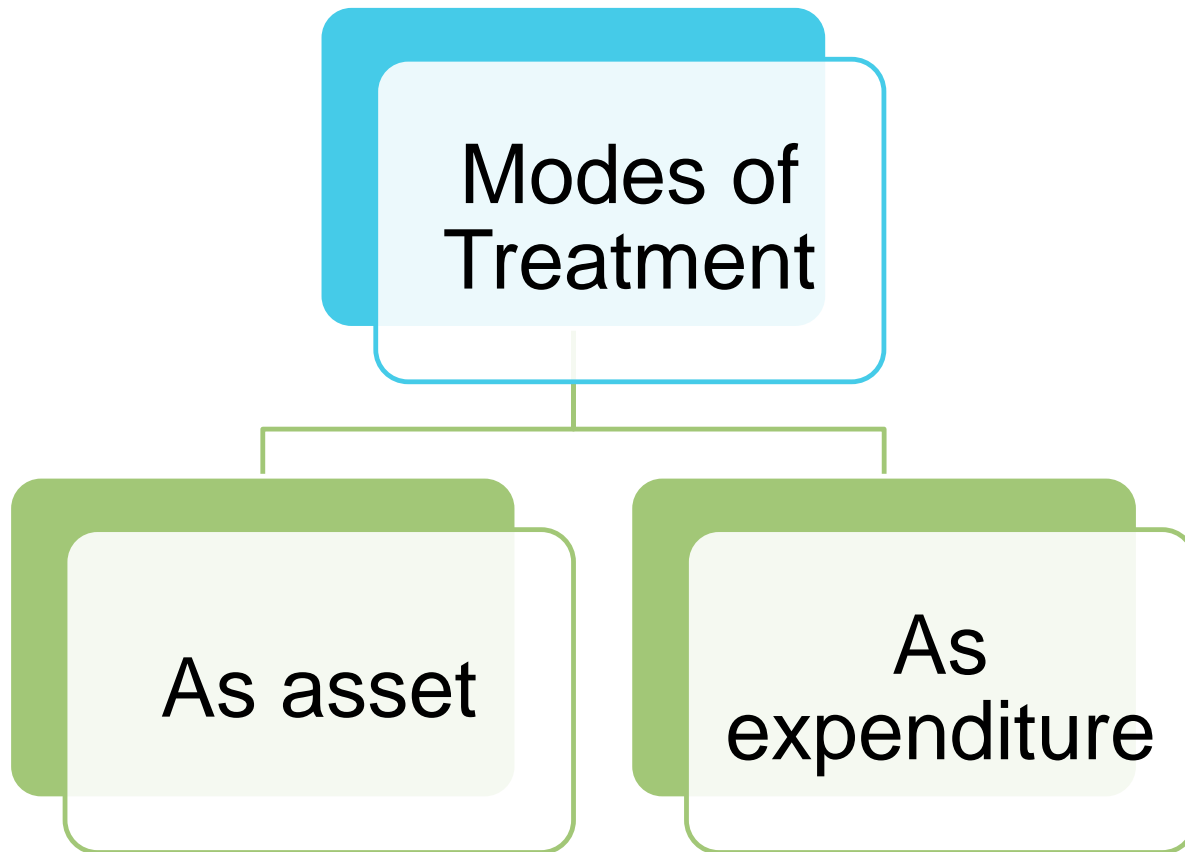
ii. When transferred to Escrow

Unspent CSR for 2020-21	Dr 1
To Bank	1

When CSR expenditure is made in F.Y. 2021-22

i.	<u>Amt wrt 2020-21 spent</u>	<u>Amount (in Cr.)</u>
	CSR Expenditure Account	Dr 1
	To Unspent CSR for 2020-21	1

Accounting Treatment – Excess CSR Spent



- **As an asset**

(i) At the time of Prepaid expense (on 31.03.2021)

Prepaid CSR for 2020-21 A/c Dr xx
To CSR Expenditure

XX

(ii) On 01.04.2021

CSR Expenditure A/c *Dr* *xx*

To Prepaid CSR for 2020-21

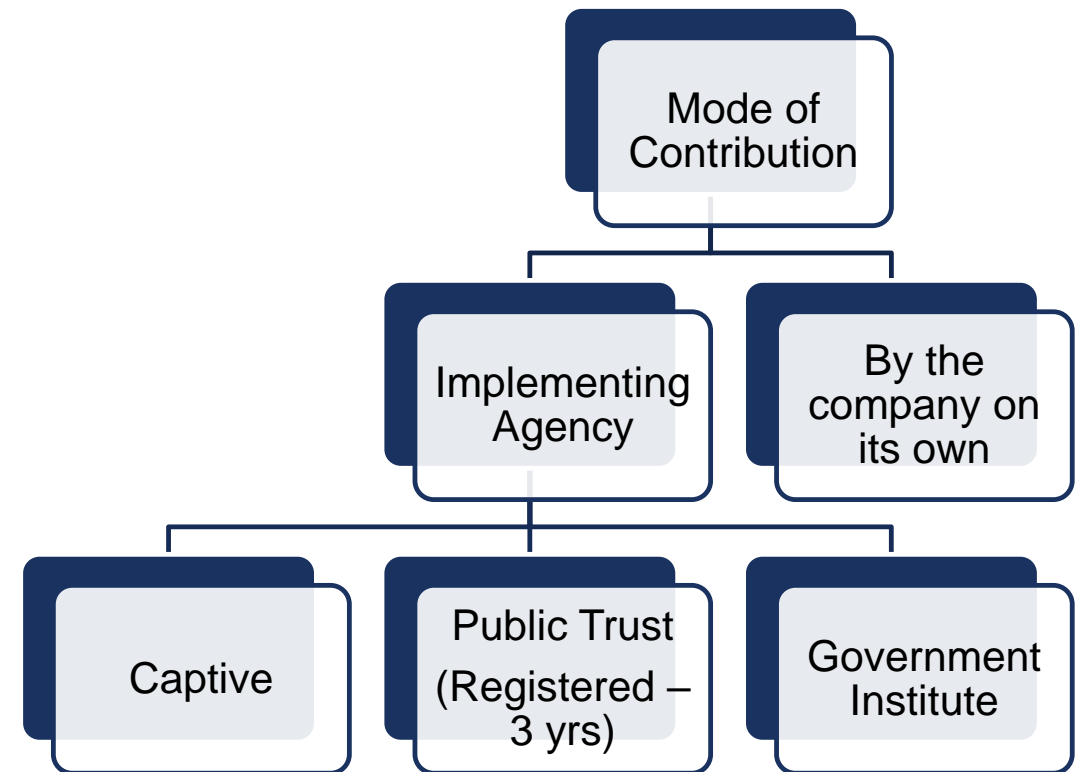
XX

- **As an expense**

In this case, while computing the CSR obligation for F.Y. 2021-22, the excess amount spent shall be deducted, and reported

Other Considerations – Recognition & Measurement

- **Surplus from CSR Activities –**
 - As per Rule 6 (2), **surplus arising out of the CSR projects** or programs or activities **shall not form part of the business profit** of a company.
- **Grant received from others –**
 - Where a company receives a grant from others for carrying out CSR activities, the CSR expenditure should be measured net of the grant.
- **Capital Asset –**
 - If you have created a capital asset by virtue of CSR Spending, the capital asset should not belong to the company
 - **Capital assets can be held by**
 - 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
 - **beneficiaries of the said CSR project**, in the form of self-help groups, collectives, entities; or
 - **a public authority:**
 - **For existing capital assets** - this has to be complied within 180 days i.e by 21st July, 2021 or additional period of 90 days



TAXATION ASPECTS OF CSR



Deductions (1/3)

Section 37 (1) of Income Tax Act, 1961

- *“any expenditure incurred by an assessee on the activities relating to corporate social responsibility referred to in section 135 shall not be deemed to be an expenditure incurred by the assessee for the purposes of the business or profession”*
- ***However, the CSR expenditure which is of the nature described in section 30 to section 36 of the Act shall be allowed as deduction under those sections subject to fulfillment of conditions, if any, specified therein.***
- Idea behind 37 (1) exclusion was that CSR expenses have a **philanthropic nature and were not a business expense**
- Explanatory Memorandum to Finance Bill, 2014 stated that
“....Moreover, the objective of CSR is to share burden of the Government in providing social services by companies having net worth/turnover/profit above a threshold. If such expenses are allowed as tax deduction, this would result in subsidizing of around one-third of such expenses by the Government by way of tax expenditure...”

Deductions (2/3)

Section 35

- Section 35 – Scientific Research;
- Section 35C – Agriculture Development Allowance
- Section 35CC – Rural Development Allowance
- Section 35CCD – Expenditure on Skill Development Project

These activities align with activities mentioned in Sch VII – will deduction be allowed ?

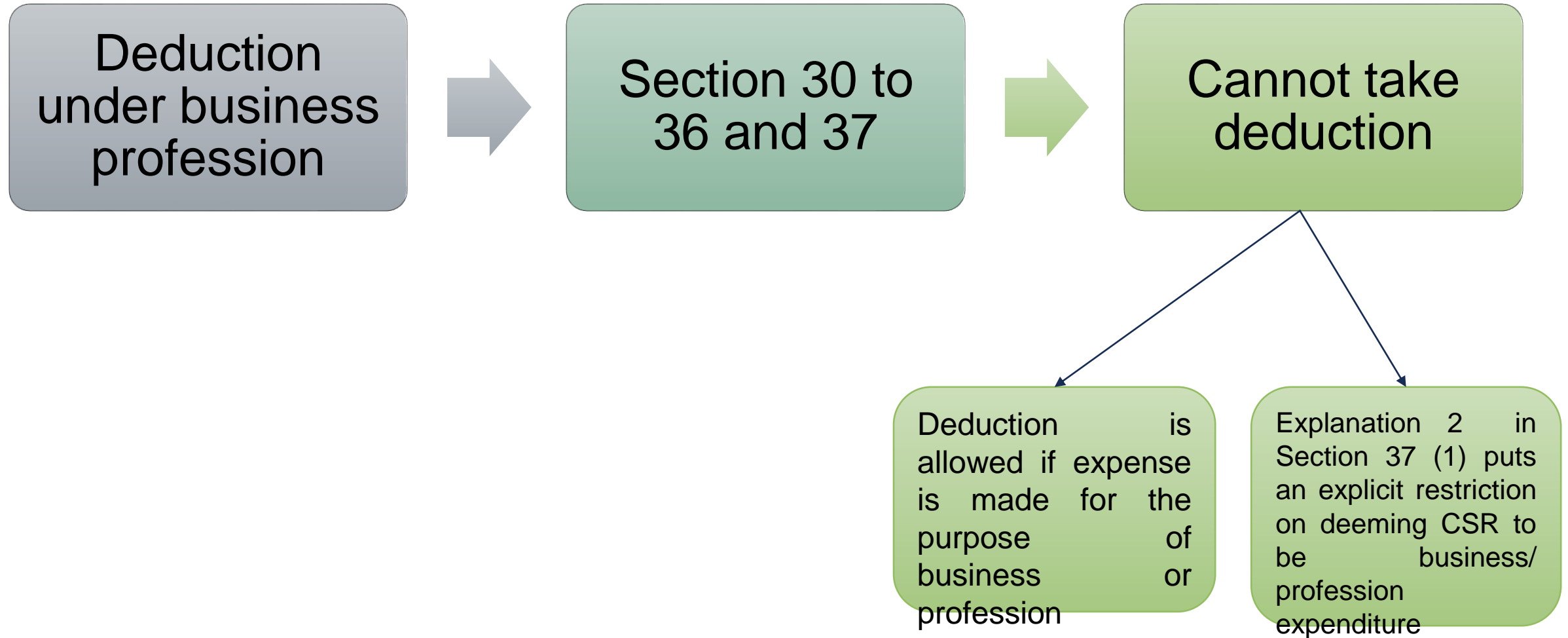
- Section 37 (1) states “*Any expenditure (not being expenditure of the nature described in sections 30 to 36)*”
- Hence, it may be interpreted that deduction will be available
- **However, in view of the intent and objective, as also stated in the Finance Bill 2014, a view is formed that the deduction shall not be allowed**

Deductions (3/3)

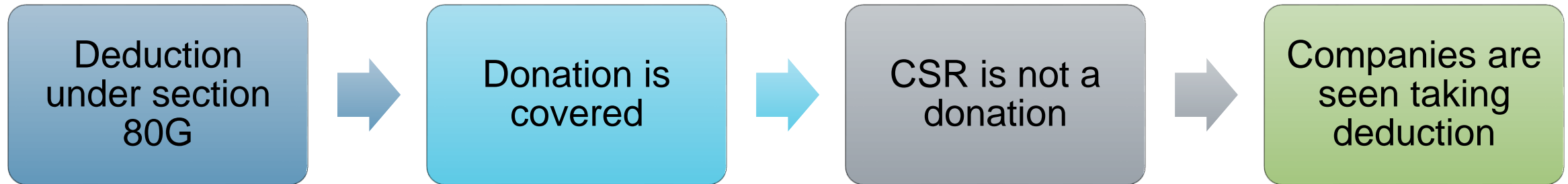
Section 80G

- Deals with deduction in respect of donations to certain funds, charitable institutions, etc
 - In *Goldman Sachs Services Pvt. Ltd. Vs JCIT (ITAT Bangalore)* the ITAT allowed the deduction
 - In *National Seeds Corporation Ltd. v. ACIT, CIT(A)* had held that the expenditure in the nature of CSR expense should be allowable as deduction under sections 35AC and 80G of the IT Act
- However, deduction would render the CSR expense as business expense. **CSR is not equivalent to business expenditure**
- Further, donation under 80G is an incentive for voluntary donations – **CSR is not voluntary**
- In *First American (India) Pvt. Ltd v. ACIT (ITA No.1762/Bang/2019)* & *Allegis services (India) Pvt. Ltd v. ACIT (ITA No.1693/Bang/2019)* the ITAT disallowed deduction under 80G stating that donation is not voluntary and hence not allowable

Taxation Takeaway (1/2)



Taxation Takeaway (2/2)



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CSR DISCLOSURES

Disclosures

Under the 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.
- CSR projects are approved on ongoing basis
- Some of them are fairly minor in terms of expense
- It will be reasonable for the board to make a policy and disclose only material projects

Under BRR

- % of CSR spending of the PAT
- Activities on which CSR spending is done

Under BRSR

- % of beneficiaries from vulnerable and marginal groups
- Other details similar to the annual report on CSR

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