Strengthening the CSR Framework

Why in news?

The Corporate Social Responsibility (CSR) spending in India has risen from Rs. 10,065 crore in 2014-15 to Rs. 24,865 crore in 2020-21.

What is Corporate Social Responsibility?

> *India was the first country to have statutorily mandated CSR for specified companies.*

- Corporate Social Responsibility is a management concept whereby companies integrate social and environmental concerns in their business operations and interactions with their stakeholders.
- **Legal mandate**- Section 135 of Companies Act 2013, mandates the eligible companies to spend **2%** of the average net profits of the immediately preceding 3 years on CSR activities.
- **Applicability**- The provisions of CSR applies to every company, its holding company, its subsidiary company and foreign company having in the preceding financial year
  - Net worth > 500 crore
  - Turnover > 1000 crore
  - Net profit > 5 crore
- **Categories**- Generally, corporate social responsibility initiatives are categorized as
  - Environmental responsibility
  - Human rights responsibility
  - Philanthropic responsibility
  - Economic responsibility
- The Act enumerates the activities that can be undertaken and the manner in which the companies can undertake CSR projects.
- Section 135(5) of the Act is that the company should give preference to local areas around it where it operates.
- **Tax exemption**- The CSR expenditure referred in section 135 **cannot** be claimed as a tax deductible expenditure under **Section 37(1) of the IT Act**.
- However, the CSR expenditure of nature described in Section 30 to 36 of the Act, shall be allowed as deduction under those sections subject to fulfilment of specified conditions.
- Corporates spending on activities like rural development, skill development, agricultural extension projects, contribution to Prime Minister’s National Relief Fund, etc., has tax exemption under other provisions of the IT Act, like Section 80G and 35AC.

What is the current picture of CSR in India?

- Although the CSR spending in India has risen, there is no data to verify whether this increase is commensurate with the increase in profits of Indian and foreign companies.
- There were 2,926 companies in 2020-21 with zero spend on CSR while companies spending less than the prescribed limit of 2% rose in 2020-21.
- There was also a decline in the number of companies participating in CSR — 25,103 in FY2019 to 17,007 in FY2021.

What are the benefits of CSR?

- Stronger brand image, recognition, and reputation
- Increased customer loyalty and sales
- Operational cost savings
- Retaining key and talented employees
- Easier access to funding
- Reduced regulatory burden

What are the issues in CSR framework?

- **Spending percentage**- The requirement of 2% is only a minimum requirement and companies should be encouraged to spend more than this.
- **Registering as trusts**- Many private companies have registered their own foundations/trusts to which they transfer the statutory CSR budgets for utilisation.
- It is unclear if this is allowed under the Companies Act/CSR rules.
- **Geographical bias-** Reports point that 54% of CSR companies are concentrated in Maharashtra, Tamil Nadu, Karnataka, and Gujarat (receiving the largest CSR spends) while populous Uttar Pradesh and Madhya Pradesh receive little.
- **Less focus on environment**- An analysis of CSR spending (2014-18) reveals that most CSR spending is in education (37%) and health and sanitation (29%), whereas only 9% was spent on the environment.
- **Review of reports**- Companies report their CSR spending annually to the Corporate Affairs Ministry (MCA) through annual report.
- It is not known if there is a review of these reports.
- **Output over quality**- It focuses on output rather than quality of the expenditure and its impact.
- The Standing Committee on Finance had observed that information regarding CSR spending by companies is insufficient and difficult to access.
- **Compliance issues**- An auditor can investigate only the details of CSR spending but is not mandated to qualify the accounts for non-compliance or inadequate CSR performance in the audit report.
- **Tax policy**- There is absence of a uniform tax policy in respect of CSR expenses.

What is the need of the hour?

- **Targeted approach**- A national-level platform centralised by the MCA can be curated where all States could list their potential CSR-admissible projects.
- This will help the companies to assess where their CSR funds would be most impactful

with, preferential treatment to areas where they operate.

- **Prioritising the environment**- Companies need to prioritise environment restoration in the area where they operate, earmarking at least 25% for environment regeneration.
- **Participation**- All CSR projects should be selected and implemented with the active involvement of communities, district administration and public representatives.
- **Enhanced compliance**- CSR non-spend, underspend, and overspend should be qualified by the auditor in the audit report.
- **Tax deduction**- India must consider allowing CSR expenditure as deduction from business income.
    - For instance, Philippines allows deduction of all expenses incurred by any corporation whether a large taxpayer or not, in the exercise of its CSR from the taxable income.
- **Recommendations by 2018 high-level committee**
    - Strengthening the reporting mechanisms with enhanced disclosures concerning selection of projects, locations, implementing agencies, etc.
    - Bringing CSR within the purview of statutory financial audit with details of CSR expenditure included in the financial statement of a company
    - Mandatory independent third-party impact assessment audits

References

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