CORPORATE SOCIAL RESPONSIBILTY (CSR)

(TOTAL NO. OF QUESTIONS – 8)

INDEX

S.No.	Particulars	Page No.
1	RTP Questions	31.1
2	MTP Questions	31.3
3	Past Exam Questions	31.5

RTPs QUESTIONS

Q1 (RTP - May 19, April 19 MTP – 8 Marks, May 20 MTP – 4 Marks, October 19 & 21 MTP – 6 Marks, Nov 20 Exam, July 21 – 5 Marks)

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 financial state:

(Rs in Crore)

	March 31, 2019 (Current year)	March 31, 2018	March 31, 2017	March 31, 2016
Net Profit	3.00	8.50	4.00	3.00
Sales (turnover)	850	950	900	800

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 the financial year ended

March 31, 2018.

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

Q2 (RTP Nov 20)

In order to encourage companies and organisations to generously contribute to the Government's COVID-19 relief fund, taxation laws have been amended to reckon these contributions as deductible for the financial year ending 31st March, 2020 even if the contributions are made after the year end but within three months after year end. Government of India issued the notification on 31 st March, 2020 by way of an Ordinance. Such contributions to COVID-19 funds are considered for compliance with annual spends on corporate social responsibility (CSR) for the current accounting year under the Companies Act, 2013. In this scenario, whether the contributions to COVID-19 Relief Funds made subsequent to reporting date of the current accounting period can be provided for as expenses of the current accounting period? Also show its impact on deferred tax, if any.

Solution

According to paragraph 14 of Ind AS 37, a provision shall be made if:

a. An entity has a present obligation (legal or constructive) as a result of a past event;

b. It is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and

c. A reliable estimate can be made of the amount of the obligation. If these conditions are not met as of reporting date, no provision shall be recognised for that financial year.

Government of India issued the notification on 31st March, 2020 by way of an Ordinance and hence, it is most unlikely for any entity to have a present obligation on 31st March, 2020, for such a commitment. As these conditions are not met as of reporting date of financial year 2019 - 2020, no provision should be recognised in the financial statements for that financial year.

In the fact pattern given above, the accounting implications for the financial year 2019-2020 are as follows:

- Do not recognize expense / liability for the contribution to be made subsequent to the year ended 31st March, 2020 as it does not meet the criteria of a present obligation as at the balance sheet date. However, the expected spend may be explained in the notes to the accounts as the same will also be considered in measurement of deferred tax liability.
- If the entity claims a deduction in the Income Tax return for the financial year 2019 - 2020 for that contribution made subsequent to 31st March, 2020, recognise Deferred Tax Liability as there would be a tax saving in financial year 2019 - 2020 for a spend incurred in subsequent year.

MTP QUESTIONS

Q3 (April 18)

Discuss whether any unspent amount of CSR expenditure is to be provided for?

SOLUTION

***Section 135 (5) of 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 profit 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 reason 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 of CSR, in the prescribed format.*

*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 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 reason 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.

Q4 (August 18)

State whether any unspent amount of CSR expenditure (any shortfall in the amount that was expected to be spent as per the provisions of the Companies Act on CSR activities) at the reporting date shall be provided for? Also state in case the excess amount has been spent (ie more than what is required as per the provisions of the Companies Act on CSR activities), can it be carry forward to set-off against future CSR expenditure

SOLUTION

(i) *Treatment of any unspent amount of CSR expenditure*

Since the expenditure on CSR activities is to be disclosed only in the Board's Report, 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 Act requires 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.

(ii) *Treatment of excess amount spent on CSR Activities*

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 CSR spending can be set off against the required 2% CSR expenditure up to the immediately succeeding 3 financial years subject to compliance with the conditions mentioned under Rule 7(3) of Companies (CSR Policy) Rules, 2014. However, the excess amount spent on CSR activities can be set off from 22 January 2021. No carry forward in financial years before FY 2020-21.

QUESTIONS FROM PAST EXAM PAPERS

Q5 (May 18 – 8 Marks)

What are the provisions of section 135 of the Companies Act, 2013 regarding the constitution of a Corporate Social Responsibility (CSR) Committee. Also explain the role of the Corporate Social Responsibility (CSR) Committee and Board.

XYZ Limited is a company which has net worth of Rs 250 crore. It manufactures parts for automobiles. The sales of the company are affected due to low demand of the products. The previous year's financial states of company are as below:

(Rs in crore)

	31st March 2018 (Current Year)	31st March 2017	31st March 2016	31st March 2015
Net Profit	4.25	8.00	3.50	3.25
Turnover	500.00	900.00	400.00	350.00

Examine whether the company has an obligation to form a CSR committee since the applicability criteria is not satisfied in the current financial year.

SOLUTION

As per section 135 of the Companies Act 2013

Every company having either

- net worth of Rs 500 crore or more, or
- turnover of Rs 1,000 crore or more or
- a net profit of Rs 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).

B. Role of Corporate Social Responsibility (CSR) Committee

The CSR Committee shall formulate and recommend to Board-

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
c. 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 percent 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 an amount, the Board shall specify the reasons for not spending the amount.

D. In the given scenario

The MCA has 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, is still required to constitute a CSR Committee and comply with provisions of sections 135 of the Companies Act, 2013.

As per the criteria to constitute CSR committee -

1. *Net worth greater than or equal to Rs 500 Crore: This criterion is not satisfied.*
2. *Sales greater than or equal to Rs 1000 Crore: This criterion is not satisfied.*
3. *Net Profit greater than or equal to Rs 5 Crore: This criterion is satisfied in the financial year ended March 31, 2017 when the net profit was Rs 8 crore.*

Hence, the XYZ Ltd. is required to form a CSR committee.

Q6 (Nov 18 – 4 Marks)

Baby Limited manufactures consumable goods for infants like bath soap, cream, powder, oil etc. As part of its CSR policy, it has decided that for every pack of these goods sold, Rs0.75 will go towards the "Swachh Bharat Foundation" which will qualify as a CSR spend as per Schedule VII. Consequently, at the year end, the company sold 40,000 such packs and a total of Rs 30,000 was recognized as CSR expenditure. However, this amount was not paid to the Foundation at the end of the financial year. Will the amount of Rs 30,000 qualify to be CSR expenditure?

SOLUTION

Baby Ltd. has earmarked 75 paise per pack to spend as CSR activities. However, only by earmarking the amount from such sales for CSR expenditure, the company cannot show it as CSR expenditure. To qualify the amount as CSR expenditure, it has to be spent. Hence, Rs30,000 will not be automatically considered as CSR expenditure till the time it is spent on CSR activities i.e it is deposited to 'Swachh Bharat Foundation'.

Q7 (Jan 21 – 4 Marks)

Sun Shine Limited is a company which seems to be covered under the ambit of CSR rules. As part of its CSR contribution an amount of Rs. 40,000 p.m. was spent by way of adoption of 2 families of drought hit areas.

The average net profits of immediately preceding the financial year was Rs. 1,80,00,000. Please note that the company commenced its commercial activities only on the first day of the immediately preceding financial year. The Accountant of the company says that CSR provisions are not applicable to his company since it is one year old and in case if it is applicable he wants to carry forward the excess amount spent on account of CSR activities to future years.

You are required to comment with the figures, whether the contention of the Accountant is correct in context of CSR provisions?

SOLUTION

As per section 135 of the Companies Act 2013, every company having either

- *net worth of Rs. 500 crore or more, or*
- *turnover of Rs. 1,000 crore or more or*

- *a net profit of Rs. 5 crore or more*

during the immediately preceding financial year *shall constitute a Corporate Social Responsibility (CSR) Committee.*

In the given case, the average net profits of immediate preceding financial year of Sun Shine Limited is Rs. 1,80,00,000 (i.e. Rs. 1.80 crore). Hence, net profit criteria is not met.

Company is covered under the ambit of CSR rules (assuming that net worth or turnover criteria is met):

Since it is given in the question that the company seems to be covered under the ambit of CSR rules, it is assumed that either the net worth of Sun Shine Limited might have exceeded Rs. 500 crore or more, or turnover might have exceeded Rs. 1,000 crore or more during immediate preceding financial year. Accordingly, CSR provisions are applicable to Sun Shine Limited irrespective of the fact that the company is in its second year of operations.

If the company meets any one of the thresholds in the immediately preceding previous year, then the contention of the accountant is incorrect that CSR provisions will not be applicable to the company as it is only one year old.

The accountant wants to carry forward the excess amount spent on account of CSR activities to future years which is Rs. 1,20,000 [Rs. 40,000 x 12 - (Rs. 1,80,00,000 x 2%)]. The excess CSR spending can be set off against the required 2% CSR expenditure up to the immediately succeeding 3 financial years subject to compliance with the conditions mentioned under Rule 7(3) of Companies (CSR Policy) Rules, 2014. However, the excess amount spent on CSR activities can be set off from 22 January 2021. No carry forward in financial years before FY 2020-21.

Q8 (July 21 – 4 Marks)

Nice Limited is a company incorporated on 1st April 2019. The Company has a net worth of Rs. 350 crore. The business of the company was affected due to low demand of its products. The following financial data is available as on 31st March 2021:

Rs. in crore

	31st March 2020 Audited	**31st March 2020 Provisional**
Net Profit	7.10	4.80
Turnover	550.00	1,050.00

During the financial year 2020-2021:

- *The Company has spent Rs. 55,000 per month for developing vocational skills of local youth;*
- *The Company has also provided its products at a considerable discount for the benefit of the under-privileged, the cost of which to the Company is Rs. 3,50,000.*

The Company wants to carry forward its entire expenditure to next year as it is of the opinion that it does not have to spend anything on CSR activities during the current year.

Comment on the Company's applicability under Corporate Social Responsibility as per section 135 of the Companies Act, 2013 for the financial year 2020 -2021. Does it have any obligation to transfer any amount to any fund?

SOLUTION

Applicability of CSR:

A company which meets the net worth, turnover or net profits criteria in immediately preceding financial year will need to comply with provisions of sections 135(2) to (5) read with the CSR Rules.

According to the Act, the Board of every company shall ensure that the company spends, in every financial year, at least two percent of the average net profits of the company made during the three immediately preceding financial years or where the company has not completed the period of three financial years since its incorporation, during such immediately preceding financial years, in pursuance of its Corporate Social Responsibility Policy.

Analysis of given case:

As per the criteria

1. *Net worth greater than or equal to Rs. 500 crore: This criterion is not satisfied.*
2. *Sales greater than or equal to Rs. 1,000 crore: This criterion is not satisfied.*
3. *Net profit greater than or equal to Rs. 5 crore: This criterion is satisfied in financial year ended 31st March 2020 i.e. immediate preceding financial year.*

Hence, the Board has to spend on CSR Activities.

Quantification and mode of utilisation: *As per the facts given in the question amount spent on CSR Activities during the year 2020-2021 pertains to the average net profits of the immediately preceding financial year i.e. 2019-2020. Accordingly, the company is under the obligation to transfer/expense 2% of Rs. 7.10 crore i.e. 0.142 crore = Rs. 14,20,000 in the year 2020-2021.*

Nice Limited has spent Rs. 6,60,000 during the financial year 2020-2021 for developing vocational skills of local youth which is a permissible activity of Corporate Social Responsibility under Schedule VII to the Companies Act, 2013. However, expenditure of Rs. 3,50,000 spent on commercial activities at concessional rate does not qualify as expenditure on CSR activity. Hence, the amount spent of Rs. 6,60,000 by Nice Limited for financial year 2020-2021 is less than the required expenditure of Rs. 14,20,000 to be spent as per the provisions of CSR Rules.

Decision:

Since the company fails to spend such amount, the Board has to report the reasons for not spending the amount as per section 135(5). Further, because the company does not have any on-going project, the unspent amount of Rs. 7,60,000 (Rs. 14,20,000 – Rs. 6,60,000) will be transferred to a Fund specified in Schedule VII to the Companies Act, 2013 within a period of 6 months of the expiry of the financial year 2020-2021.