



## ERGO

*Analysing developments impacting business*

### COMPANIES (AMENDMENT) ACT 2019 HAS A NEW MEANING FOR CSR – VOLUNTARY TO MANDATORY

2 August 2019

On 31 July 2019, the Companies (Amendment) Act 2019 (Amendment) received assent of the President of India. We had written earlier on the ordinance promulgated on 2 November 2018 (Ordinance) to amend the Companies Act, 2013 ([available here](#)). On the one hand, the Amendment retains most changes brought about by the Ordinance to rationalise penalties and the ease compliance burden on businesses and on the other, the Amendment also retains the 'crackdown' provisions on black money and shell companies. The new crackdown provision is the revisions to the existing framework of Corporate Social Responsibility (CSR). The CSR regime is now no longer "comply or explain" but "comply or imprisonment".

Erstwhile CSR requirements under Section 135: Under the erstwhile framework, all companies having net worth of INR 5 billion (equivalent USD 72.5 million) or more, or turnover of INR 10 billion (equivalent USD 145 million) or more, or net profit of INR 50 million (equivalent USD 725,000) or more during any financial year, are required to constitute a CSR committee. Such companies were required to develop a dedicated CSR policy (giving preference to local areas where the company operates) and establish a CSR fund equivalent to 2 percent of the average net profits made by the company in 3 (three) immediately preceding financial years. Under the Companies Act 2013 (Companies Act), if the company failed to meet its CSR obligations, the reasons for not spending the CSR amounts were required to be disclosed in the directors' report.

#### **Key highlights of the Amendment relevant to CSR:**

Transfer of unspent funds – additional requirement under the Amendment: 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 (thirty) days from the end of the financial year. Such account, to be opened with a scheduled bank by the company, will be 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 CSR projects (under its CSR policy) within 3 (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 of 3 (three) financial years, then, such unspent amount should be transferred to a fund specified under Schedule VII of the Companies Act (Schedule VII Fund) within 6 (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 6 (six) months from the end of the relevant financial year.

In effect, the 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 backward classes, minorities and women.

Penal liability for non-compliance: If a company fails to comply with above mentioned obligations, the Amendment provides for imposition of penalty of not be less than INR 50,000 (equivalent USD 725) but which may extend to INR 2.5 million (equivalent USD 36,250). Additionally, the Amendment also provides for imprisonment of every officer of the company who is in default for up to 3 (three) years and a fine of not be less than INR 50,000 (equivalent USD 725) but which may extend up to INR 500,000 (equivalent USD 7,250) or with both. Additionally, separate penalty for continuing offences has also been prescribed.

CSR in case new companies: It has now been clarified in the Amendment that if the company has not completed 3 (three) years from incorporation, the amount to be spent on a CSR fund will be equivalent to 2 percent of the net profits made by the company in the previous financial year (as against average net profits made by the company in 3 (three) immediately preceding financial years).

Central government to have rule making power: Under the Amendment, the central government has been empowered to make rules and issue directions to ensure compliance.

### Key Takeaways:

Under current laws, in spite of not meeting the CSR obligation, companies have merely received notices from the Ministry of Corporate Affairs asking for reasons for not meeting the CSR spend. Post the Amendment, not meeting the CSR obligation will carry penal consequences. The government's case for the Amendment is that this has been done to bring in more effectiveness to the CSR regime. It is too early to assess the exact impact of the CSR related Amendment, the companies must watch out and meticulously comply with the CSR requirements. A substantial picture of compliance requirements will be clear only after the publication of the amendments to the Companies (Corporate Social Responsibility Policy) Rules, 2014 and other ancillary rules and regulations.

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