ORIGINAL RESEARCH PAPER

Management

CHANGING DIMENSIONS OF CSR ACTIVITIES FOR BUSINESS & GOVERNMENT

KEY WORDS: Corporate Social Responsibility (CSR), Assessee, Deductions, Income Tax, Net Profits, Taxable Income, Expenditures, Companies Act,

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ABSTRACT

Every economy has its own distinct needs and implications of its revenues. The governance of an economy is fuelled through its revenues. In order to generate sufficient and timely revenues, the revenue department has to be observant enough to synchronise various sectors of the industries through an established framework of different kinds of taxes, duties, cess, surcharges etc. During the whole course of collection, the revenue department has too diligently look for, not only for probable loop-holes of in collection process, but also how the assessments of taxes are made and how the assesses can be allowed certain leverages for doing their part for the good of the society. Here comes the concept of Corporate Social Responsibility for achieving a government's ultimate objective of serving its people. In a way, an assessee spends a certain amountof funds out of it's taxable income,for the good of society, taking its responsibility as a corporate entity and thereby the revenue department allows certain relaxations in taxable amount to the assessee. Incidentally, the larger good of the society is achieved.

This paper is an analysis of implications of Corporate Social Responsibility in Indian scenario, with a special reference to the mind crunching provisions of the Indian Income Tax Act, 1961 and the Indian Companies Act, 2013

INTRODUCTION:

It has been said that no one can escape from two things the first one is the Death and the other is Taxation. The Indian Income Tax Act, 1961 has been time and again been quoted as being one of the most delicate as well as most complicated taxation framework[1].

Before we go deeper in to the depths of Indian Income Tax, let us clear our basis understanding of the term "Corporate Social Responsibility". As mentioned in the Companies (CSR Policy) Rules 2014, "Corporate Social Responsibility (CSR)" means and includes but is not limited to:

1) Projects or Programs relating to activities specified in Schedule VII of the Act or
2) Projects or Programs relating to activities undertaken by the Board in pursuance of recommendations of the CSR Committee as per the declared CSR Policy subject to the condition that such Policy covers subjects enumerated in Schedule VII of the Act.

Applicability of Section 135(1) of the Companies Act 2013:

Every Company whether Private Limited or Public Limited, including its holding or subsidiary & a foreign company having, during any financial year (any of the three proceeding financial year)[2]:

1. Net Worth of Rs 500 Crores or
2. Turnover of Rs. 1,000 Crores or
3. Net Profit of Rs. 5 Crores.

Amount to be expended on CSR activities:

1) The company shall spend at least 2% of its Average Net Profit for the immediately preceding three financial years on Corporate Social Responsibility activities.
2) CSR expenditures shall include all expenditures including contribution to corpus but does not include any expenditure on any item not in conformity or not in line with activities which fall within the purview of the Schedule VII of the Act.
3) The list of activities in Schedule VII is illustrative and not exhaustive.
4) CSR Committee with a view to discharge its CSR obligation as arising under section 135 of the Act in the following three ways:
   a. making a contribution to the funds as specified in Schedule VII to the Act; or
   b. through (NGO) a registered trust or a registered society or a company established under section 8 of the Act by the company, either singly or along with its holding or subsidiary or associate company or along with any other company or holding or subsidiary or associate company of such other company, or otherwise; or
   c. in any other way in accordance with the Companies (CSR Policy) Rules, 2014, e.g. suo motto.
5) First preference shall be given to Local Area & Area around it, where company operates;
6) In case of failure to expend the amount on CSR Activities, the Board of Directors shall specify the reason for non-expenditure in the Board's Report.

Which activities shall not be considered under Corporate Social Responsibility?

1) CSR projects or programs or activities undertaken in pursuance of its 'normal course of business'
2) CSR projects or programs or activities
   - Carried out as a pre-condition for setting up a business, or
   - As a part of contractual obligation undertaken by the company; or
   - In accordance with any other Act; or
   - As a part of the requirement in this regard by the relevant authorities

(These activities regarded as normal course of business)

3) CSR Projects or Programs or Activities
   - Undertaken outside India;
   - That benefit only the employees of the company & their families
4) Contribution of any amount directly or indirectly to any Political Party (Section 182)

Composition of CSR Committee

1) Minimum 3 including 1 Independent Director except
   - Private Company or
   - The company which is not required to appoint an Independent Director or
   - Foreign Company
2) In Case of 2 Directors

Types of Company	Composition
Foreign Company	At least 2 Person , one of them must be Company's Representative

Private Company (Having 2 Director)	2 Directors
Mandatorily not requiring Independent Director	2 Directors
Any other Company (Mandatorily requiring Independent Director) Either listed or not	Minimum 3 including one of them Independent Director

Consequences of Non-Compliance of Provision

1. If a company contravenes the provision , shall be punishable with fine which

- Shall not be less than Rs. 50,000/-
- But which may extend up to Rs. 25,00,000/-, And

2. Every officers of the Company who is in Default, shall be punishable with

- Imprisonment for a term, which may extend to 3 years or
- Fine which shall not be less than Rs. 50,000/-
- But which may extend up to Rs. 5,00,000/- or
- Both

Disclosure of CSR

Every company, except foreign company shall disclose the Annual report on CSR, containing particulars specified in the Annexure, in its Board Report and publish in website as well[3].

In case of Foreign Company, the Balance Sheet file under Section 381(1) (b) shall contain an annexure regarding reporting on CSR

Format for the Annual Report on CSR Activities to be included in the Board's Report:

S No.	CSR Project or Activity Identified	Sector in Which the Project Covered	Projects/ programme location (Specify the State and district where projects or programs was Undertaken)	Amount Outlay (budget) project or programWise	Spent on the project or programs	Cumulative Expenditure up to the reporting period	Amount SpentDirect or Through implementing agency
			Local	Other		Direct Expenditure	Through Overhead

Meaning of Average Net Profit

Average Net Profit shall be calculated in accordance with Section 198 of the Companies Act, 2013.Following elements shall not be included while calculating Average Net profit [4]:

- Profit of Overseas Branch or Branches of the company,
- Any dividend received from companies in India, which are covered under & complying with the provisions of the Section 135 of the Act.

A) Accounting Treatment

- CSR Expenditure includes Spending as well as Contribution
- CSR is not Charity or mere Donation
- Calculation of CSR spend limit:
- Average profit calculated u/s 198 for last 3 year X 2 % = CSR spend
- Amount unspent or any surplus arising of the CSR activity will not be part of the business profits of company.
- No provision for unspent amount, only disclosure in Board report.
- The excess amount cannot be carried forward for set off against the CSR expenditure required to be spent in future
- If CSR activities has been taken up (in progress) & liability has been incurred (due to contractual obligation), then provisions should be made for such obligation.
- Where a company receives a grant from others for carrying out CSR activities, the CSR expenditure should be measured net of the grant.
- Any surplus arising out of CSR project or programme or activities shall be recognised in the statement of profit and loss and since this surplus cannot be a part of business profits of the company, the same should immediately be recognised as liability for CSR expenditure in the balance sheet and recognised as a charge to the statement of profit and loss and such surplus is not form part for calculating limit.

CSR Activities under taken following ways:

a) Making contribution: Treated as an expense for the year and charged to the statement of profit and loss.
b) Through others': Treated as an expense for the year and charged to the statement of profit and loss.
c) Any other way on its own:

- ***In nature of Capital Expenditure***

CSR is a Capital Expenditure if such expenditure meets the definition of an Assets According to present Accounting Standard, an asset is a resource controlled by enterprises as a result of past events, and from which future economic benefits are expected to flow to enterprises. Depreciation of such an asset can be claimed as CSR expenditure only if the expenses incurred on creation of assets are not claimed as CSR expenditure [5].

(i) in cases where the control of the 'asset' is transferred by the company, e.g., a school building is transferred to a Gram Panchayat for running and maintaining the school, it should not be recognised as 'asset' in its books and such expenditure would need to be charged to the statement of profit and loss as and when incurred

(ii) In other cases, where the company retains the control of the 'asset' then it would need to be examined whether any future economic benefits accrue to the company. Invariably future economic benefits from a 'CSR asset' would not flow to the company as any surplus from CSR cannot be included by the company in business profits.

- ***In nature of Revenue Expenditure***

CSR is revenue expenditure if company has incurred expenditure on the activities specified under Schedule VII of Companies Act, 2013. If CSR expenditure related to business of the entity then such expenditure should be treated as an expense in the statement of profit and loss.Where a company receives a grant from others for carrying out CSR activities, the CSR expenditure should be measured net of the grant [6].
Company may supply goods manufactured by it or render services as

a) the expenditure incurred should be recognised when the control on the goods manufactured by it is transferred or the allowable services are rendered by the employees.
b) The goods manufactured by the company should be valued in accordance with the principles prescribed in Accounting Standard.
c) The services rendered should be measured at cost.
d) Indirect taxes on the goods and services so contributed will also form part of the CSR expenditure

- **In nature of Appropriation**

CSR expenditure is not related to the business of the entity then such an expenditure should be treated as an appropriation of profit [7].

Presentation in Financial Statement

a) All expenditure on CSR activities, that qualify to be recognised as expense should be recognised as a separate line (Separate Ledger Head) item as 'CSR expenditure' in the statement of profit and loss. Further, the relevant note should disclose the break-up of various heads (Functional Head) of expenses included in the line item 'CSR expenditure'

b) The notes to accounts relating to CSR expenditure should also contain the following:

a. Gross amount required to be spent by the company during the year.

b. Amount spent during the year on:

S No.	Particular	In cash	Yet to be paid in cash	Total
(i)	Construction/acquisition of any asset			
(ii)	On purposes other than (i) above			

The above disclosure, to the extent relevant, may also be made in the notes to the cash flow statement, where applicable.

c) Details of related party transactions, e.g., contribution to a trust controlled by the company in relation to CSR expenditure

d) Where a provision is made same should be presented as per the requirements & movements in the provision during the year should be shown separately.

B) Taxation Matter

MCA does not come out with the clear guideline regarding tax treatment of CSR expenditure but there may be one possible solution for tax incentive of CSR expenditure is with the compliance of scope of CSR activity of schedule VII should be expanded so as it include activity which consider as social activity & also related to business for getting Best benefit to Income tax.

According to Explanation 2 of the Finance (No.2) Act, 2014.

"any expenditure incurred by an assessee on the activities relating to corporate social responsibility referred to in section 135 of the Companies Act, 2013 (18 of 2013) shall not be deemed to be an expenditure incurred by the assessee for the purposes of the business or profession."[8]

One side it is mandatory to spend money on CSR as per Companies Act,2013 and on the other side the same is disallowed under the Income Tax Act, 1961, the CSR policy should be formulated by the CSR Committee in such a manner as to require CSR expenditure to be incurred on such activities as laid down in Schedule VII that are also eligible for deduction under sections 30 to 36 of the IT Act, it would facilitate companies in complying with the CSR obligations under the Companies Act, 2013 as well as in availing of the tax benefit under the Income Tax Act, 1961 [9].

In Summary

S No.	Section	Nature
1	35	Deduction of Expenditure on Scientific Research Capital as well as Revenue Exp.
2	35AC	Expenditure on Eligible Projects or Schemes
3	35CCA	Payments to Association & Institution for Carrying out Rural Development rogrammes
4	35CCD	Expenditure on skill development project notified by the board
5	36(1)(ix)	Applicable to Company who incurs expenditure on promotion of family planning amongst employees Revenue as well as capital expenditure
6	80G	Donation to certain Funds & Institutions
7	80GGA	Deduction in respect of donation to scientific research or rural development section

As per income tax ,Contribution to Swach Bharat Kosh 80G(2)(iiihk) & Clean Ganga Fund 80G(2)(iiihl) must be other than CSR u/s 135 of Companies act.

It has been explained by the CBDT in the circular no. 1/2015 Dated 21/1/2015:

"CSR expenditure, being an application of income, is not incurred wholly and exclusively for the purposes of carrying on business. As the application of income is not allowed as deduction for the purposes of computing taxable income of a company, amount spent on CSR cannot be allowed as deduction for computing the taxable income of the company. 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."

A few relevant cases in reference to Corporate Social Responsibility

- **Krishna SahakariSakharKarkhana Ltd v CIT:** Payment to an Education Fund of the State Federal Society as required u/s 68 of the Maharastra Co-operative Society Act
- **CIT v Andra Bank:** Spent on Andra Bank Rural Development Trust which is engaged in conducting several training for providing self employment to rural youth and after the training , the bank also provided finance to rural youth.

Confusion & Vague Interpretation of Law

CIT v. Infosys Technologies Ltd : Allowed the expenditure incurred for installing traffic signal by company under social initiative by the reason of the said signal used by its employee sp its relate to business activity hence allowed u/s 37(1)

However, in the Case of **CIT v. Wipro Ltd :**Expenditure for community development near its factory, the court does not find any nexus for its business activity hence disallowed such expenditure u/s 37(1)

CIT v DTTDC Ltd: Where the income is utilized for self-imposed obligation, it signifies "Application of Income" whereas obligation where money flows out of an independent title signifies "Diversion of Income." However, Explanatory Memorandum to the Bill it is stated that CSR expenditure is an application of Income.

Here, one question raised, whether one can claim the deduction of CSR u/s 37(1) up to the amount which is necessarily required to expended u/s 135 of companies act, 2013, on the ground that it is diversion of income by successfully substantiating that the same has been expended because of mandate by the Companies Act, 2013 and not because of self-imposed.

MAT

While computing Book Profit u/s 115JB of the Income Tax Act relating to Minimum Alternative Tax (MAT) the CSR expenditure should not be considered as a below the line item meanwhile same would not be allowed under normal provision of income tax act. Hence, the Book Profit to be computed u/s 115JB of the Act should not be increased by the expenditure incurred on CSR i.e. No Adjustment for CSR u/s 115JB

CONCLUSION:

According to research done by EY, the CSR-spending stipulation is likely to apply to at least 2,500 companies. Money spent on activities including eradication of extreme hunger, promotion of education and gender equality, reduction of child mortality and improvement of maternal health, environment sustainability, social business projects, employment enhancing vocational skills, sanitation, promotion of sports and games, welfare activities for the disabled and old, setting up model villages, scholarships and combating HIV and AIDS, is likely to be made permissible to be counted under CSR expenditure.

Irrespective of the complicated regulations and provisions of Indian Income Tax Act, 1961 and the Indian Companies Act, 2013, the Corporate Social Responsibility has taken a solid ground and its true potential is yet to be charted. It should be realised with utmost caution and diligence that CSR expenditures are not a getaway or an alternative for tax avoidance and tax evasion, rather it's an imperative economic tool to reach out for the greater good of the society at large.

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