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## India Substantially Revamps CSR Requirements – The Impact on Compliance at Indian Subsidiaries of U.S.-Based Multinationals

Link Legal and Ropes & Gray previously jointly published an Alert on proposed changes to Indian corporate social responsibility requirements relevant to multinationals doing business in India. In this update to our earlier Alert, we discuss the amendments that have now been adopted. The new Indian CSR regime differs substantially from its predecessor and therefore requires significant changes to the CSR programs of multinationals with operations in India.

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CSR requirements under Indian law largely are contained in Section 135 of the Companies Act, 2013. Section 135 has been amended several times since its adoption. The amendments proposed in 2019 are discussed in our earlier joint Alert available [here](#). Our earlier Alert also describes the compliance thresholds under Section 135. These have not changed.

Earlier this year, the Ministry of Corporate Affairs (the “MCA”) notified the amendments proposed under the Companies (Amendment) Act, 2019 (“Amendment Act”) and the Companies (CSR Policy) Amendment Rules, 2021 (“CSR Amendment Rules”). The modifications introduced by the Amendment Act and the CSR Amendment Rules are discussed below.

### Permitted CSR Activities – Changes to the Definition of “Corporate Social Responsibility”

The definition of Corporate Social Responsibility has been amended to mean the activities undertaken by a subject company pursuant to its statutory obligation laid down under Section 135 of the Companies Act and the rules adopted thereunder.

In addition, a negative list of activities, which are not considered CSR activities, has been introduced. The following broad categories are on the negative list:

- activities undertaken in the normal course of business;
- activities undertaken outside India;
- contributions to political parties;
- activities that significantly benefit employees (measured as benefitting more than 25% of employees) and their families;
- activities supported on a sponsorship basis for deriving marketing benefits for products or services; and
- activities carried out in fulfillment of any other statutory obligations under Indian law.

There are, however, certain exceptions to the negative list. As a limited exception to the normal course of business, an exclusion has been carved out for companies engaged in research and development of new vaccines, drugs and medical devices. For these companies, research and development activity of new vaccines, drugs and medical devices related to COVID-19 is a permissible CSR activity for fiscal years 2020-21 through 2022-23.

Separately, the MCA has clarified that spending CSR funds for the following is an eligible CSR activity: (1) creating health infrastructure for COVID-19 care; (2) establishing medical oxygen generation and storage plants; (3) manufacturing and supplying oxygen concentrators, ventilators, cylinders and other medical equipment for countering COVID-19; and (4) similar activities. These activities, projects or programs may be undertaken by companies directly or in collaboration as a shared responsibility with other companies.

In addition, the training outside of India of Indian sports personnel representing any State or Union territory at the national level or India at the international level is a permitted CSR activity.

### **Minimum Spending on CSR Now Mandatory**

It is now mandatory for subject companies to spend at least 2% of average net profits made during the three immediately preceding fiscal years (the “Minimum CSR Amount”) on CSR initiatives in accordance with the company’s CSR Policy.

If the company has not been in existence for three fiscal years, the Minimum CSR Amount is determined based on the average net profits made during the fiscal years since the company’s formation.

### ***Treatment of Unspent CSR Amounts***

Any unspent Minimum CSR Amount relating to an “Ongoing Project” is now required to be transferred within 30 days after the end of the fiscal year to a special account (an “Unspent CSR Account”) to be maintained by the company. Funds in the Unspent CSR Account are required to be spent by the company in furtherance of its CSR Policy within three fiscal years from the date of transfer to the account.

Under the CSR Amendment Rules, an “Ongoing Project” is a multi-year project undertaken by a company in fulfilment of its CSR obligation, with timelines not exceeding three years (excluding the fiscal year in which the project was commenced). An Ongoing Project includes a project that initially was not approved as a multi-year project but the duration of which was subsequently extended beyond one year by the board based on reasonable justification.

If the company fails to spend the funds in the Unspent CSR Account within the prescribed three-year period, the unspent amount is required to be transferred to a CSR fund set up by the Government of India (a “Government CSR Fund”). In the case of an Ongoing Project, this must occur within 30 days after the end of the third fiscal year. If the unspent amount in a fiscal year does not relate to an Ongoing Project, the company is required to transfer the unspent amount to the Government CSR Fund within six months after the end of its fiscal year.

### ***Concept of a Set-Off Introduced***

If the company spends an amount in excess of the Minimum CSR Amount, it has the discretion to set off the excess against its spending requirement in the succeeding three fiscal years. The company may elect to do so by resolution of its board of directors.

### ***CSR Overhead Is Capped***

The board of directors is now required to ensure that Administrative Overheads do not exceed 5% of the total CSR expenditures of the company for the fiscal year.

“Administrative Overheads” has been defined under the CSR Amendment Rules as the expenses incurred by the company for general management and administration of CSR functions. Expenses directly incurred for designing, implementing, monitoring and evaluating a particular CSR project or program are not considered to be Administrative Overheads.

### *Treatment of Surplus Funds*

Any surplus arising out of CSR activities cannot form part of the business profit of the company. The surplus must be used as follows:

- for the same project;
- transferred to the Unspent CSR Account and spent in furtherance of the CSR Policy and annual action plan of the company; or
- transferred to the Government CSR Fund within six months after fiscal year end.

### *Creation or Acquisition of a Capital Asset*

CSR amounts may now be spent by a company for the creation or acquisition of a capital asset. However, the asset must be held by one of the following:

- a company established under section 8 of the Companies Act, or a registered public trust or registered society, having charitable objects and a CSR Registration Number;
- beneficiaries of the CSR project, in the form of self-help groups, collectives or entities; or
- a public authority.

### **There Has Been a Shift from a “Comply or Explain” to a “Comply or Be Penalized” Regime**

If a company is not in compliance with the amended CSR provisions, it may be fined up to twice the amount required to be transferred by it to the Government CSR Fund or the Unspent CSR Account, up to INR 10 million (approximately USD 136,400).

In addition, every officer of the non-compliant company can be fined up to 10% of the amount required to be transferred by the company to the Government CSR Fund or the Unspent CSR Account, up to INR 0.2 million (approximately USD 2,730).

As originally proposed, the Amendment Act would have included a criminal penalty for non-compliance, which could have carried a prison term of up to three years. That proposal is not part of the amendments ultimately adopted.

### **There Are New Limits on Entities that Can Undertake CSR Activities**

Pursuant to the CSR Amendment Rules, only specified types of entities can undertake CSR activities on behalf of a subject company. These are:

- a company established under Section 8 of the Companies Act (a not-for-profit company), or a registered public trust or a registered society established by the subject company, either singly or along with another company;
- Section 8 not-for-profit companies or a registered trust or a registered society established by the Central Government or State Government;
- an entity established under an act of Parliament or a State legislature; or

- Section 8 not-for-profit companies, or a registered public trust or a registered society, with an established track record of at least three years in undertaking similar activities.

### ***Mandatory Registration of Entities Undertaking CSR Activities***

Pursuant to the CSR Amendment Rules, every entity that intends to undertake a CSR activity is required to register with the Central Government by filing the e-Form CSR-1 electronically with the Registrar of Companies. Upon submission of the e-Form CSR-1, the company is assigned a unique CSR Registration Number.

An e-Form CSR-1 is not required to be filed for entities undertaking CSR projects or programs approved prior to April 1, 2021.

### ***Engagement of International Organizations***

A company now has the discretion to engage an “International Organisation” for designing, monitoring and evaluating CSR projects or programs approved pursuant to its CSR Policy, as well as for capacity building of its personnel for CSR activities.

“International Organisation” is defined under the CSR Amendment Rules to mean “an organisation notified by the Central Government as an international organisation under Section 3 of the United Nations (Privileges and Immunities) Act, 1947, to which the provisions of the Schedule to the said Act apply.”

### **The Role of the CSR Committee and the Board Has Been Enhanced**

#### ***Change in the Definition of “CSR Policy”***

The new definition of “CSR Policy” recognizes the importance of the recommendations of the CSR Committee.

“CSR Policy” has been redefined under the CSR Amendment Rules to mean “a statement containing the approach and direction given by the board of directors of a company, considering the recommendations of its CSR Committee, and includes guiding principles for selection, implementation and monitoring of activities as well as formulation of the annual action plan.”

The role of the board and the CSR Committee is further discussed below. Requirements relating to the composition of the CSR Committee also are further discussed in our earlier Alert available [here](#).

#### ***The New Role of the CSR Committee and New CSR Policy Requirements***

Pursuant to the CSR Amendment Rules, the CSR Committee is required to formulate and recommend to the board of directors an annual action plan in furtherance of the company’s CSR Policy. The board may alter the plan at any time during the fiscal year, based on the recommendation of the CSR Committee, if it has reasonable justification for doing so.

The CSR Policy must include the following:

- the list of approved CSR projects or programs;
- the manner of execution of the projects or programs;
- the modalities of utilizing the funds and the implementation schedules for the projects or programs;

- monitoring and reporting mechanism for the projects or programs; and
- details of need and the impact assessment (discussed later in this Alert), if any, for projects undertaken by the company.

### ***Stringent Board Monitoring Requirement Added***

The board of directors is now required to monitor the implementation of ongoing CSR projects, with reference to approved timelines and the allocation of funds. The board is charged with making modifications, if any, necessary for smooth implementation of the project within the overall permissible time period.

The board also is now responsible for ensuring that funds are utilized for approved purposes. The chief financial officer or the person responsible for financial management of the company is required to certify annually that funds are being used for approved purposes.

### **An Impact Assessment Now Is Required for Many CSR Projects**

Companies that have an average CSR obligation of INR 10 million (approximately USD 135,100) or more in the three immediately preceding fiscal years are required to undertake an impact assessment of their CSR projects that have outlays of INR 10 million (approximately USD 135,100) or more and that have been completed not less than one year before undertaking the impact study.

The impact assessment must be conducted by an independent third party.

Impact assessment reports are required to be placed before the board and annexed to the annual report on CSR (which is discussed below).

### **New Reporting and Website Disclosure Requirements Have Been Added**

#### ***Annual Reporting on CSR Activities***

The CSR Amendment Rules have introduced a format for annually reporting on CSR activities. The CSR report must be included in the board's report beginning with the fiscal year commencing on or after April 1, 2020.

#### ***Website Disclosures***

A subject company must disclose its CSR Policy on its website.

In addition, the board now also is required to ensure that the composition of the CSR Committee and CSR projects approved by the board are disclosed on the company's website.

### **About Ropes & Gray's Practice**

Ropes & Gray has a leading ESG, CSR and business and human rights compliance practice. We offer clients a comprehensive approach in these subject areas through a global team with members in the United States, Europe and Asia. In addition, senior members of the practice have advised on these matters for more than 30 years, enabling us to provide a long-term perspective that few firms can match.

For further information on the practice, click [here](#).