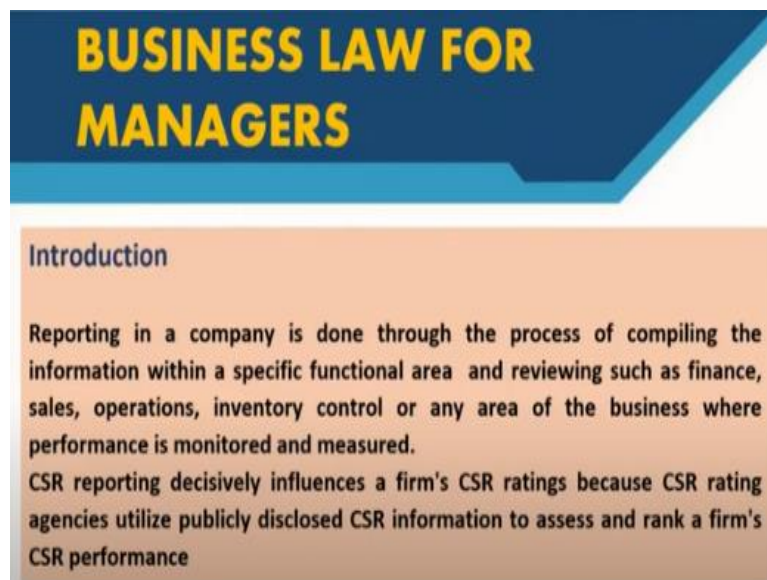


Business Law for Managers
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Module-1: Corporate Law

Lecture - 05
Reporting and Various Activities under CSR

Good evening. We are into the lecture 5, module 1 Reporting and Various Activities under CSR.

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CSR is something which is known perhaps to all even otherwise without knowing business law. You do not have to know business law to know CSR. Corporate Social Responsibility is a world buzzword, which is making rounds for the last few years. And there are strong yes and no for this, let me tell you. I have been interacting, I have been to lot of debates on this.

Being into the corporate for the last so many years, more than 30 years, I have my own views, maybe little bit influenced by the corporate side, but I try to be as independent as possible, when it comes to open topics like CSR, but largely there are very strong views. One view is yes, corporates needs to be disciplined. Other view is no, it cannot be strangled, it cannot be coerced.

It should come naturally, create environment for that. Of course, the other view is even if you create environment, corporate are creatures who are congenitally since birth indisciplined, so they need to be disciplined. So having said that, let us see what the Indian corporate law and the makers of law in India thought of CSR and where is CSR standing today.

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CSR does contain a large part of the annual reports today. Annual reports we all know are annual reporting books or status or documents of any company be it listed or non-listed. Listed meaning listed in the bourses, stock exchanges are non-listed. India has little more than 7000 listed companies today. But this provision is applicable for both listed and non-listed companies.

But I am talking of mostly listed companies because there you find the challenges galore because they have various stakeholders and the largest stakeholder is a shareholder where a private company does not have and a non-listed company does not have. Now the annual report which is a primary document for a corporate which is read by all the people, all the stakeholders, vendors, customers, largely report the government authorities, the income tax authorities.

Most importantly the institutional investors, the foreign portfolio investors, they bank on the annual report, they study on the annual report. And if you go through the annual report of any big corporate today a large chunk of the glossy, colorful pages

non-statutory pages. Annual report contains both statutory documents, non-statutory documents. So what are the statutory documents?

The statutory documents are the profit and loss account for the period, the balance sheet for the as on a particular date that is 31st March, which is on a date and profit and loss is for the period, 1st April to 31st March along with all explanations, notes. Most importantly, the statutory auditors report to the members whether the accounts are absolutely okay or not.

And then these are the accounting statutory requirements. The other statutory requirements are non-accounting which are the directors' report, very important where the directors give their views on the performance of the company to the owners of the company to the shareholders.

This document is relied upon everywhere, by the income tax authorities, by Reserve Bank of India, by government authorities, by Ministry of Corporate Affairs, by any investigating authorities whether it is a MRTP, CCI, FEMA, FERA, ED, they all depend on this one particular document which is audited, signed by the directors. Onus is taken by the directors. Directors are responsible for this document is called the annual report.

And then a specific paragraph in every directors' report today, which talks of Directors' Responsibility Report DRR where the director says each and every thing which is mentioned in the Annual Report statutory part we take the onus, we take the responsibility that these are correct. Now these are the statutory part.

But the non-statutory part contains all that the company has done by showing pictures by showing various activities the company has taken for good. And for good basically of the society. And you will find at least few pages containing all CSR activities there. Why it is done? Because the foreign portfolio investors, the Foreign Institutional Investors are very particular on this. They called it the triple bottom line concept.

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Annexure-1: Format for the Annual Report on CSR

Initiatives to be Included in the Board Report by Qualifying Companies

1. Provide a brief outline of the Company's CSR Policy including the **Statement of Intent** reflecting the **ethos** of the company, **broad areas of CSR interest** and an **overview of activities proposed to be undertaken**.
2. Indicate the web-link to the CSR Policy. The Policy should include the **full list of projects/activities/programmes proposed to be undertaken by the company**.
3. The board Report referring to any financial year initiating on or after the 1st April 2014, shall include an Annual Report on CSR.
4. In case of foreign company, the balance sheet filed shall contain an Annexure regarding a report on CSR

There is the concept called triple bottom line, which means a company has three types of profits. One is the profit we all know that is the profit the normal course of statutory auditors audit, the accounts prepared which is disclosed in the annual report. But the institutional investors look for other two profits, environment and society. How much you have spent on environment, how much you have spent on society?

Supposing a company's net profit shows 40 crores and when it comes to environment it shows it has not spent anything. Whereas another company has spent 40 crores, has the same profit 40 crores, same. If you see accounting profit there is no change 40 and 40. But institutional investors are looking at the company saying how much you have spent on environment it comes to 0.

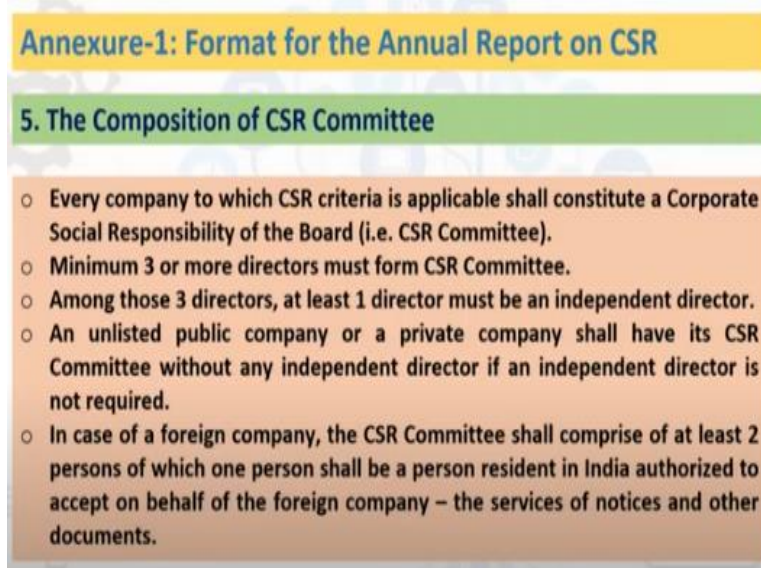
But the other company has spent 10 crores on environment. So immediately the institutional investor will add the 10 crores and make your profit 50 crores parallel 40 crores for this company. Similarly, for CSR. They will say how much you have spent for CSR? Suppose it has spend 5 crores and the other company has spent only 2 crores. So we will add to 2 to 40 make it 42 and this company will add 5.

So you will add another 5 here. So 30 plus 10, 40 plus 5, 45. This is how they compare the two companies. So the corporates have understood this and they have started showing CSR activities they have undertaken in the annual report. Good there is nothing wrong in that. If you do something good if you show it to the world, there is nothing wrong.

But point is are all companies doing it what they are showing, that is one thing. Second thing who is auditing that? These are non-statutory pages. This has not been audited. So many times the question still remains, are the CSR activities which have been shown are duly audited and who is auditing the same? Some action has been taken of late by the Ministry of Corporate Affairs asking for give me the detail CSR expenses done duly audited by the statutory separately.

But again, that is far from what is to be what could have been done earlier or even now what is to be done. There are still gaps in that. Now coming back to this item of CSR to be reported in the board's report, it is categorically mentioned what are to be taken into consideration. What activities they have taken, what amount they have spent in the directors' report. To that extent this matter has been addressed.

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Annexure-1: Format for the Annual Report on CSR

5. The Composition of CSR Committee

- Every company to which CSR criteria is applicable shall constitute a Corporate Social Responsibility of the Board (i.e. CSR Committee).
- Minimum 3 or more directors must form CSR Committee.
- Among those 3 directors, at least 1 director must be an independent director.
- An unlisted public company or a private company shall have its CSR Committee without any independent director if an independent director is not required.
- In case of a foreign company, the CSR Committee shall comprise of at least 2 persons of which one person shall be a person resident in India authorized to accept on behalf of the foreign company – the services of notices and other documents.

CSR committee has to be constituted. One director must be an independent director. The question remains why not all three independent directors? The question remains why the chairman is not mentioned to be an independent director. Some leeway is given to a foreign company.

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Annexure-1: Format for the Annual Report on CSR

Initiatives to be Included in the Board Report by Qualifying Companies




6. Average **Net Profit** of the company for last 3 financial years
7. **Threshold Limit**-(2% of this amount as in 4 above)
8. Details of CSR activities/projects undertaken during the year:
 - a. **total amount** to be spent for the year
 - b. **amount carried forward** from earlier years
 - c. **amount spent during the year** as below
 - d. **amount carried forward** for the year.

Average net profit has been mentioned for the last three financial years. Total amount to be spent for the year, amount carried forward from earlier years, amount spent during the year, amount carried forward for the year. Now this is important. 2% of the net profits of the company you have to spend every year. If there is a shortfall, which you have not spent, you have to keep it in a separate account for spending.

And that spend must happen within a certain period of days. It may happen before the period end 31st March you are undertaking a project, school project. But the school project would require 1.5 maybe crores but you could spend only 50 lakhs by 31st March. Spend meaning you have to show receipt, documentary evidence that you have spent which is audited or needs to be audited, at least prima facie you have to show.

Now one 50 lakhs have been shown, 0.5 crores have been shown. Now 1 crore is pending. Now 1 crore is pending for this year, it can be carried forward to next year. You have said you are spending this year, however you could not give the receipt for this year. So it cannot be shown as a spend for the next year.

You are given a timeline within so many days, six months, you can get another extension for six months, you have to spend and give that this amount has been spent. In case that has not been spent it will remain as an expenses for that year and then it will be transferred to a trust of the government. It is outside your view now.

You do not have to control. It goes to the government's benevolent or really fund kind of thing. Similarly if you have overspent any year, you are supposed to spend say 2 crores, 2% of net profits come 2 crores. Supposing you have spent 5 crores. The additional 3 crores now is allowed to be carried forward and adjusted in the next year. Earlier it was not there. This is a positive development.

If for any reason a project I have undertaken and that project requires 5 crores but 2% of the net profits makes it only 2 crores. So as a corporate I could have spent just 2 crores and kept quiet because my compliance is done. Who will give the balance 3 crores? Now it is saying okay you are undertaking a big, so every corporate was trying to take a project within my limit.

I will not take a big project because a big project is only means bigger expenditure. Finally, I will not get any relief. I again next year I have to spend within 2%. See the difficulty of a corporate in a scenario like this. Please understand a corporate is not a charitable institution, it goes on giving CSR. End of the day there are other stakeholders whose interest also have to be met.

So the corporate says then let us take small projects. Considering all these the ministry thought this is wrong. Let us encourage the corporates take bigger projects. Let the corporate take a bigger project which might take two years, three years, four years, five years. But if it spends over and above 2% in the first year itself or in the second year, whatever extra spending goes that goes carried forward to the next year, positive development.

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Annexure-1: Format for the Annual Report on CSR

Initiatives to be Included in the Board Report by Qualifying Companies

9. In case the company has failed to spend the 2% of the Average Net Profit (INR) of the last 3 financial years, please provide the reasons for not spending the amount.

10. A Responsibility Statement, of the CSR Committee, that the CSR policy implementation and monitoring thereof is, in letter and spirit, in compliance with CSR objectives.



Now as I disclosed that if you are unable to spend 2% then you have to give a reason for not spending which hampers the image of the company in the directors' report. The directors have to say it that we are unable to spend. What can be the reason for unable to spend? You have to specify that. The good point is the jailing provision there has been removed.

At least now no promoter or owner or director will be jailed, but reasoning is there. Now reasoning also has been removed. You have to spend. If you do not spend then that amount of money you have to keep in your book as unspent amount and liability you have to look at provision or a liability. So the loss or the profit will be curtailed down and a provision has to be made, stricter provision, better than jailing.

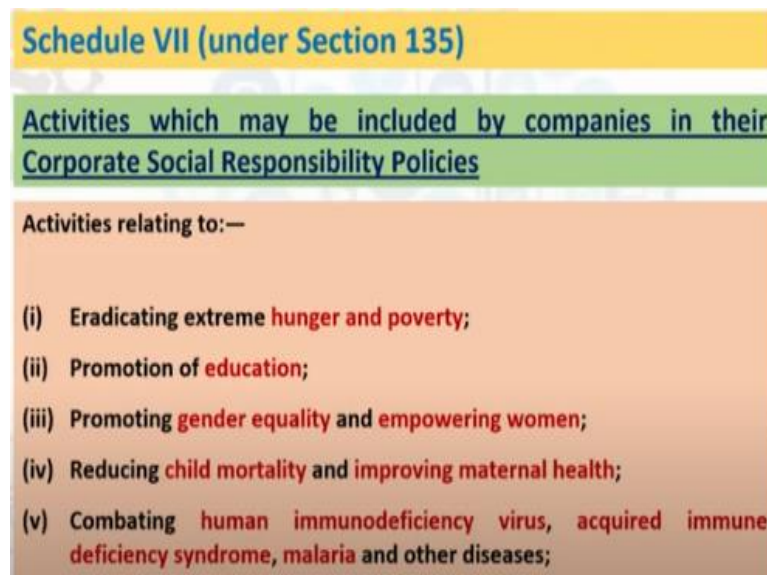
At least you are giving him room to create a provision and do it. By forcing somebody they will be jailed if you do not do then you will not get directors to be in the board, no person of value would join a board. Today, there is a huge dearth of independent directors in corporates because of this reason.

Criminalization of non-compliance which are not related to do with any fraud or anything, even procedural noncompliance has been treated as criminal offenses. Procedural noncompliance, non-filing of returns. Like CSR expenses not complied with 2%. Non-disclosure of events. Who are to be criminally prosecuted, the directors. And therefore, directors of any repute were saying we do not want to be directors in the board.

Finally the government understood, the ministry understood, and it has been totally decriminalized now. None of these provisions contain now anything to do with criminal prosecution for noncompliance of procedural matters like this. If there is a violation of environmental laws with the violation of Air Pollution Control Act, Water Pollution Control Act, hazardous waste management rules, of course section 37 is very clear.

It was earlier, even now. The occupier of the factory, the directors, the independent directors, all can be criminally prosecuted, can be. That provision is welcome provision. That should be there, but not procedural noncompliance. A form has to be filed within 30 days. If has not been filed within 30 days, then a director will be pulled to jail for that. Can it happen? Similarly this 2% provision was there. Now it has been removed.

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Activities relating to. These are the activities, very broad. Eradicating extreme hunger and poverty. Can anybody make out what can be a CSR for that? These are the activities. Eradicating extreme hunger and poverty, any activity. Promotion of education. Promoting gender equality, empowering women. Reducing child mortality, improving mental health, sorry maternal health. Combating human immunodeficiency virus.

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Schedule VII (under Section 135)

Activities which may be included by companies in their Corporate Social Responsibility Policies

- (vi) Ensuring environmental sustainability;
- (vii) Employment enhancing vocational skills;
- (viii) Social business projects;
- (ix) Contribution to the Prime Minister's National Relief Fund or any other fund set up by the Central Government or the State Governments for socio-economic development and relief and funds for the welfare of the Scheduled Castes, the Scheduled Tribes, other backward classes, minorities and women; and
- (x) Such other matters as may be prescribed.

So generalized social business projects. PM relief fund, of course other things are there. Such other matters as may be prescribed. Now whenever you keep it too open there are positive and negative side of it. First of all, it should not have been there. It is not required at all. Corporate should do it on their own. Create environment for that.

And even if you are doing it and keeping it such wider interpretation and open, actually it becomes lot for interpretation and discretion. When it comes to interpretation and discretion, what comes is corruption. The moment you leave things for interpretation and discretion, you are inviting corruption or unethical means. That is exactly where it needs to be introspected, redone and revisited.

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7 Deadly Sins as rightly preached by Mahatma Gandhi

Mahatma Gandhi said that seven things will destroy us. Each of these deadly sins (as noted down below) is an explicit external standard or something that is based on natural principles and laws, not on social values.

- Wealth Without Work
- Pleasure Without Conscience
- Knowledge Without Character
- Commerce (Business) Without Morality (Ethics)
- Science Without Humanity
- Religion Without Sacrifice
- Politics Without Principle



I mean, this is something which I found very interesting, old sayings that natural principles and law, be good. Be good cannot be defined. This is what you need to do. Early morning yoga, good diet. I mean there are no prescription for this. It should come from within. Value systems should be from within. For business create the environment, value system is bound to happen.

No one will be able to sustain if they do not do CSR. That should be the system. Employees will reject to work in a company which does not follow CSR. We have seen recruitments of GATs in various Management Institutes and some of the GATs which join Management Institutes when you go for interviews, I have been invited in number of cases, many things they ask.

One of the things now they are asking is how is the company faring in ESG parameters? I never thought to five years back somebody will be asking this question. Takes us back to the Mahatma Gandhi days when he talks of social good. Growth, inclusive growth. Business to take care of society. Business of business yes is to do business, but with social good.

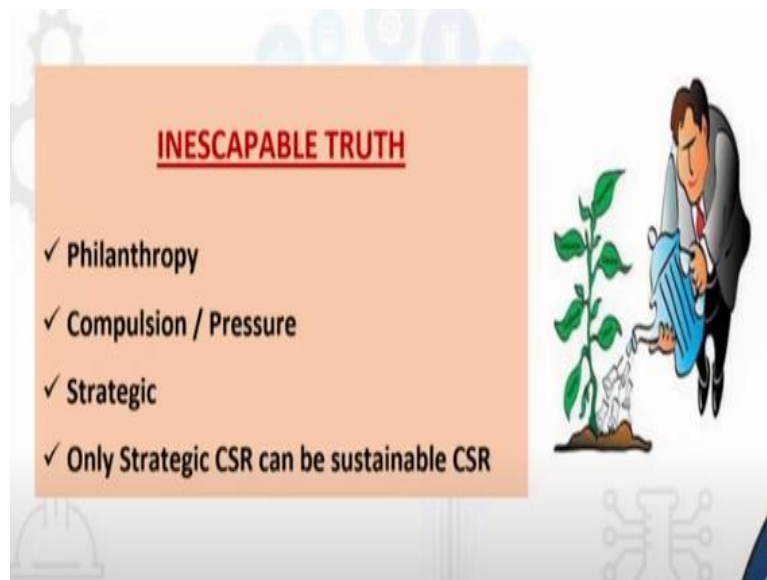
So when these young minds ask questions on ESG then corporate social responsibility would be very soon imbibed in the corporate philosophy or strategy. There is no way out. No one can, no corporate can sustain without ESG.

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Tax is another example also because you have to give some leeway to corporate social responsibility, those who are doing that 2%. Some leeway is required. Some tax relief is required extra, those who are doing corporate social responsibility. This was a talk long time going but government has not paid any heed to this. They reduce the corporate tax rate they might say for that they have reduced a corporate tax rate to some extent.

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Now what is very important and close to me is that I always say this is that CSR to be strategic has to be strategic to be sustainable. And there are three types of CSR; philanthropic, compulsion, and strategic. Philanthropy is only one way. We corporates donate, corporate does charity. Corporates are requested to do charity. Corporates are requested to contribute, one-time contributions, philanthropy.

Do and forget. Do not think of any return. Do not think of anything else. But this is a one way traffic, which time to time every corporate has done, will do. It is the need of the hour. It is the call of the time. It is the call of the nation. That COVID crisis, each and every corporate responsible have contributed, generously. And that contribution is a philanthropy.

That contribution is a call of the nation. No one will ever speak of that. That was the need that will be done. Maybe too little, could have been much more but has been done silently by responsible corporates. That is philanthropy. Compulsion and pressure. This is again something which is not desirable at all.

There was a time when some corporates in the south near the river Perrier were releasing toxic water in the river and one of the very big MNCs were doing it. And somehow they were able to manage everything. But group of people who are affected by that water filed a petition. It was before the Green Tribunal and finally that MNC with all its power, all its power could not stop the closure of that unit.

The unit was closed permanently and in that judgment, the judge quoted pollute and pay is not what is to be allowed. You pollute and you pay the damages. You cannot continue to do this. But all this happened because of a pressure of a compulsion, not there on their own. People went and filed a litigation, a petition kind of thing before the Green Tribunal.

Philanthropy is something which will happen, continue to happen, is good. Compulsion/pressure, not desirable. Should happen on own. But again, something which is going to happen cannot be stopped because there will be some cases where people will not listen. So pressure group has to work and make it happen.

But strategic is something which is going to happen and going to take basically to the next level of corporate social responsibility. Examples of those can be many. One is the very famous example, which is given everywhere perhaps, is the ITCs each of all.

The old one where ITC used to go and develop the village panchayats young folks to understand how they can immediately inform them when they are ready with their produce. They do not have to engage anybody or store their produce in the warehouses of the mahajans, the intermediaries. Kiosks were given to them, established.

Lot of money was spent by ITC to give those to them, so that when they are ready, they could inform that this much is ready for with them. I mean, they would reach the ITCs buying team directly. So what they were getting was 9 rupees if we consider that as 9 and ITC was paying 12. The intermediary was getting 3. ITC paying however the former getting 9.

Now with these kiosks, they do not have to store anywhere. ITC brought down the price to 11. The farmer was getting 9. So farmer gained from 9 to 11. ITC gained from 12 to 11. And the intermediary in between, undesirable entity in the whole process was knocked down. A perfect example where the investment in the kiosks, the extensive survey done by ITC, the learning they spread around all, the perseverance they showed finally gave them and continued to give them returns, sustainable.

And this is given as an example everywhere. Another organization, Apollo Tyres is also done us wonderful strategic exercise in upliftment and development of the truck driver community knowing fully well that this truck drivers are the greatest advertisers of tyres.

So taking care of their health, ensuring that they get checkups regularly and tying up with the dhabas, roadside dhabas, to give them various medical aids, protections, and even during vaccination, doing that drive, ensuring they are vaccinated. So these are all strategic investments. And finally, this gives return. CSR can never be a charity. Philanthropy one time, CSR to be sustainable, has to be strategic.

It has to be win-win. There are so many models which can be, even Lijjat Papad is a classic example of sustainable CSR. Taking care of the entire village, the women are not doing anything other than Lijjat Papad. That entire village women are taking care of; their health, the children education. They do not have to think left, right, center, anything.

Just Lijjat Papad making. There are some models are being even developed today to see to it that it becomes sustainable both ways. Research is required in this. Various business houses are working on it so that CSR is actually becomes a DNA of a corporate's business. That would be the time when CSR would be totally sustainable. And we do not have to go on talking about CSR and 2%.

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That is all what I want to share with you on CSR. Thank you.