CSR

NORMS AND PRACTICES

FROM POLICY TO PRACTICE: UNDERSTANDING CSR GOVERNANCE

Financial Management Service Foundation
Promoting Accountability
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I. INTRODUCTION

In India, engagement with charity and social good has deep roots. For centuries, giving back to society has been guided by our history, cultural values, and ethical principles drawn from various religious philosophies. Ideas such as responsible stewardship of wealth, supporting local communities, and viewing resources as belonging to society at large have shaped Indian business behaviour long before the modern term "CSR" existed. Yet, these contributions were largely voluntary and unstructured. Every organisation followed its own understanding of what social responsibility meant. This landscape changed with the introduction of mandatory Corporate Social Responsibility under the Companies Act, 2013. India became one of the few countries to provide a statutory framework for CSR. The law did more than define eligibility thresholds. It placed strong emphasis on governance. The intention was clear to shift CSR from scattered individual efforts to a structured and accountable system that reflects national priorities and ensures responsible use of corporate resources.

In previous issues of the CSR Norms & Practices series, we explored the background and applicability of CSR, the scope of eligible expenditure, and the practical aspects of fund utilisation. With this issue, we move to the next stage which is understanding CSR governance. This edition provides an analytical understanding of the CSR framework under the law, and what systems need to be in place for CSR to be implemented effectively, consistently, and responsibly.

The Issue 4 of the series titled, "From Policy to Practice: Understanding CSR Governance", examines how this framework is actually operationalised within companies. It explores the formation and functioning of the CSR Committee, the formulation and approval of the CSR Policy, and the statutory obligations of the Board in relation to implementation, monitoring, reporting, and disclosure of CSR activities. The objective is to provide an understanding of how the Board, as the apex authority, ensures that CSR initiatives are executed effectively within the legal and ethical framework, while related provisions on transparency, accountability, and compliance together strengthen the overall architecture of CSR governance in India.

II. CSR COMMITTEE

The foundation of an effective CSR framework lies in the establishment of a dedicated Corporate Social Responsibility (CSR) Committee. A CSR Committee (Corporate Social Responsibility Committee) is a statutory Board-level committee mandated under the Companies Act, 2013 for eligible companies. It forms part of the company's governance structure and is constituted by the Board of Directors to provide oversight related to the organisation's CSR obligations. It is not an independent body but an integral component of the Board's formal governance framework.

Rule 2(e) of The Companies (Corporate Social Responsibility Policy) Rules, 2014: "CSR Committee" means the Corporate Social Responsibility Committee of the Board referred to in section 135 of the Act

a. Applicability of CSR Committee:

Rule 3(1) of The Companies (CSR Policy) Rules, 2014, states that every company including its holding or subsidiary, and a foreign company defined under clause (42) of section 2 of the Act having its branch office or project office in India, which fulfills the criteria specified in sub-section (1) of section 135 of the Act shall constitute a Corporate Social Responsibility Committee.

Further, a company that has any amount in its Unspent CSR Account of a financial year with regard to an ongoing project, shall also be required to constitute a CSR Committee and comply with the relevant provisions. (Proviso inserted to Rule 3(1) of Companies (CSR Policy) Amendment Rules, 2022.)

Section 2(42) of Companies Act, 2013:
"foreign company" means any company or body corporate incorporated outside India which
(a) has a place of business in India whether by itself or through an agent, physically or through electronic mode; and
(b) conducts any business activity in India in any other manner.

b. Composition Requirements:

Based on the applicability discussed above, in case a company is required to form a CSR Committee, it needs to take into consideration the following composition requirements that are laid down under Rule 5 of The Companies (CSR Policy) Rules, 2014:

- Every company (except those discussed below) who is mandated under law to carry out CSR activities as per Section 135(1) of the Companies Act, 2013, shall have to constitute a CSR Committee of the Board consisting of three or more directors, of which at least one director should be an independent director.
- When a company is not required to appoint an independent director under section 149(4) of the Act, i.e. unlisted public company or a private limited company, it may constitute its CSR Committee with two or more directors, without an independent director.
- A private company having only two directors on its Board shall constitute its CSR Committee with two such directors.
- In the case of a foreign company, the CSR Committee shall consist of at least two people, one as specified under Section 380(1)(d) of the Act, i.e. the person authorized to accept on behalf of the company any notices or other documents required to be served on the company, and another nominated by the foreign company.

Note – Independent Director is a director of a company who does not have any material or pecuniary relationship with the company or its promoters, management, or subsidiaries, other than receiving director's remuneration. They are expected to act impartially and help in corporate governance and board oversight. Section 149(6) of the Companies Act, 2013 defines an independent director.

Section 149(4) of the Companies Act, 2013 states that every listed public company shall have at least one-third of the total number of Directors as independent Directors and the Central Government may prescribe the minimum number of independent Directors in case of any class or classes of public companies.

Under Section 135(2) of the Companies Act, 2013, every company to which CSR provisions apply must disclose the composition of its CSR Committee in the Board's Report.

c. Role of CSR Committee:

Once the CSR Committee is formed, certain Roles & Responsibilities are to be undertaken by the said Committee, which are laid down under Section 135(3) of the Act & Rule 5(2) of the CSR Rules. These roles are with regard to developing an annual action plan as well as other such matters related to the CSR Policy, which are discussed as under:

- The Committee is responsible to formulate and recommend to the board, a CSR Policy which shall indicate the list of CSR activities, projects or programmes, to be undertaken by the company, in the areas that are approved under Schedule VII of the Act.

- It would recommend the amount of expenditure to be incurred based on the activities suggested as above.

- It would formulate the manner of implementation of such projects, as allowed in Rule 4(1), e.g., whether the CSR activities would be undertaken by itself or through an organisation established for the same, via an existing organisation having a track record of at least 3 years or an entity established under Act of Parliament or a state of legislature, etc., as allowed under Schedule VII of the Act. (The modalities of implementation of CSR projects are discussed in detail in earlier issues of CSR Norms & Practices, which can be referred to for detailed understanding.)

- It would suggest the modalities of utilisation of funds and implementation schedules for the projects.

- It would develop a monitoring and reporting mechanism for the suggested projects.

- It would develop a need and an impact assessment plan, if any, for the projects undertaken by the company.

- It would monitor the CSR policy of the company, from time to time, to incorporate changes, if required.

The board is allowed to alter the said plan at any time during the financial year, as per the recommendation of its CSR Committee, based on the need and on providing a reasonable justification for the same.

d. Exception to formation of CSR Committee:

In order to provide relief to companies that do not have substantial CSR expenditure, Section 135(9) of the Act provides that in cases where the amount to be spent by a company on CSR activities does not exceed ₹50 lakhs, the requirement to constitute a CSR Committee shall not apply, and the functions of the Committee shall be discharged by the Board of Directors itself. However, the circumstances in which a company may discontinue its CSR Committee need to be assessed with caution. The exemption is linked to the CSR liability in that particular financial year. If the prescribed CSR obligation for the year exceeds the specified limit, the company must retain or constitute a CSR Committee, even if its actual spending is lower than ₹50 lakhs.

e. Quorum of CSR Committee:

Paragraph 3.5 of the Secretarial Standards on Board Meetings (SS-1) issued by The Institute of Company Secretaries of India (ICSI) states that the Board may decide the quorum for any of its committees. If the Board has not specified a quorum, then all members of the committee must be present for the meeting to be valid. Therefore, in the absence of a specified quorum for the CSR Committee, every member's presence is required to constitute the meeting.

f. CSR Committee for Group Companies:

CSR requirements under the Companies Act apply separately to each company. Therefore, any company that meets the criteria under Section 135(1) of the Act is required to form its own CSR Committee. Nevertheless, companies in a group can coordinate their CSR policies and activities with a group-level framework, as long as it adheres to the provisions of the Act.

III. CSR POLICY:

A CSR Policy is a formal Board-approved statement. It sets out a company's overall approach, priorities, and guiding principles for Corporate Social Responsibility. This includes the activities a company will undertake, how these will be implemented and monitored, and how the required CSR spending will be applied in line with the law. In view of this, the law has laid down certain provisions which are discussed below:

Rule 2(f) of Companies (CSR Policy) Rules, 2014:

"CSR Policy means a statement containing the approach and direction given by the board of a company, taking into account 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 definition of CSR Policy was revised through the Companies (CSR Policy) Amendment Rules, 2021, notified on 22 January 2021. Companies that were already subject to CSR provisions before this amendment had to revise their existing CSR Policy to align with the updated requirements. The revised policy had to incorporate, among other elements, the guiding principles for selecting, executing, and monitoring CSR activities, as well as the framework for preparing the annual action plan.

a. Purpose of CSR Policy:

A CSR Policy is prepared to provide a structured and transparent framework for a company's CSR initiatives. It ensures that the company's CSR efforts are aligned with its core values, legal obligations, and national development priorities. By formulating this policy, the Board of Directors and the CSR Committee can clearly define objectives, set measurable goals, and establish accountability mechanisms for CSR implementation.

Moreover, a well-defined CSR Policy promotes consistency in decision-making, enhances stakeholder trust, and enables the company to monitor and evaluate the impact of its CSR activities effectively. In essence, the policy serves as a strategic roadmap that guides the organization in fulfilling its social and ethical responsibilities in a systematic and compliant manner.

b. Drafting of CSR Policy:

The CSR Rules require companies to include guiding principles in their CSR Policy, which serve as broad indicators of the areas in which CSR initiatives will be undertaken. These principles operate at a strategic level and are further detailed each year in the company's annual action plan. Illustrative guiding principles may include:

- Selection of CSR Projects: Key parameters to be considered that influence project choice. These may include identifying the priority themes, assessing needs within the local area or other regions requiring intervention, recognising projects of national significance. The principles may also indicate how CSR funds will be allocated across these priorities to ensure that the company's initiatives generate a meaningful and positive impact.

- Implementation Approach: The manner in which CSR activities will be carried out, whether directly by the company or through an implementing agency. This may include criteria for selecting implementing partners, such as the absence of conflicts of interest, non-political background, due diligence outcomes, and performance history.

- Monitoring Mechanisms: The processes for tracking progress, including review frequency, need for field visits, persons responsible for oversight, and types of documentation or evidence to be collected to assess implementation.

- Formulation of Annual Action Plan: Considerations for preparing the plan, such as choosing between long-term or short-term projects, evaluating environmental or regulatory requirements, assessing project suitability, and determining the timelines or frequency for impact assessments.

Before the amendments to the CSR Rules, a CSR Policy was expected to contain detailed information such as the list of proposed CSR activities, execution modalities, implementation timelines, and monitoring arrangements. Following the Companies (CSR Policy) Amendment Rules, 2021, notified on 22 January 2021, these operational details are now intended to be part of the annual action plan, while the CSR Policy provides the overarching framework and direction.

c. Suggestive structure of a CSR Policy:

- Purpose: States the company's CSR intent, the meeting in which the Policy was approved by the Board, its alignment with the company's vision. It should also confirm that the Policy is framed in compliance with section 135 of the Companies Act and the CSR Rules.

- Effective Date: The financial year from which the Policy becomes applicable should be clearly stated.

- Definitions: Key terms used in the Policy should be mentioned as defined under the Companies Act and the CSR Rules.
- Functions of CSR Committee: The policy should cover the Committee's responsibilities, including drafting the CSR Policy, preparing and recommending the annual action plan, suggesting budgets, monitoring implementation, and proposing changes as required.
- CSR Activities: Lists the activities permitted under Schedule VII and any additional activities, approved by the Board in line with legal provisions.
- Focus Areas: Highlight priority sectors such as health, environment, water, rural development, education etc.
- Annual Action Plan: The policy should state that the annual plan shall be prepared by the CSR Committee and recommended to the Board, with provisions for the Board to modify it during the year if justified.
- CSR Spending: Specify the annual CSR allocation, how surplus will be used, the requirement for pre-approval of expenditure, and the treatment of unspent amounts.
- Modes of Implementation: Explain how CSR work will be carried out, either direct implementation, or through registered implementing agencies, through company-established foundations, or in collaboration with other organisations.
- Need and Impact Assessment: Provide for conducting need assessment before initiating a project and impact assessment after completion, with the results placed before the Board.
- Capital Assets: Clarify ownership and custodianship of CSR assets and ensures such assets are used for the intended beneficiaries.
- Information Dissemination: Mandate the upload of the CSR Policy and annual CSR information on the company website and to be published in the annual return of the company.
- Review: The clause related to periodic review and revision of the Policy by the CSR Committee and the Board, based on legal requirements and operational needs should also be included.

A well-structured CSR Policy ensures compliance with the statutory requirements and reflects the organisation's broader vision, mission and goals.

d. Spending on Activities Outside the Existing CSR Policy:

Section 135(5) of the Act requires that the company's CSR expenditure be carried out strictly in line with its approved CSR Policy. When a company intends to support any activity that is permitted under Schedule VII but is not currently reflected in its CSR Policy, it must first revise the Policy to include that activity. This update must be approved by the Board, ensuring that the proposed activity becomes an integral part of the company's CSR framework. Only after such incorporation can the company validly allocate and utilise CSR funds for those additional programmes or projects.

e. Annual Action Plan:

An Annual Action Plan is a yearly roadmap that outlines the specific CSR projects a company will undertake, along with how those projects will be implemented, monitored, and funded during that financial year. It translates the broader principles of the CSR Policy into concrete steps, listing the activities, timelines, responsibilities, and expected outcomes.

The annual action plan is updated every financial year, as it reflects the guiding principles set out in the CSR Policy and their relevance for that particular year. The plan should also indicate the expected results for the next financial year. For instance, elements may include:

- List of CSR programmes or broad criteria about what constitute a CSR project that align with priority areas and are likely to create meaningful impact.

- Execution framework, such as the allocation of funds for each project during the current year, projected spending for the next year, and identification of implementing agencies etc.

- Fund-utilisation modalities, including the stages at which funds will be released (for example, disbursement upon completion of specific milestones).

- Monitoring and reporting mechanisms, such as engagement of external agencies for verification, along with defined frequency and parameters for review.

- Impact assessment arrangements, specifying who will conduct the assessment, the projects covered, and the timelines.

As per Rule 5(2) of The Companies (CSR Policy) Rules, 2014

The CSR Committee shall formulate and recommend to the Board, an annual action plan in pursuance of its CSR Policy, which shall include the following, namely:-

(a) the list of CSR projects or programmes that are approved to be undertaken in areas or subjects specified in Schedule VII of the Act;
(b) the manner of execution of such projects or programmes as specified in sub-rule (1) of rule 4;
(c) the modalities of utilisation of funds and implementation schedules for the projects or programmes;
(d) monitoring and reporting mechanism for the projects or programmes; and
(e) details of need and impact assessment, if any, for the projects undertaken by the company:

Provided that Board may alter such plan at any time during the financial year, as per the recommendation of its CSR Committee, based on the reasonable justification to that effect.

f. Disclosure:

The Board of Directors of the Company shall mandatorily disclose the CSR Policy approved by the Board on company's website, if any, for public access.

IV. ROLE OF BOARD OF THE COMPANY:

The Companies Act, 2013 and Companies (CSR Policy) Rules, 2014 collectively establish that the Board of Directors of a company are the central authority responsible for CSR governance. The Board must ensure that CSR initiatives are strategically planned, properly implemented, financially sound, and transparently reported. Accordingly, the Board's roles and responsibilities includes:

a. Approval and Disclosure of CSR Policy:

The Board of every company that is required to carry out CSR activities, approve the CSR Policy for the company, after taking into account the recommendations of the CSR Committee. It is also required to disclose the contents of the CSR Policy in the Board's report and place the same on the company's website, if any, in such a manner that the company's CSR intent and focus areas are transparent and publicly accessible.

Section 135(4) of the Companies Act, 2013 states:

The Board of every company referred to in sub-section (1) shall,

(a) after taking into account the recommendations made by the Corporate Social Responsibility Committee, approve the Corporate Social Responsibility Policy for the company and disclose contents of such Policy in its report and also place it on the company's website, if any, in such manner as may be prescribed; and
(b) ensure that the activities as are included in Corporate Social Responsibility Policy of the company are undertaken by the company.

b. Annual Action Plan:

Approve the annual CSR action plan recommended by the CSR Committee, including any amendments during the financial year.

c. Implementation & Monitoring of CSR Activities:

The Board shall ensure that the activities included in the approved CSR Policy are actually undertaken by the company.

Further, in the case of ongoing projects, as per Rule 4(6) of The Companies (CSR Policy) Rules, 2014, the Board is required to monitor the implementation of the project, with reference to approved timelines and year-wise allocation. The Board is allowed to make modifications, if required, to ensure smooth implementation of the project within the overall permissible time period. This ensures proper governance over long-term CSR commitments.

Rule 4(5) of The Companies (CSR Policy) Rules, 2014

The Board of a company shall satisfy itself that the funds so disbursed have been utilised for the purposes and in the manner as approved by it and the Chief Financial Officer or the person responsible for financial management shall certify to the effect.

d. Mandatory CSR Expenditure:

The Board must ensure that the company meets the statutory requirement of the CSR expenditure, in every financial year, i.e. it spends at least 2% percent of the average net profits of the company made during the three immediately preceding financial years, or such shorter period as applicable, in accordance with the CSR Policy.

If the company fails to spend the stipulated amount in any financial year, the Board is responsible to specify the reasons for the same in its report. Further, unless the said unspent amount relates to an ongoing project, the Board should make sure that such unspent amount is transferred to a Fund specified in Schedule VII within six months from the end of the financial year.

Section 134(3)(o) of Companies Act, 2013:
"the details about the policy developed and implemented by the company on corporate social responsibility initiatives taken during the year;"

e. Financial Prudence:

While carrying out CSR activities, it is expected that the company acts prudently with regard to its finances. Thus, Rule 7(1) of the CSR Rules lay down the responsibility on the Board to ensure that administrative overheads do not exceed 5% of the total CSR expenditure of the company for the financial year. It is worthwhile to mention that the said 5% cap on administrative overheads is applicable only to the company. It does not apply to the administrative or operational expenses incurred by implementing agencies. This provision is discussed in detail in the earlier issues of CSR Norms & Practices, which can be referred to for further insight.

f. CSR Surplus:

The Board must ensure that any surplus arising from CSR activities shall either be reinvested into the same project, transferred to the unspent CSR account for utilization in accordance with the company's CSR Policy and annual action plan, or deposited into a fund specified in Schedule VII of the Act, within six months from the end of the financial year.

g. Impact Assessment:

The Board shall ensure that an independent impact assessment is conducted for CSR projects wherever applicable. It shall review the reports of such assessments and annex them to the annual CSR report. While approving projects, the Board shall consider the identified need for the project as a key parameter, ensuring that the assessment measures the effectiveness and outcomes of the CSR initiatives.

h. Reporting and Disclosure Obligations:

Accurate and transparent disclosure of CSR initiatives is a key governance obligation of the Board. Thus, as per Rule 8(1) of the CSR rules, the board of the company is required to include an annual CSR report in the Board's Report, providing details as required under the CSR Rules.This disclosure forms part of the statutory reporting obligations under the Act.

i. Section 166 of the Act:

Section 166(2) of the Act further places responsibility on the directors of the company, requiring them to act in good faith in order to promote the objects of the company for the benefit of the community & for the protection of the environment, apart from its employees and shareholders.

V. CONCLUSION

The CSR framework under the Companies Act, 2013 places the Board of Directors at the core of responsibility for ensuring that CSR commitments are fulfilled both in compliance and in spirit. While the CSR Committee acts as a recommending and monitoring body, the Board bears the ultimate accountability for the planning, approval, execution, and oversight of CSR activities. Compliance with the statutory provisions not only safeguards the company from legal exposure but also enhances its goodwill, reputation, and commitment towards sustainable and inclusive growth. A well-structured CSR policy, coupled with proactive Board engagement, transparent reporting, and diligent monitoring, reinforces stakeholder confidence and enhances the company's role as a responsible corporate citizen. Thus, effective CSR governance under the stewardship of the Board plays a crucial role in translating corporate intent into tangible social impact.

Creating a strong business and building a better world are not conflicting goals – they are both essential ingredients for long-term success.

- Bill Ford

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