E-Book

Corporate Social Responsibility

The Institute of Chartered Accountants of India

(Set up by an Act of Parliament)

Southern India Regional Council

Chennai

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This e-book has been authored by

CA. Venkata Kali Prasad Malapaka

The Institute of Chartered Accountants of India
(Set up by an Act of Parliament)
Southern India Regional Council
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Post Box No. 3314, Nungambakkam,
Chennai - 600034

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FOREWORD

Corporate Social responsibility (CSR) refers to practices and policies undertaken by corporations intended to have a positive influence on the world. CSR is the concept that a business has a responsibility to do well. CSR means that a company should self-regulate its actions and be socially accountable to its customers, stakeholders, and the world at large.

The key idea behind CSR is for corporations to pursue other pro-social objectives, in addition to maximizing profits. Examples of common CSR objectives include minimizing environmental externalities, promoting volunteerism among company employees, and donating to charity.

This e-book provides in-depth knowledge on the topic of Corporate Social Responsibility detailing the meaning, specific provisions/compliances under the regulations to comply with the legal requirements which the corporates are mandated. It also provides insights on the accounting and recognition aspects, penal implications on non-compliances, requirements of Audit and responsibility of auditors towards Corporate Social Responsibility activities, reporting, disclosure requirements and tax benefits for Corporate Social Responsibility activities.

The e-book also contains relevant templates, format for annual reporting of Corporate Social Responsibility activities and other Annexures, provisions relevant to determine the activities which could be eligible for Corporate Social Responsibility, companies for whom the same is mandatory, etc.

On behalf of SIRC, I wish to place our sincere gratitude and appreciation to CA. Venkata Kali Prasad Malapaka, for sharing his rich experience and expertise on the Corporate Social Responsibility amongst our members through this e-book. I also take the privilege of thanking CA. Vijayasundhar S I for reviewing the basic draft of e-book and adding value to the substance of the e-book.

We are conscious of the fact that in a publication meant for professional accountants like this there is a scope for further improving form, contents, presentation and coverage. Accordingly comments and suggestions on the e-book are welcome at sirc@icai.in

CA.China Masthan Talakayala
Chairman, SIRC of ICAI

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BACKGROUND

India is a developing country with lots of negative aspects; biggest of them being population. The ailments such as hunger, poor living conditions, malnutrition, lack of education, basic amenities etc. are the result of this. Government of India has the responsibility of good governance, which includes uplifting of the standards of living. Lot has been done in this regard and much more is to be done.

Laying of roads, providing electricity, potable drinking water, hygiene, health, education, food, are but a few of the priorities of the Government.

Government is run by a set of parliamentarians who focus on the concept of Governance and taking a macro view of the situations such as improving the infrastructure, building of irrigation projects, dams, laying of highways, defense, science and technology so on. Not many of these parliamentarians have management skills and innovative thoughts.

In this backdrop, The Government has hit upon an idea to involve the corporates to help the Government with focus on localized requirements and meeting the need of the people. ***The idea is to utilise the innovations and management skills of the corporate sector rather than merely funding of the activities of the Government.***

Chapter 1:

CORPORATE SOCIAL RESPONSIBILITY

As a sequel, necessary amendments have been made in The Companies Act 2013 incorporating the guidelines for Corporate Social Responsibility. S.135 has been included laying down the broad framework of corporate social responsibility and relevant rules have been formulated as CSR rules 2014. This section and the rules made thereunder lay down the principles and regulations for implementation of CSR in India

OBJECTIVE OF CSR

The objective of corporate social responsibility is to involve the corporate sector in the nation building activity by utilizing the innovative thinking and management skills to compliment the objective of social upliftment. As a result, the society and the living conditions would improve. Poor people would get a helping hand. The Government shall not involve directly or indirectly in the CSR activities of the Company in any manner.

Chapter 2:

LEGAL PROVISIONS:

S.135 of The Companies Act provides for COPORATE SOCIAL RESPONSIBILITY (CSR). CSR rules 2014 have been notified to ease the implementation of the scheme. These two enactments govern the implementation of CSR by Companies.

1. **Applicability:**

   Section 135 of the Companies Act, 2013 [The Act], requires the board of directors of every company having

   a. **A Net Worth of Rs. 500 Crore or more**
   b. **Or Turnover of Rs. 1,000 Crore or more**
   c. **Or A Net Profit of Rs. 5 Crore or more**

during the immediate preceding financial year to constitute a Corporate Social Responsibility (CSR) Committee of the board. The word used in between is **"or"** which makes the above provisions are alternative and not cumulative. A company would have to fulfill theprovisions If any one of the above conditions are applicable,

Implications of the words used: Net worth of Rs.500 crores

As per S.2 (57) of the Companies Act, 2013: The term net worth is the aggregate value of the paid-up share capital and all reserves created out of the profits and securities premium account, after deducting

A) the aggregate value of the accumulated losses,

B) deferred expenditure and

C) miscellaneous expenditure not written off,

as per the audited balance sheet but does not include reserves created out of revaluation of assets, write-back of depreciation and amalgamation.

Fresh Issue or buyback of share capital during the year:

The term used says " ... net worth of Rs 500 Crores at any time during the year" implying that the net worth being more than RS.500 Crores before the buy-back of shares or after the fresh issue of shares.

If a fresh share issue is made during the year and the paid up capital is increased, the increased capital is to be considered.

If there is a reduction in capital, capital before reduction is to be considered

Note: **But, the concept of deferred revenue expenditure and misc expenses do not existany more since the provisions of AS 26**

// para appears incomplete//

Turnover of Rs.1000 crores

> Section 2(91) of the Companies Act, 2013 defines “turnover” to mean **the aggregate value of the *realisation* of amount made from the sale, supply or distribution of goods or on account of services rendered**, or both, by the company during a financial year.

The provision suggests that the consideration is realisation rather than actual sales during the year. Cashflow from operations would be the consideration.

Net Profit of Rs. 5 Crore or more

For this purpose, Profit is net profit as calculated in accordance with S.198 of the Companies Act. Extraneous profits/ losses are to be excluded. Income tax is to be excluded. Any windfall or any loss due to unavoidable circumstances to be eliminated.

Ideally profit before Tax (PBT) is to be considered.

Chapter 3:

CORPORATE SOCIAL RESPONSIBILITY COMMITTEE

The provisions lay down that any company fulfilling any of the above conditions shall constitute a CSR Committee. The requirements are as under:

For listed companies	Not less than three directors, of which at least one of the directors to be independent director
Unlisted companies	
With independent director:	As above
Without independent director:	Two or more directors
Private Companies:	Two or more directors
Foreign company:	Two or more directors, of which one is an Indian Director Others nominated by the Foreign Company

Constitution of CSR committee is not mandatory where the amount spent on CSR is less than Rs.50 lakhs. Board of directors can discharge the functions.

Composition of the CSR committee and the dates of meetings are to be mentioned in the directors' report of the Company. Details of the committee and the projects undertaken under CSR are to be stated in the website.

FREQUENCY OF MEETINGS OF THE CSR COMMITTEE

Law has not specified any stipulations with regard to meetings of the Committee. The Board of directors may stipulate the frequency of meeting of the CSR Committee. Secretarial standards state that the committees of the Board should conduct at least 4 meetings in a year. The same principles apply to this committee also

FUNCTIONS OF THE CSR COMMITTEE:

The Committee is constituted with the following responsibilities.

- To formulate and recommend to the Board, a CSR Policy which shall indicate the activities to be undertaken by the company as specified in Schedule VII of the Act.
- To recommend the amount of expenditure to be incurred on the CSR activities.
- To monitor the CSR policy of the company from time to time.
- Formulate and recommend to the board the annual action plan in pursuance of rthe CSR policy.

BOARDS RESPONSIBILITIES:

The Board of directors of the Company is laden with the responsibility of considering and approving the recommendations of the CSR committee. After the policy is finalised, it is to be disclosed in the website of the Company. The BOD is alo requird to ensure that the activities are, in fact, carried out and the expenditure is in line with the legal requirements. The details are to be filed in the Anual report of the Company.

GUIDELINES ON EXPENDITURE

There should be actual expenditure on CSR. Monetary value of any assets transferred to the CSR project is not considered to be CSR expenditure. The Company should layout at least 2% of the average Net Profits of the company during the three immediate preceding financial years towards corporate responsibility spending. In case a company has not completed three financial years since its incorporation, the average net Profits shall be calculated for the financial years since its incorporation. The term "average profits" implies simple average profits.

Administrative expenses cannot be more than 5% of the project expenditure.
Involvement of the employees of the Company is encouraged but their salaries cannot be part of CSR.

The Company may choose multiple projects with different partners.

ELIGIBLE PROJECTS:
CSR rules lay down the eligible projects for implementing the activity. The Company may opt to carry out multiple projects as CSR. However, each of the projects is to be monitored and reported separately.

GEOGRAPHICAL AREA OF ACTIVITY
The Company shall carry out the CSR in the geographical area of operations of the Company, be it plant, corporate office, branch office. Etc. Exception to the rule where the activity can be beyond the boundaries are such as welfare of war widows, development of art and culture etc. or the training and development of skills of a national or state level player outside India.

Chapter 4:

MODE OF IMPLEMENTATION:

Schedule VII of The Companies Act lays down the guidelines for implementing the CSR.

CSR may be implemented by the Corporates in multiple ways be it directly taken up by the Company or in collaboration with other corporates. The Company might as well choose to collaborate with other organizations permissible as per schedule VII of the Companies Act, 2013. The other permissible means is to contribute to the approved funds as per Schedule VII. The Actlays down certain conditions wherein the corporate may carry out the social responsibilitythrough a third party.

Implementing directly by the company

It is a stupendous task to carry out the CSR activities by any Company. The likely posers are:
Significant effort is required on the part of the management to identify the line of activity and the geographical location.
The activity consumes substantial time and effort, which may eat in to the time to be allocated for pursuing the objectives of the Company.
Carrying out the activity is one aspect and monitoring and reporting on the activity is another. Funding the activities may pose quite a problem. However it gives the satisfaction of helping the society.

Collaborating with another corporate(s)

The next option available is to collaborate with another one or more corporate(s) to carry out the responsibility. Since two or more corporates are jointly carrying out the project, larger projects may be taken up. Responsibilities can be shared among the corporates. It leads to ease of implementing the projects.

A separate SPV may be created to implement the CSR activities. The modalities, roles and responsibilities of the partner corporates are to be scripted. Minutes of the meetings are to be recorded for smooth functioning and implementation of the projects. Management of the SPV will be accountable to the CSR committees of all the participating corporates.

Donating to approved projects of the Government

The next possibility is to simply donate to the approved projects of the Government. Such a donaton is due compliance of the requirements of law.

Contributing to a charitable organisation

Last but not the least is to contribute to the cause of a charitable organisation engaged in carrying out CSR activities. Such an organisation can be

- Section 8 Company or
- Registered Trust or
- Registered Society which is -
    - Established by the company (Independent / Collaborative).
    - Or Established by Central / State government.
    - Or Any Entity established under an Act of Parliament / State.
- It should have an established track record of three years (rule 4 (1) (d))
- It should be registered with Income Tax department u/s 12A and 80 G

- It should be registered with the MCA (effective 01.April 2021)
- The entity should specify -
  - The Projects.
  - Modalities of Utilization of Funds.
  - And Monitoring & Reporting Mechanism.

The compliance is completed only when the amount is spent by the third party. This situation calls for a continuous monitoring of the activities of the third party. The corporate should obtain a report from the auditor of the third party to the effect of the expenditure incurred on the CSR activity.

CSR committee of the corporate is responsible to monitor such activities.

Chapter 5:

COMPLIANCE IN DIFFERENT SITUATIONS:

OVERALL LIMITS:

The Company has to operate the CSR activity subject to certain overall limits as under:
These overheads cannot be more than 5% of the project cost excluding expenses for designing, implementing, monitoring and evaluation of CSR activity and operating expenses of the activity of both the Company and the implementing activity. However, Salaries and training expenses of the employees, Cost of travelling of the Company employees and administrative expenses shall be a part of the 5% overalllimit.

FOREIGN COMPANIES

In case of a foreign company, the balance sheet filed under sub-clause (b) of sub-section (1) of section 381 shall include an annual report on CSR containing particulars as required in Annexure I or Annexure II of the CSR rules.

HOLDING/ SUBSIDIARY COMPANIES

S 135 says "every company" which implies that it is applicable to the Company on astandalone basis and does not extend to the holding Company or the subsidiary Company.

EXPENDITURE INELIGIBLE AS CSR:

The following expenditure does not qualify to be considered as CSR:

Expending in kind or monetary value of any facilities:
The term used is "spend" which means necessarily an outflow of cash in relation tothe CSR. Monetary value of any expenditure in kind cannot be considered towards CSR. If an existing asset is transferred to the project, it shall not qualify to be CSR expenses.

Activities that benefit only the employees of the company and their families:
The objective is Corporate Social responsibility. Welfare of the employees or their families does not come under this category. The society should benefit from the activity. Where an activity is carried out only for the benefit of the employees or their families, it can be staff welfare but does not qualify to be CSR activity.

One-off events such as marathons/ awards/ charitable contribution/ advertisement/sponsorships of TV Programmes etc.
CSR activities cannot be a medium of popularity or publicity. The objective is to sustain the activity. One off activity cannot be continuous and does not qualify to be CSR activity.

Expenses incurred by companies for the fulfillment of any Act/ Statute of regulations(such as Labour Laws, Land Acquisition Act etc.)

There is no compulsion to carry out the activity in a particular manner. If any compliance is mandatory, spending on the count cannot be CSR.

Contribution of any amount directly or indirectly to any political party.

Activities undertaken by the company in pursuance of its normal course of business: For a Company engaged in manufacture of vaccines for COVID, free supply of vaccines does not constitute CSR activity.

Contribution to Corpus of a Trust/ Society/ Section 8 Companies etc. will not qualify as CSR expenditure w.e.f. 22.01.2021. However, Contribution to any particular fund of the entity to implement CSR will be acceptable.

CAPITAL EXPENDITURE

The Company may create an asset for CSR activity. But the asset should be transferred to the beneficiary. Such asset cannot be carried in the financial statements of the Company. Consequently depreciation cannot be claimed on the asset.

DISASTER RELIEF:

Disaster relief can cover wide range of activities that can be appropriately shownunder various items listed in Schedule VII. For example,

- Medical aid can be covered under promoting health care including preventivehealth care.
- Food supply can be covered under eradicating hunger, poverty and malnutrition.
- Supply of clean water can be covered under sanitation and making availablesafe drinking water

EXPENDITURE OVERSEAS

Any amount spent overseas does not qualify as CSR unless spent on state or national level player(s) outside India for coaching and skill development.

INCOMETAX TREATMENT

Explanation 2 has been added to S 37(1) of The Income Tax Act to the effect that CSR expenditure will not qualify as business expenditure. No deduction will be availablefor the CSR expenditure.

SPENDING MORE THAN STIPULATED LEVELS

It is a legal requirement that at least 2% of net profit to be spent on CSR. There is no restriction to spend more than 2% of net profits. Any excess expenditure under CSRcan be carried forward for a period of three years immediately succeeding the year.

SURPLUS ON CSR EXPENDITURE

Any surplus arising out of the CSR expenditure also should be spent on CSR. Any interest earned on deposits of CSR money has also to be spent on CSR activity.

Chapter 6:

UNSPENT FUNDS ON CSR

In the event of a delay in identifying and commencing the project, Law requires that the specified amount be transferred to a specified bank account as under:

If Project is not identified or not commenced, the funds should be transferred to a fund within 6 months from the date of Balance sheet.
If Project is commenced the transfer to specific bank account shall be within 30 days from the date of Balance sheet. There need not be separate bank accounts for each of the activity. However, there should be a mechanism to monitor the transfers withthe projects.

In either case, the funds should be spent within three years from the date of such transfer. The above provisions of unspent funds indicate that the activity should becompleted within a period of three years from the date of transfer to the specific account.

PENALTIES FOR NON COMPLIANCE

Non-compliance with the provisions of S 135 is a civil wrong and the penalties are asunder:

For the Company

Twice the unspent amount required to be transferred to Unspent CSR fund or Rs.100 Lakhs whichever is less

Every officer of the Company:

10% of unspent amount required to be transferred to the fund or Rs.2 lakhs whicheveris less.
Penalty is not an alternative to transfer the funds. The company is not relieved of the liability to transfer funds. It is in addition to the penalties.

Chapter 7:

IMPACT ASSESSMENT

The concept of Impact assessment is inserted effective 22 Jan 2021. The objective of the study is to assess the impact of the CSR expenditure on the society. Such a study helps the Company to take considered decisions before deploying the funds and toassess whether the objective of the project is achieved or not.

Such a study is mandatory in case of Companies with a minimum average CSR obligation of Rs.10 cr or more in the immediately preceding three financial years and Companies that have CSR projects with outlays of more than Rs. 1 crore and which have been completed not less than one year before undertaking the impact assessment. Others may take up on a voluntary basis

This study has to be undertaken by an independent agency. The Board of directors can appoint the independent agency to carry out the impact study. Fee paid for theimpact study can not be more than 5% of the project outlay or Rs.50 lakhs. Expenditure for impact assessment does not come under the administrativeoverheads limit of 5%.

Report of the impact study is to be tabled before the Board of directors and the report shall be annexed to the report on CSR. Providing a Web link to the report andproviding an executive summary of the impact assessment report in the annual reportwould be sufficient compliance,.

In case of a collaboration of two or more Companies, a single report would sufficeand can be share with all the participating Companies. Sharing of the cost of suchimpact study is to be decided among the participating Companies.

DISCLOSURE REQUIREMENTS

CSR should be disclosed as a separate line item in the financial statements. A separate annual report on the CSR containing the particulars as required in CSR rules shall be furnished.

Chapter 8:

AUDIT OF CSR ACTIVITY

There is no specific requirement of audit of CSR activity under S.1 35 of the Companies Act. Sub rule (2) of rule 5 requires that the CSR committee shall institute a transparent monitoring mechanism for implementation of the CSR projects or programmes or activities undertaken by the company. Sub Rule (1)(B) of Rule 6 states that the CSR policy of the company shall, inter alia, include Monitoring Process of such projects and programs.

AUDITORS RESPONSIBILITY WITH RESPECT TO CSR ACTIVITIES

Whenever a company undertakes CSR activity itself, the Auditor of the company shall ensurethat -

The Activity / Project undertaken is within the purview of Schedule VII of the Act.

Separate disclosure of Expenditure on CSR activities is made as per Schedule III of the Act. The Expenditure on the project is incurred as per Companies (CSR Policy) Rules 2014.

The Company has complied with applicable **Accounting Standards** in Accounting**;** Recognition & Disclosure related to CSR spend.

Comply with relevant Standards on Auditing for Audit of CSR spend including -

- **SA 250**: Consideration of Laws & Regulations in an Audit of FinancialStatements.
  - **SA 720 (Revised)**: The auditor's responsibilities relating to other information.

Comply with the guidance note on **Audit of Expenses**.

Verification of the CSR spend has been done as per guidance note on **Audit of Expenses** issued by ICAI.

The utilization of CSR funds reports is issued in accordance with the guidance note on **Reports or Certificates for Special Purposes** issued by ICAI.

If mere contribution / donation is given, then the same is specially allowed as per Schedule VII of the Act.

Whenever the company undertakes CSR activity through a third party, the company shouldobtain an independent practitioner's report on utilization of such CSR funds to whom the funds are given by the company for implementing CSR activity.

The Auditor / CA in practice of the third party before issuing the independent practitioner'sreport on utilization of CSR funds should ensure that the third party has spent the funds on CSR activities as per Section 135 of the Companies Act, 2013 read with schedule VII to the Act and related regulations.

AUDITIORS RESPONSIBILITY IN CASE OF UNSPENT FUNDS:

- Clause XX has been inserted in the CARO which specifically requires reporting on CSR. The same is read under -
- (XX) (A) Whether, in respect of other than ongoing projects, the company has transferred unspent amount to a fund specified in Schedule VII to the Companies Act within a period of six months of the expiry of the financial year in compliance with second proviso to sub section (5) of Section 135 of the saidact.
- (XX) (B) Whether any amount remaining unspent under Sub Section (5) of Section 135 of the Companies Act, pursuant to any ongoing project, has been

transferred to special account in compliance with the provisions of Sub Section (6) of Section 135 of the said act.

AUDIT PROCEDURES

- Having seen the Legal & Professional requirement of their auditors, the following procedures merit attention:
  - The auditor should build in to the audit programme a mechanism to carry out the audit of CSR transactions.
  - The procedures followed have to be documented.
- Examine whether the Provisions of S 135 are applicable to the company
  - If YES: Plan to carry out the Audit.
  - If NO: Document the reasons and keep it as a part of documentation.
- Ensure that the management includes a note on this activity as a part of the management representation.
- Ascertain from the management **The Modality of Implementing the CSR Activities** and that it is within purview of the provisions of Schedule VII.
- Procedures depend upon the way CSR activities are implemented by the management.
- Seek minutes of the meeting of the Board of Directors for having constituted the CSR Committee and its composition and document the same.
- Verify the minutes of the meetings of the committee about the basis of arriving at apolicy and the basis on which the committee has quantified the amount of CSR andcross check the same with the earlier year's financial statements.
- Obtain a copy of the CSR Policy of the company as recommended by the CSR Committee.
- Verify the minutes of the meeting of the Board of Directors of the company having adopted the CSR policy.
- Discuss the basis on which the committee has identified the nature of the activity and the area and location of carrying out the activity.
- Be skeptical if any of the related parties are interested in the activity.
- Carry out **Audit of the Expenditure of CSR** in accordance with the guidance note of the ICAI on **Audit of Expenditure** being
- Evaluation of internal control
- Management representation
- Analytical procedures
- Presentation and disclosure
- Documentation
- Check the budget provisions for the same and release of funds.
- Examine the methodology to monitor the CSR activity by the CSR Committee and ensure compliance.
- Examine the progress reports on the ongoing projects and the amounts incurred.
- Ascertain the amount remaining unspent on the ongoing projects as well as the bank account for disclosing in CARO.
- Whenever possible carry out a physical inspection of the project or the activity of the ongoing CSR activity.
- Ensure compliance with Sub Rule (2) of Rule 5 and sub rule (1)(B) of rule 6 of CSR rules.
- Discuss with the CSR Committee the basis on which the particular institution was preferred.
- Examine the receipt issued for the amount.

- Trace the transaction in the back account.
- Discuss with the CSR Committee about the progress of work and any written evidence about the status of the project as received from the agency.
- Examine supporting evidence such as Photographs or Videos etc.

IN CASE OF COLLABORATION WITH ANOTHER CORPORATE

- Examine MOU with the other company.
- Determine who is taking the lead and the basis for sharing of expenditure.
- Examine the minutes of the meeting of the CSR Committee to monitor the progress of the CSR project.
- Obtain a representation from the CSR Committee with regard to the expenditure.

IN CASE OF CONTRIBUTION TO A THIRD PARTY

Ensure that the third party complies with the requirements of S.135 read with Schedule VII on implementations

- Examine the **Modalities of Utilization**.
- Examine the **Reporting Mechanism.**
- Examine the Periodical Reports as received from the **third party.**
- Where the activity is carried through a third party, it is essential to obtai a report from an Independent Practitioner's or Auditors of the third party.

INDEPENDENT AUDITORS REPORT ON ACTIVITIES OF THE THIRD PARTY

- To be issued by the Auditor of the third party or the NGO to whom funds are given.
- Or by a CA in practice.
- Examine the Independent Practitioners report about the expenditure on CSR.
- Ensure that the report is on the lines as specified by the ICAI.
- Such a CA should submit the report on utilization of the CSR funds after verifying that the third party has spent the funds on CSR activities as per S.135 of the CompaniesAct 2013 read with schedule VII and related regulations in accordance with the guidance note on **Reports or Certificates For Special Purposes** issued by ICAI.

REPORTING ON UNSPENT FUNDS

- Obtain management representation from the CSR committee about the projects planned and the funds set apart for the project
  - Obtain the calendar of implementation
- In case the project has not taken off, obtain evidence that the funds set apart are deposited into specific fund as required for reporting under CARO
- In case the project is grounded, ensure that the unspent funds are deposited in to a designated bank account for reporting under CARO

UPON COMPLETION OF THE AUDIT

- Ensure that the company complies with the applicable **Accounting Standards**.
- Insist upon a representation from the management about the -
  - Applicability.
  - CSR Policy.
  - Quantum of Expenditure.
  - Modalities of Expenditure.
  - And that the expenditure complies with the provisions of law.
- Transfer of funds other than ongoing projects to a specific fund within six months from the end of the financial year.
- That the unspent funds in respect of the ongoing projects are deposited in a separate bank account.
- Ensure that the CSR expenditure in disclosed as a separate line item in the financial statements.
- Additional clause included in CARO to report on the CSR -
  - Whether in respect of other than on going projects the company has transferred the earmarked funds to a specific fund.
  - Whether the unspent amounts on an ongoing project are deposited in a specified bankaccount

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