Deloitte.

Corporate Social Responsibility (CSR) Advisory services

Reducing risk | Increasing value

Forensic

Section 135 of the Companies Act, 2013 (the "Act") specifies certain CSR requirements that need to be mandatorily undertaken by corporates. These new regulatory provisions impose responsibilities such as setting up a Board level CSR committee, planning and approving CSR activities (for the year), as well as ensuring their implementation.

While CSR activities are generally viewed by companies as an onerous task/ regulation imposed upon them (by regulatory bodies/ the government), approaching this as a 'tick-in-the-box' process, may expose an organization to a variety of fraud risks (some of which are elaborated below), all arising from ineffective due diligence and poor monitoring.

Understanding the law

The Act attempts to place onus on the Board of Directors towards governance of CSR activities, prescribing specific mandatory requirements to be adhered to:

Applicability of the CSR regulations:

Companies meeting any one or more of the following criteria are required to contribute toward CSR:

01. Net worth of INR 500 crore or more
02. Turnover of INR 1,000 crore or more
03. Net profit of INR 5 crore or more

Board-Level CSR Committee:

01. Comprising 3 or more Directors with at least one Independent Director
02. Composition to be disclosed in the annual Board of Directors' report

Responsibilities of the CSR Committee:

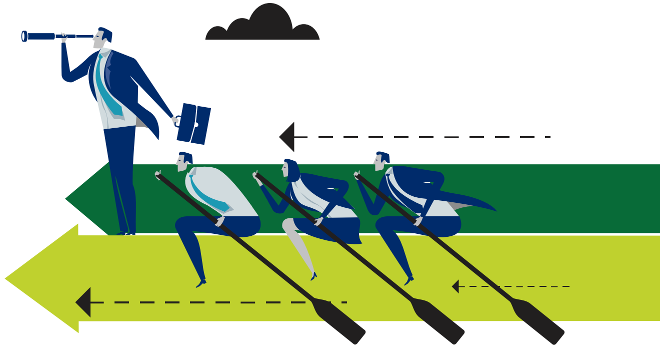
01. Formulate and recommend a CSR policy and amount of CSR expenditure
02. Regular monitoring of the CSR initiatives
03. Board to approve CSR policy; disclose its contents in the Board report; make it public on the company website and deploy the funds

Annual spending on CSR:

01. Every financial year, at least 2% of the average net profits made during the three preceding financial years
02. Schedule VII of the Act indicates activities that may be included by a company in their CSR policies

Responsibilities on the Board:

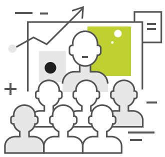
01. Approve and disclose the CSR policy in the annual Directors' report and on the company website
02. Ensure implementation of CSR activities as per the policy
03. Directors' report to specify reasons in case the specified amount is not spent



Your exposure to the risk of fraud

While the process of implementing CSR activities varies across companies, some of the inherent fraud risks that companies could be exposed to are as follows:

Process	Key fraud risks	Scheme	Root causes
 **Creation of CSR Committee**	**Conflict of interest**	Employees on the CSR Committee may use their position to direct CSR activities toward NGOs/ Trusts in which they have some personal financial stake or connections that could be leveraged for their personal gain.	• Inadequate screening and due diligence of committee members selected
 **Development of CSR strategy and policy**	**Advertising/ Marketing fraud**	Conflation of public relation activities with CSR activities may result in undertakings which do not benefit the society in any tangible way, rather are seen only as brand promotion or a marketing gimmick.	• Inadequate review of CSR strategy and policy • Lack of an appropriate presence of Independent Directors/ Members in the CSR Committee

 **Identification of a Partner**	**Related or fraudulent entities/ charitable trusts**	Companies, in the name of conducting CSR activities, may misappropriate funds by either setting up fake NGOs, trusts and other charitable institutions or signing contracts with related parties on inflated prices to divert money for personal purposes.	• Poor or ineffective due diligence on the project implementation partner (e.g., NGO, trust or other entities) • Lack of identification of any potential conflict of interest between CSR committee members and owner(s) of the project implementation partner's entity
 **Project finalization and approval**	**Bribery/ Corruption**	Gain business favor from politicians or government entities by disguising what would ordinarily be considered a bribe under the guise of CSR activities.	• Poor evaluation of project finalization process • Lack of identification of any potential conflict of interest between CSR committee members and owner(s) of the project implementation partner's entity
	Inflated projects	Develop project budgets on inflated prices in collusion with the owner/ employees of the partner entity with an intention to divert funds at a later stage.	
 **Project implementation**	**Fictitious projects**	Overstate or claim projects (that only exist in theory) in collusion with the employees of the company, enabling the existence of a fraudulent entity/ trust.	• Inadequate mechanisms to monitor the utilization of funds and appropriateness of the work carried out • Lack of a periodic 'red flag system' to highlight the misuse of funds
	Financial Frauds	Disguise potential fraudulent activity by inflating bills, expenses, skip agreed upon deliverables and use wrong classifications to dodge tax liabilities etc.	

How we can help

CSR advisory partner – Providing an end-to-end solution

While most companies have an internal team that manages the execution of CSR activities, fraud risk-related vulnerabilities are, however, often overlooked or undiagnosed. Working alongside forensic experts can help reveal inadequacies in the CSR process/ activities on a real-time basis depending on the stage of involvement.

	CSR stage	Forensic Solutions
1	Development of CSR strategy and policy	Review the CSR policy in line with appropriate regulations and identify potential gaps.
2	Identification of Partner	Conduct due diligence on entities/ implementation partners (NGO, Trust, etc.) including but not limited to their business activities, registration with government authorities, other business activities indicative of any potential conflict of interest, existence, adverse media information and political affiliations etc. (to name a few).
3	Project evaluation and feasibility analysis	Carry out a detailed 'Forensic screening' of your CSR proposals (this could include identifying any inconsistencies from the approved CSR strategy/ policy, identifying potential indicators of conflict of interest, etc.).
4	Project implementation	Analyze end utilization of funds and due diligence to identify unusual trends and patterns in payments, the ultimate beneficiary of funds, etc.
5	CSR effectiveness assessment	Conduct forensic spend analytics to determine the effectiveness of your CSR efforts/ funds in line with CSR strategy.
6	Need basis	Carry out an investigation or gather intelligence, where required, basis any incident occurred.

For more details, reach out to

Rohit Mahajan
APAC Leader
Partner and Head – Forensic
Financial Advisory
Deloitte India
T: +91 22 6185 5180
E: rmahajan@deloitte.com

Sumit Makhija
Partner
Forensic
Financial Advisory
Deloitte India
T: +91 124 679 2016
E: sumitmakhija@deloitte.com

Rohit Goel
Director
Forensic
Financial Advisory
Deloitte India
T: +91 124 679 2340
E: rogoel@deloitte.com

Deloitte.