CSR & ESG

RULES, REGULATIONS, AND PROVISIONS IN INDIA

Corporate Social Responsibility ("CSR") has been widely recognized as a corporate entity's duty to contribute to society through philanthropic means and ethical practices. Most jurisdictions mandate such CSR to be undertaken by companies to offset the potential harms the business activities of a company might bring to the society as a whole. ESG stands for Environmental, Social and corporate Governance, and has been considered the broader category within which CSR falls. Socially responsible investors concerned with a company's environmental impact, its social repercussions, and its inclination to do right by the community that provides business to such a company, are mindful of its adoption of ESG responsibilities while making the decision to invest.

It is believed that CSR gave rise to increased duties of the company, resulting in the significance of ESG. However, CSR only falls within the third prong of ESG, the one concerned with corporate governance. CSR activities have mostly been self-regulated, although under a broad legislative instruction to companies of a certain size. In the Companies Act 2013, the threshold size of a company mandated to undertake CSR activities is in terms of any of the following three metrics calculated during the immediately preceding financial year: net worth (Rs. 500 crore or more), turnover (Rs. 1,000 crore or more), or net profit (Rs. 5 crore or more). A company satisfying any of these three criteria is obligated to form a CSR committee, which would in turn make recommendations in the form of a CSR Policy for implementing CSR activities.

As mentioned above, the management of CSR is left to the company, with minimal instructions from the government. However, in order to ensure that a company while spending towards CSR, does not deviate from the generally recognized social causes which need to be supported, the Companies Act 2013 contains Schedule VII, which lists out certain activities that the company may include in its CSR Policy. These include eradicating hunger, promoting education, promoting gender equality, ensuring environmental sustainability etc.

CSR obligations of companies under Section 135 of Companies Act, 2013 are further supported by Companies (Corporate Social Responsibility Policy) Rules ("CSR Rules"). First rolled out in 2014, the CSR Rules are amended from time to time to adapt to the needs of the community. For instance, as per the CSR Rules, activities undertaken by a company in its normal course of business are not considered as activities in fulfilment of their CSR obligations. However, in view of the Covid pandemic, the Ministry of Corporate Affairs ("MCA") vide a notification dated 24th August, 2020 had amended this provision as a result of which research and development activities undertaken by companies in the normal course of their business in relation to new vaccines, drugs and medical devices were considered as valid CSR activities for three financial years (2020 – 2023).

In a significant overhaul of the CSR rules, the MCA notified CSR Amendment Rules, 2021 ("2021 Rules") with an increased focus on 'impact' created by use of CSR funds. Rule 8(3) of the 2021 Rules mandates companies having an average CSR obligation of ten crore rupees or more to undertake impact assessment of their CSR projects through an independent agency. It must be noted that any such impact assessments by companies were not required previously. However, this new requirement is in line with the increased sensitivity of investors to ESG factors. Carrying out impact assessments would not only help funders and companies understand the on-ground impact of their social investments but also help them identify hurdles and make more meaningful contributions in future.

It can be seen from the contents of Schedule VII of the Companies Act, 2013 that certain aspects of ESG have also been incorporated within the ambit of CSR. These two practices are quite evidently interlinked. The United Nations Sustainable Developments Goals (SDGs) illuminate the path to be taken while implementing ESG norms. SDGs, set up in 2015, comprise of the 17 global goals designated by the UN to be a 'blueprint to achieve a better and more sustainable future for all by 2030', and include, among other things, No Poverty, Zero Hunger, Clean Water and Sanitation. The UN has in place a non-binding pact by the name of UN Global Compact, which encourages companies to incorporate ESG norms in their policies. A wide array of literature is available on its website, dealing with corporate responsibility relating to human rights, climate change, labor and employment amongst other things. In pursuance of these goals, an affiliate independent body by the name of PRI (Principles for Responsible Investment) has been set up. PRI is an investor initiative contributing towards a sustainable global financial system by proposing various ways of incorporating ESG norms into investment practices. The six core principles advocated by the PRI are as under:

- Principle 1: To incorporate ESG issues into investment analysis and decision-making processes.
- Principle 2: To be active owners and incorporate ESG issues into ownership policies and practices.
- Principle 3: To seek appropriate disclosure on ESG issues by the entities in which investments are made.
- Principle 4: To promote acceptance and implementation of the Principles within the investment industry.
- Principle 5: To work together to enhance investors' effectiveness in implementing the Principles.
- Principle 6: To report on investor activities and progress towards implementing the Principles.

The signatories to PRI are required to report on their responsible investments activities annually. This helps summarize and monitor responsible investment activities, acts as an accountability mechanism; leads to the continuous improvement of the company's internal processes; and provides feedback so that the company can evaluate its progress.
The importance of CSR and ESG has been felt universally. The guidelines with respect to each of them are constantly evolving, taking into account ubiquitous as well as endemic issues of the global community. More than gaining goodwill, such practices must be enforced by ethical companies to give back to the society as much as possible, guided by the various instructions of the government and the UN.

The increased focus on responsible investment in India and increasing reporting requirements around ESG, in the form of recently introduced Business Responsibility and Sustainability Reporting (BRSR) requirements for top 1000 listed entities (by market capitalization), underlines the growing relevance and importance of CSR. Commitment by companies to ESG and CSR is the need of the hour for a sustainable future between businesses and stakeholders.

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