Corporate Social Responsibility

- A "Beyond Law" Commitment*

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Recently, the Lok Sabha passed the Companies Bill, 2012 (the "Companies Bill"), which aims at making the corporate sector more transparent, efficient and responsible. Interestingly, this is also an attempt on the part of the Indian Government to foster philanthropy and introduce mandatory rovisions for responsible corporate governance in India Inc. in the form of Corporate Social Responsibility ("CSR") provisions.

Preface to CSR

The idea that the corporate firm exists and operates within the societal framework, whereby it has to fulfill its obligations not only towards internal stakeholders but also towards

its external stakeholders, is the dominating theme of CSR. In India, the origin of CSR can be traced in the Vedas; the Gandhian trusteeship model, long traditions of philanthropy[1] and modern CSR initiatives[2]. Active involvement of Indian companies in CSR as well as the advent of globalisation, privatisation and deregulation has been a stimulus for lawmakers to formulate such a regulation.

Globally, the CSR concept has echoed in the principles outlined by different international organisations such as the United Nations Global Compact,[3] the OECD[4] and the European Commission,[5] in which the role of public administration and public policy initiatives is identified as key to a more sustainable, inclusive economy and an integral component of corporate strategy.

Voluntary Guidelines for Corporate Social Responsibility, 2009

In 2009, the Ministry of Corporate Affairs released a set of CSR-Voluntary Guidelines for Corporate Social Responsibility, 2009 ("Guidelines") to incorporate a broader vision of CSR into Indian corporate law and aimed at promoting businesses' contribution to the well being of stakeholders and society. The Guidelines set out six core elements for companies to address: respect for all stakeholders; ethical functioning; respect for workers' rights and welfare; respect for human rights; respect for the environment and activities for social and inclusive development. The Guidelines, though had a very broad vision, failed to provide guidance as to what "CSR" meant and also failed to provide assistance to companies in selecting their CSR activities.

CSR in the Companies Bill, 2012

The Companies Bill makes CSR a mandatory legal requirement for India Inc. determined by a financial threshold. A company in this provision refers to an entity incorporated under the Companies Bill or under the other previous company law.[6]

- *Applicability:* As prescribed under Section 135 of the Companies Bill, the company satisfying any of the following criteria has to comply with the CSR provisions as stipulated under the Companies Bill:

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[1] Several companies like the Tata Group, Birla, Infosys and Indian Oil amongst many other corporates, have been contributing to India's development and social welfare in the form of voluntary CSR since as early as the mid-1960s. [2] In the Indian context, the origin of CSR can be traced from the Vedic literatures such as the Valmiki Ramayana, the Mahabharata and the Puranas. Historically, CSR has been a strong influence on business, government and society. The Indian business has traditionally been socially responsible. [3] The UN Global Compact is a strategic policy initiative for business and has come up with 10 principles in relation to CSR and these relate to Human Rights, Labour Standards, Environment, Anti-Corruption, etc. [4] The OECD Guidelines for Multinational Enterprises are recommendations to enterprises made by the governments of OECD member countries and their aim is to ensure that multinational enterprises operate in harmony with the policies of the countries where they operate and with some standards set out in the Guidelines. [5] In October 2011, the European Commission published a new policy on corporate social responsibility. [6] Section 2(20) of the Companies Bill; Section 2(i) of the Companies Act, 1956 defines a "company."

Criteria	Threshold	Definition
Net worth	INR 500 crore or more (USD 918 Million)[7]	"Net worth" is defined to mean the aggregate value of the paid-up share capital and all reserves created out of the profits and securities premium account, after deducting the aggregate value of the accumulated losses, deferred expenditure and 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.[8]
Turnover	INR 1000 crore or more (USD 1836 Million)	"Turnover" is defined 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.[9]
Net Profit	INR 5 crore or more (USD 9.2 Million)	"Net profit" is defined to mean the total and final revenue of the company after deduction of expenses, interests, dividends etc.[10]

- *Constitution of a CSR Committee:* The company which falls within the above criteria shall be required to constitute a Corporate Social Responsibility Committee ("CSR Committee") of the Board comprising minimum three directors, out of which at least one director shall be an independent director.[11]
- *Formulation of CSR policy:* The CSR Committee shall formulate and recommend to the Board, a CSR Policy which shall indicate the activities to be undertaken; recommend the amount of expenditure to be incurred on the activities referred and monitor the CSR Policy of the company from time to time. The Board after taking into account the recommendations made by the CSR committee, approve the CSR policy for the company.
- *CSR activities:* CSR activities which may be included by companies in their CSR Policies may relate to (i) eradicating extreme hunger and poverty; (ii) promotion of education; (iii) promoting gender equality and empowering women; (iv) reducing child mortality and improving maternal health; (v) combating human immunodeficiency virus, acquired immune deficiency syndrome, malaria and other diseases; (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.[12]
- *Allocation towards CSR:* The Board is required to ensure that the company spends, in every financial year, at least 2% of the average net profits of the company made during the three immediately preceding financial years, in pursuance of its CSR Policy.
- *Disclosure and reporting:* The Board is required to provide[13] in the General Meeting, a report disclosing the composition of the CSR Committee along with the details about the CSR policy developed.[14] The contents of the policy shall also be placed on the company's website. Further, the statement of profit and loss statement shall accord the amount of expenditure incurred on CSR activities.
- *Reasons for non-spending:* The CSR provision follows a "comply or explain" approach, which requires the company to formulate a CSR policy and furnish details of spending of such amount. If the company does not have adequate profit or is not in a position to spend the prescribed amount on CSR, the Board is required to disclose and report the specific reasons for not spending the amount.[15]

Larger picture and the road ahead for CSR in India

India's proposal is part of the new wave of development in the realm of CSR. Key points of the proposed regulations are as under:

- *Additional taxes v. 2% of net profit:* The lawmakers instead of simply taxing companies in the name of "social good" have mandated expenditure for the same. The intention has been to invoke the spirit of voluntary corporate philanthropy. The major advantage of mandating CSR spending, as opposed to levying additional taxes, is the preservation of the company's autonomy in selecting how its funds should be used and what CSR activity the company invests in. The company would have the leverage to invest its resources into a desired cause directly.
- *Broad scope of Schedule VII of the Companies Bill:* Traditionally, the majority of Indian companies have been investing in education, health followed by environmental issues. Several social sectors such as creating jobs, providing

[7] Calculated as per exchange rates on 10/11/2012. [8] Section 2 (57) of the Companies Bill and Section 29 of the Companies Act, 1956. [9] Section 2 (91) of the Companies Bill and Section 43 A (10) (b) of the Companies Act, 1956. [10] Net Profit is to be calculated in accordance with section 198 of the Companies Bill. [11] Section 292(A) of the Companies Act, 1956 defines "independent director" is a director who is not related to the chairman, managing director, whole time director, or the company secretary and should not have held any position in the company and should not hold below two per cent of the shares of the company, presently or in past. [12] As mentioned under Schedule VII of the Companies Bill. [13] Section 134 (3) of the Companies Bill. [14] Section 134 (3) (o) of the Companies Bill. [15] Second proviso to sub-section (5) of section 135 of Companies Bill.

employment enhancing vocational skills, resources for social business projects and promoting gender equality and empowering women have not received much attention. Schedule VII of the Companies Bill covers such aspects of social growth and will ultimately result in broadening the view of Indian companies, giving them diverse opportunities.

- *All corporates at a level playing field:* Several companies have been imbibing the case for social good in their operations long before CSR become a popular cause. In spite of having such successful examples, CSR in India is at a very nascent stage and is one of the least understood initiatives in India. With the Government making it a mandatory requirement for Indian companies to do a CSR spending, all companies will be put on a level playing field to engage in CSR.
- *Global access to companies: CSR is seen* as an enabler for companies trying to access the global international markets since spending on social development guarantees a positive public image. Apart from this, it helps in retaining staff, higher productivity and reduction in costs and increase in profitability, improving customer satisfaction. A positive impact on the company's image due to CSR investment makes a company more acceptable and attractive as a global player.
- *Fiduciary duty and reinvestment:* CSR ultimately leads to re-investing in communities, where a company functions/operates. It builds reputational legitimacy, trust and reciprocity from which companies benefit. It also makes the stakeholders feel that the company is extending its fiduciary duty to encompass their well-being. Companies engaging in CSR spending also create positive externalities recognised and appreciated by the local community.

Fallout of the CSR provision under the Companies Bill

The CSR clause is comprehensive in its approach, however the absence of a penalty for non-compliance with the CSR provision is a potential setback because there is no deterrent force. Likewise, the absence of the powers, responsibilities and duties of the CSR Committee to carrying out the CSR policy cannot foster the purpose of providing a framework to companies for the CSR road ahead. Further, the extent of liability of the Board is also not outlined in the Companies Bill. In terms of disclosure and reporting of the CSR Policy of the company, apart from the shareholders, the Companies Bill does not provide as to whether there is a requirement to disclose or report before any regulatory authority.

A strict reading of the Companies Bill entails that CSR is not required to be followed by business structures such as limited liability partnerships and partnerships, which are also profit making business entities and this is unlike other countries mandating CSR provisions, for example in Philippines, a large taxpayer falls within the CSR provision, in Mauritius, even banks, trusts and societies are covered and UK includes subsidiaries of companies as well, based on a monetary threshold. The Companies Bill should cover such business structures to carry out CSR activities as they are responsible towards the society they operate in.

Conclusion

The introduction of mandatory CSR instead of imposing additional tax liabilities on companies in the name of "social good" is evidence of the fact that voluntary CSR has been a success in India. It represents the government's faith in India Inc.'s spirit for corporate philanthropy and giving back to the community. The companies have been given a free hand to determine how and where their funds are used for this cause, but with the presence of such a provision, arises the need to ensure that every social sector mentioned in Schedule VII gets almost equal benefit from CSR.

Though there is a possibility of fallout of the CSR provision under the Companies Bill due to the lack of a deterrent force, the "comply or explain" approach, as discussed above, should do the trick in ensuring that every company does its part in this noble effort. What remains to be seen is how efficiently India Inc. responds to the mandatory CSR spending, especially in the light of the fact that there is no regulatory body to oversee and implement the same.

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On a going forward basis, the government should look at instilling a commitment for voluntary CSR in India Inc. to ensure accountability and transparency towards contributing for the welfare of the society, rather than imposing an additional tax burden which would only entail contributing to the coffers of the government, taking away the responsibility of India Inc. to give back to the society in the form which they desire.

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