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Original Article

A Critical Insight into Corporate Social Responsibility in Companies Act, 2013

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Abstract

This paper provides a brief background of Corporate Social Responsibility (CSR), the concept and its evolution in India and in the world. The paper seeks to analyse in detail the CSR provisions new companies' bill and provide critical comments, identify key issues and provide solutions to it. The paper talks about the shift from Corporate Social Responsibility to Corporate Social Obligation. It talks about properly channelizing the huge funds expected to be generated by 2% mandatory CSR norm. It talks about taking an integrated approach by companies to pursue CSR by collaborating with other companies and NGOs and sharing their core-competencies. It has been suggested in the paper that companies can serve well researching and developing innovative solutions for our socio-economic problems by using their core-competencies. The paper also underlines that CSR also must involve environment friendly solutions and integrate social and ecological aspects in their CSR work. The paper also urges that CSR is as much about how companies earn their money as about how they spend it. There is no meaning of spending on CSR if, first of all, a company earns profit by illegal and dubious means. The paper has also analysed a long term possibility of rise of a flourishing CSR industry on lines of outsourcing industries like BPO, IT outsourcing etc. The paper has also analysed problems such as apparent rigidness of Section 135 according to which CSR policies should be framed only in accordance with Schedule VII. The Author has advocated a mix of flexibility and rigidness in this. Problem of enforceability has been discussed and solutions like penalty taxes been suggested. Other problems like continuing support to NGOs, taking voluntary part out of CSR, mitigation of impact of a business, stress on local areas etc. have been analysed.

Keywords: Corporate, Social, Responsibility, Companies, Problems, Opportunities

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Introduction

The Concept of Corporate Social Responsibility (hereinafter 'CSR') can be defined as a concept in which the businesses voluntarily incorporate the social, environmental values in their operation and interactions and are considered responsible not only for profit maximisation, but also for welfare of other stakeholders like consumers [1], employees and the regions where they operate. It is a method of giving something back to society that a business receives from it. According to the World Bank, "Corporate social responsibility is the commitment of business to contribute to sustainable economic development by working with employees, their families, the local community and society at large to improve their lives in ways that are good for business and for development" [2].

There are mainly three approaches to view CSR. Firstly, some view the CSR policies as evidence of the philanthropy of businesses and entrepreneurs. Secondly, others see CSR as a holistic strategy to secure greater goodwill, market itself as a people-friendly business and thereby secure better competitive advantage over the long run. So by integrating business with certain social goals, the business legitimises itself as one which is selflessly contributing to society in a meaningful way and by this businesses can balance their profit-seeking behaviour with the concerns of other agents or stakeholders including workers, consumers, non-governmental organizations etc. Thirdly, some others scathingly attack the concept of CSR and accuse that it serves only as a 'smokescreen' for MNCs which have exploited the people and it deflects attention away from an unsavoury practices of such firms [3].

Some view CSR as "more a public relations gimmick, or representative of some cynical 'enlightened self-interest,' than a serious corporate concern with the ethical and political implications of capitalism." They point out that companies which had dubious records of running sweatshops or exploiting local inhabitants like Shell, Vedanta, Nike etc. have the glossiest CSR campaigns to create a false impression of how ethical they are [4]. On a similar vein, some have argued that CSR is a "predatory soft power form of extending corporate influence in late capitalism and it is a key element of the neo-corporate search for both legitimacy and new markets." There are also three views about the drivers behind the CSR policies. First view is that the societal value is changing and the consumers are not going to tolerate crass and ruthless profiteering anymore. The consumers also have the choice due to competition to do so. Furthermore as the awareness of issues like environmental degradation etc. is growing, the consumers are becoming increasingly unwilling to consume products which involve practices like child labour which are perceived unethical.

There have been examples like boycott of nestle when the powdered baby milk scandal broke out and it led to major changes in the firm's practices. Similar was the case with Nike and Gap when it was found out that they were using sweatshops. Second view is the changing values among employees are forcing the employers to consider change in CSR policies [5]. Presently, firms consider the problem of recruiting and motivating the emergent generation of employees who might otherwise find the world of business antithetical to their own values and hence leave jobs. The third driver is that CSR is driven by a concern with corporate reputation and legitimacy and serves as pre-emptive or reactionary public relations exercise.

The author argues that CSR is both a strategy of an enterprise to project itself as ethical and hence create greater goodwill and also in some cases a smokescreen over their wrongs. Author will adopt this approach while analysing it in context of the new Companies bill.

Emergence and Evolution of the Concept of CSR

The phrase Corporate Social Responsibility was coined in 1953 with the publication of Bowen's "Social Responsibility of Businessmen" which explored the question of how much responsibilities for betterment of societies be assumed by the business men. The idea was slowly explored further in 1960s and 1970s when it was suggested that companies go beyond the mandates of law in fulfilling its societal responsibilities. Management experts increasingly started viewing social problem as potential opportunities for firms and viewed CSR as path to long term sustainability and success. However as the anti-corporate activism, North-South divide, dependency theories, environment concerns started growing, emphasis on CSR as a source and tool of corporate legitimacy, reputation management, risk management, employee satisfaction, better investor relations, competitiveness, operational efficiency by reducing waste, reducing mistrust, long term profits and sustainability etc. also started growing [6].

The first company to actually publish a CSR report was Ben and Jerry's in 1989. Also the protest against crass profit making of companies showing itself in earth summits, WTO rounds etc. CSR began to be considered more seriously. This was exemplified in the controversies about Bhopal Gas Tragedy, Shell's alleged complicity in executions of human rights activists like Ken Saro Wiwa, Nike sweatshop scandal, several major oil spills. Now companies could indulge in ruthless profiteering only at their peril. In 1998 Shell became one of the first major firms to publish CSR reports and spent millions on CSR and publicity to shake off scandals [7]. So it can be seen that CSR was considered more as a direct response to increasing anti-corporate voices like Greenpeace, Human Rights and other such activism to resurrect their public image and reputation. During this period consultancy firms such as Sustainability, Business for Social Responsibility came up. They promised a positive image of companies by CSR activities and broader engagement with NGOs etc. Practices of CSR also evolved to include more comprehensive dialogues and engagement with stakeholders. Dedicated CSR research centres also came up [8]. UN also came up with Global Compact- a framework for businesses to work while adhering to its ten principles which include human rights, environment, labour rights, and anti-corruption etc. Although they have been criticised for lack of enforcement mechanism, they have shown a global commitment. In 2002, calls of corporate accountability were made in the World Summit on Sustainable Development (WSSD) instead of self-regulatory CSR. Although this did not bear fruit, it showed at some level dissatisfaction with CSR model which is seen as largely subservient to corporate interest. However, despite this CSR is going strong and most of world is increasingly accepting CSR which is evident from the fact that in 1977 less than half of the Fortune 500 firms even mentioned CSR in their annual reports, by the end of 1990, it rose to 90% [9].

CSR in India: Pre New Company Bill

The philanthropic activities of businessmen in India date back to colonial rule. In late 19th century the entrepreneurs like Tata, G.D. Birla etc. had strong social leanings and later in 20th century, under the influence of nationalist movement, started spending on social activities like public education, public health, labour welfare etc. In this time it was not called CSR but a kind of philanthropic gesture by industrialists. During this time Gandhiji's talked about the concept of trusteeship and the business being a trust working for benefit of society. Post-independence a great amount of importance was given on the public sector which was seen the driver of growth. Although the public sector enterprises addressed the labour concerns etc. still the concept of CSR never really took off [10]. CSR really started in India in globalisation era in 1990s. The concerns about social and environmental impact of the new MNCs started being felt and the discourse on CSR developed. Now both public and private sector companies have started spending on CSR in a bid to project themselves as responsible corporate firms. Some of the highest CSR spending companies are Public sector enterprises like ONGC, GAIL, HPCL, Coal India and private stalwarts like Tata, Reliance, Airtel, L & T, and TCS etc. However it is to be noticed that very few companies currently spend the 2% of net profit which is being envisaged in the new Companies' Bill.

CSR in the New Companies Bill: Possibilities and Problems

The new Companies bill 2013 seeks to make CSR compulsory for a certain set of companies. According to Section 135 of the Bill which has been passed by Lok Sabha every company

i. Having net worth of rupees five hundred core or more, or turnover of rupees one thousand core; or.
ii. More or a net profit of rupees five core or more during any financial year; Is required to constitute a CSR committee from its Board which must consist of three directors including one independent director [11].

The committee is supposed to frame the CSR policy of the company and monitor and disclose its CSR activities mandated in Schedule VII. Under Section 135 (5) the company is mandated to spend at least two percent of its average net profits over last three years, failing which it has to give an explanation in its report. The section also asks the company to give primacy to local areas where it operates [12]. In light of this mandatory instruction to spend CSR for the companies, the term "Corporate Social Responsibility" seems a misnomer. The term 'responsibility' evokes an image of a moral norm self-enforced, which is desirable but not binding. In view of this binding legal mandate it would be better to call it Corporate Social Obligation (enforced by law). It is now essentially like a 2% tax, which the companies have to spend according to its own policy for CSR instead of paying to the government. With this law, India is all set to become the first country in the world to oblige companies to spend on CSR.

Opportunities

This 2% CSR norm is expected to bring in huge funds from the companies for spending in CSR. At least 1, 20,000 core is expected to flow in from India's top 1000 corporations, MNCs, SMEs etc. This translates into 18 core for each of India's 660 districts. This huge amount of funds, if properly channelized, can go a long way in poverty alleviation and social welfare. The Act itself in Schedule VII lays down nine activities according to which companies will formulate their CSR policy [13]. These include combating extreme hunger and poverty, diseases, promotion of education, gender equality, child and maternal health, environmental sustainability, employment skill training etc. and any other matters as may be prescribed. This however raises a question that, are the companies totally barred from other CSR activities? What about the corporate support for issues not covered in Schedule VII? If a company spends on issues not covered like supporting other NGOs, old age homes, investment in CSR infrastructure etc. will it not count in CSR? A plain reading of Section 135 (3) (a) suggests that CSR spending is bound to be within limits of schedule VII.

If that is the case then, there is little left to the discretion of the companies how to frame their CSR policies. Also if in future some other social issue emerges and the issues enumerated in Schedule VII like education cease to be major concerns, then the entire CSR exercise will become meaningless [14]. However it is also true that if complete discretion is given to companies to frame their CSR policies then some companies will come up with cleverly engineered accounts and will define their CSR policy in such a way that it will benefit their company and the societal element will be missing. For example- a sports company may decide to promote its sport as its 'CSR' activity may defeat the purpose of CSR altogether. So although, complete discretion is undesirable, certain flexibility should be given. A solution could be that a company may be required to take permission from local authorities stating their case before spending on CSR on an issue which is not enumerated in Schedule VII.

There are some other measures needed to ensure that 2% spending on CSR actually translates to real impact [15]. One of them is promotion of innovative solutions, related to their core competency as part of CSR. The private companies are usually exceedingly good in innovation. Their strength in innovation can be used for social solutions. As a part CSR companies can be encouraged to research and develop innovative solutions for our socio-economic problems. For example- Indian Pharmaceutical Companies have core competency in producing cost-effective medicines. As a part of CSR they may be asked to fund the free medicines distribution schemes in hospitals or help insuring poor rural people or fund research institutes for cancer, AIDS and other terminal diseases. As part of innovation, they can do R&D on new solutions which are not otherwise commercially viable to produce.

Similarly other companies which have good profile in research and innovation can research to create socially useful inventions and supply them at subsidised prices as a part of CSR. They can do research to develop environment friendly products and contribute to sustainability and reducing carbon footprint of India [16]. It companies can help in skill building and providing IT infrastructure remote parts of the country. Real Estate Companies can partner with government to build low-cost houses for economically backward people either under schemes like Indira Awas or otherwise. So CSR will be particularly successful if companies use their core competency to innovate and produce solutions in a long term plan rather than doing random and aimless acts of philanthropy. Therefore apart for what they spend, how they spend CSR is also important. The companies can frame their CSR policies according to the Corporate Social Responsibility Voluntary Guidelines 2009 according to which CSR policy should cover elements like care for all stakeholders, ethical functioning, respect for workers' rights, human rights and environment.

Another Issue is CSR also must involve eco-friendly solutions. Most people tend to view CSR as only social and some corporate version of welfarism. However it must be realised that CSR is as much about environmental sustainability as it is about social welfare. The problems like malnutrition, healthcare, poverty, water scarcity etc. [17] are also closely interrelated with ecological problems as has been recognised by World Summit on Sustainable Development. Therefore the companies need to integrate social and ecological aspects in their CSR work. Also rather than working individually on their respective CSR budgets, certain like-minded corporations can collaborate on CSR front. This certainly makes sense if we are interested to make a large scale impact in a certain area. Such collaborations and partnerships will mean higher funds, greater expertise, and benefits of scale. Currently the Schedule VII of the bill does not include assistance given to NGOs for their activities. There is ambiguity about whether assistance given to them will amount to CSR which needs to be removed and support to NGOs should be allowed.

Otherwise all the NGOs which are now being supported by corporates for their charitable activities may suddenly find themselves short of corporate sponsors and become cash strapped. Also there will be better impact of a CSR project when done in such integrated and holistic way rather than bits and pieces assistance to poor [18]. Also the government needs to ensure that CSR is as much about how companies earn their money as about how they spend it. There is no meaning of spending on CSR if, first of all, a company earns profit by illegal and dubious means. In the Bill there is currently no definition of CSR but it appears that CSR is being linked to spending only. This should be remedied and it should be made clear that unless the profit is made legally, the spending on CSR will not be taken into account or accepted as CSR. India does not need an Enron Scandal to remind that companies that are built on dubious base and earn profit illegally, try to whitewash over their wrongs by spending large on CSR. There is also a prospect, even though it may seem far-fetched, that at some point of time there may be a flourishing CSR industry.

CSR process outsourcing industries may come up on the lines of BPO industry. Just as companies are outsourcing their legal, IT needs etc. they may outsource the CSR work to some other companies which have made CSR activities their core-competency [19]. These companies may make their business to do CSR activities (like NGOs) along the lines of respective companies' policy and the companies will be left alone to focus on their core-competency. They might employ their skill to economise cost and earn some profit from this work.

Problems

"CSR must not be defined by tax planning strategies alone. Rather, it should be defined within the framework of a corporate philosophy which factors the needs of the community in which it functions."-said Prime Minister Manmohan Singh in 2007. However it is difficult to see that kind of corporate benevolence in India [20]. Till now most of the CSR has been driven with considerations of long-term gain, creating goodwill, or creating smokescreen over their excesses. There have been few illustrious exceptions of course, it they do not really create the universal corporate philosophy of factoring community needs which Dr. Singh was hinting at. Although he stated that CSR defined by tax planning will achieve little good, his government has done almost that.

By making CSR mandatory it has taken the voluntary element out of it and has turned into a corporate social obligation. This has effectively nipped the creation of a CSR friendly 'corporate philosophy' in the bud by forcing the philosophy down companies' throat. However by mandating 2% government has been able to create uniformity. No longer can a particular company boast about spending on CSR as all will be mandated to do so. Earlier companies sometimes used CSR as smokescreen for their wrong. They were showing how ethical they were by spending (even if little) on CSR. But now if companies want extra praise they will have to spent more than 2% or create a larger impact within the limited spending. But now they can no longer show moral high ground by puny CSR spending.

Again there is the quintessential problem of enforcement [21]. The only measure of enforcement the act has provided is that a company has to give an explanation if it fails to spend 2%. But now he question is to who the company will give explanation? And who will decide if the explanation is adequate- Union Government, State Governments, Parliament or Shareholders? What can the government do to enforce CSR norms of the explanation is considered inadequate? The Bill does not provide answers to this. However answers to these questions are essential as if, the law however well-meaning and attractive it may be, is not effectively enforced has no meaning. Government has to come up with some strong enforcement measure if it is serious about CSR. Some of them may be penalty taxes, or some other similar measures.

Another problem is firms may employ 'creative accounting' and accounting reclassification methods to show that they have spent entire 2% without actually doing so. Such loopholes which may arise in future will have to be closed. Mr. Pawan Sukhdev has come out with an important difference between what he calls the old CSR (Corporate Social Responsibility) and the new CSR (Corporate Sustainability Response) paradigms. He argues quite correctly that the companies have different impacts in society. A mining company have huge environmental impact in a region. However instead of trying to minimise its environmental impacts it may try to gloss over by spending on high publicity programs. For example- If coal corporations instead of trying to reduce pollution and serious environmental damage caused due to their activities and instead spend CSR money on building schools, question arises is it desirable? Surely building school is good but it would serve society better if it reduced its own carbon footprint.

These issues need to be tackled by the government before the bill is enacted into law. Also the stress in the act on areas in vicinity of business for CSR might mean the areas which have higher concentration of companies will benefit more, creating inequity.

Conclusion

From the above discussion on evolution of CSR and its status under the new company bill, it can be concluded that the mandatory CSR opens a new vista of possibilities. If the funds raised by 2% CSR are harnessed properly and equate to impact on ground, it can lead to a lot of development and sustainable growth. However the above challenges and ambiguities need to be overcome.

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