

CSR@ 2%: A New Model of Corporate Social Responsibility in India

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Abstract

Corporate Social Responsibility (CSR) earlier applied as corporate philanthropy and has been in practice in India since ages. However, philanthropy in globalised and modern India does not solve the purpose in quantity and quality. Clause 135 of Company Act 2013 created huge hue and cry among the business community in India. As per clause 135 of the Companies Act, 2013, Every company with an annual turnover of 1,000 crore INR (\$161 million) and more, or a net worth of 500 crore INR (\$80 million) and more, or a net profit as low as five crore INR (\$800,000) and more have to spend at least 2% of their average net profit over the previous three years on CSR activities. With the introduction of new Company act 2013 India became the first country in the world to have legislation for compulsory CSR spending. The paper aims at analyzing the motive of making CSR spending mandatory and it also attempts to explain the concept of CSR in the present Indian scenario, the social issues addressed by the Indian corporations, and methodologies adopted by them to address those issues.

Key Words: CSR, Company Act 2013, India, Philanthropy, CSR Disclosure, Mandatory CSR

Introduction

The 21st century is characterized by unprecedented challenges and opportunities, arising from globalization, the desire for inclusive development and the imperatives of climate change. Indian business, which is today viewed globally as a responsible component of the ascendancy of India, is poised now to take on a leadership role in the challenges of our times. It is recognized the world over that integrating social, environmental and ethical responsibilities into the governance of businesses ensures their long term success, competitiveness and sustainability. This approach also reaffirms the view that businesses are an integral part of society, and have a critical and active role to play in the sustenance and improvement of healthy ecosystems, in fostering social inclusiveness and equity, and in upholding the essentials of ethical practices and good governance. This also makes business sense as companies with effective CSR, have image of socially responsible companies, achieve sustainable growth in their operations in the long run and their products and services are preferred by the customers.

According to World Business Council for Sustainable Development, 2001, CSR is “the commitment of business to contribute to sustainable economic development, working with employees, their families, and the local communities”.

Literature Review

The history business impacts on society and environment has been as old as the existence of the institution of business (Boyce and Ville, 2002; Youd-Thomas, 2005). But over a period of time, the perspective towards business impacts on society has changed. The Friedman’s (1970) view “There is one and only one social responsibility of business -- to increase its profits” on the limitations of the responsibility of business does not hold true in current scenario where media, civil society and social institution have become very pressing and agile to ask and force response by the business organizations towards various issues occupying the boundary between business and society (Altman, 1998). Doing Corporate Social Responsibility (CSR) (Carrol, 1979) activities today, most parts of the world is becoming a necessity for business organization rather than just remaining a choice (Moir, 2001; Valor, 2005).

In the recent past social responsibility has been engaging the minds of big business magnates and emerging as a force to reckon with. Though they might have amassed plenty of the wealth in the business but later on they realized to donate their wealth for social cause. A pretty number of iconic personalities’ focus has now shifted from wealth maximization to wealth distribution for social causes. Among these some prominent names are Warren Buffet, Bill Gates, Vinod Khosla, John Doerr, Larry Ellison, Tom Steyer and Mark Zuckerberg, Ratan Tata, Azim Premji, G.M. Rao, Sunil Bharti Mittal, Nandan Nilekani, Ramchandra Guha, Vineet Nayyar and there are many more in the queue treading on the path of philanthropy. Moved by this wave, 69 elites have become signatories to the public pledge that supports philanthropy (Press Trust of India, 2011). The present philanthropic wave is a diversion from the stakeholder theory propagated by Milton Friedman (1962, 1970) which argues that the business of business is business and the only social responsibility of business is to increase profit. This shift in philosophy is further substantiated by the chairman, Reliance Industries limited (largest company in India in terms of market capitalization) stating that “It is important to get the business of businesses right. The primary responsibility of business is social improvement” (Ambani, 2011). Perhaps this attitude of the rich people is driven by the Maslow need hierarchy theory, i.e. the highest order needs of “Esteem and self actualization”.

The Objective of the Study

Following are the main objectives of the study

1. To study the current CSR practices adopted by Indian firms.
2. To analyse the clause 135 of Company Act 2013 on CSR and suggest the ways to strengthen the 2% CSR model.

Data Collection & Research Methodology

This paper is conceptual in nature. The approach adopted is analytical and based on extensive literature review on CSR. The sources of data are research paper, news paper articles, magazines, and internet etc.

State of CSR in India

CSR is not a new concept in India. Ever since their inception, corporate like the Tata Group, the Aditya Birla Group, and Indian Oil Corporation, to name a few, have been involved in serving the community. Through donations and charity events, many other organizations have been doing their part for the society. The basic objective of CSR in these days is to maximize the company's overall impact on the society and stakeholders. CSR policies, practices and programs are being comprehensively integrated by an increasing number of companies throughout their business operations and processes. A growing number of corporate feel that CSR is not just another form of indirect expense but is important for protecting the goodwill and reputation, defending attacks and increasing business competitiveness.

India is the first country in world to make CSR spending mandatory. Under the new law (Company Act 2013), every company having a net worth of Rs.500 crore or more or revenue above Rs.1,000 crore or a net profit above Rs.5 crore needs to spend at least 2% of the average net profits for the past three years on CSR activities.

Company Act 2013, Clause 135: An Overview

The Companies Act, 2013 ('2013 Act'), enacted on 29 August 2013 on accord of Hon'ble President's assent, has the potential to be a historic milestone, as it aims to improve corporate governance, simplify regulations, enhance the interests of minority investors and for the first time legislates the role of whistle-blowers. The new law will replace the nearly 60-year-old Companies Act, 1956 ('1956 Act').

The 2013 Act has introduced several provisions which would change the way Indian corporate do business and one such provision is spending on Corporate Social Responsibility (CSR) activities. CSR, which has largely been voluntary contribution, by corporate has now been included in law. Basis the CSR provisions, as laid down under the 2013 Act and the draft CSR rules made available for public comments, in this bulletin we bring out the key provisions, analysis and challenges relating to the compliance of these provisions for companies to consider.

Applicability and Constitution of CSR Committee

Section 135 of the 2013 Act states that every company having:

- Net worth of Rs 500 crore or more, or
- Turnover of Rs 1000 crore or more, or
- Net profit of Rs 5 crore or more during any financial year shall constitute a Corporate Social Responsibility Committee of the Board
- The committee would comprise of three or more directors, out of which at least one director shall be an independent director.

The mandate of the said CSR committee shall be:

- To formulate and recommend to the Board, a Corporate Social Responsibility Policy, which shall indicate the activities to be undertaken by the company as specified in Schedule VII;
- To recommend the amount of expenditure to be incurred on the activities referred to above;
- To monitor the Corporate Social Responsibility Policy of the company from time to time.

Responsibility of the Board

The Board of every company referred to above shall after taking into account the recommendations made by CSR Committee:

- approve the CSR Policy for the company and disclose contents of such Policy in its report and also place it on the company's website, and
- ensure that the activities as are included in CSR Policy of the company are undertaken by the company, and
- ensure that the company spends, in every financial year, at least two per cent of the average net profits
- If the Company fails to spend such amount, the Board shall, in its report specify the reasons for not spending the amount.
- "Average net profit" shall be calculated in accordance with the provisions of section 198 of the 2013 Act.

CSR activities as per Schedule VII

CSR activities to include:

1. Eradicating extreme hunger and poverty
 2. Promotion of education
 3. Promoting gender equality and empowering women
 4. Reducing child mortality and improving maternal health
 5. Combating human immunodeficiency virus, acquired
 6. Immune deficiency syndrome, malaria and other diseases
 7. Ensuring environmental sustainability
 8. Employment enhancing vocational skills
 9. Social business projects
 10. 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 such other matters as may be prescribed.
- The 2013 Act provides that the company shall give preference to the local area and areas around it where it operates.

Government Argument for CSR

The government perspective on CSR has been that though India's business sector has generated wealth for shareholders for decades, the country continues to grapple with problems of poverty, unemployment, illiteracy and malnutrition. Corporate growth is sometimes seen as widening the gap between India and Bharat (rural India) through its income-skewing capability. This gap needs to be bridged. While the government undertakes extensive developmental initiatives through a series of sectoral programs, the business sector also needs to take the responsibility of exhibiting socially responsible business practices that

ensure the distribution of wealth and the well-being of the communities in which the business operates.

Dr Manmohan Singh (Former PM of India) has advised the corporate to heed Mahatma Gandhi and look upon themselves as trustees of the people, and warned of social unrest:

“In a country with extreme poverty, industry needs to be moderate in the emolument levels it adopts... The electronic media carries the lifestyles of the rich and famous into every village and slum. Media often highlights the vulgar display of their wealth.... An area of great concern is the level of ostentatious expenditure on weddings and other family events. Such vulgarity insults the poverty of the less privileged, it is socially wasteful and it plants the seeds of resentment in the minds of the have-nots”.

Presently in India, there is a widespread feeling that the high GDP growth rate of past decade has remained confined to urban areas only and has not reached the rural India, particularly to the Spoor section of the society. Corporate have the know-how, strategic thinking, manpower, and financial strength to enable widespread social transformation. Operational partnerships between corporations, NGOs and the government will place India’s economic growth and social development more inclusive. Besides the corporate India, many writers, academicians and NGOs who generally support CSR view the mandatory proposal as an anomaly. They contend that CSR should be voluntary. Business scholars as well as international agencies such as the UN, ILO or World Bank also favor treatment of CSR through soft laws, rather than non-negotiable statutory laws.

Views against Mandatory CSR

Mandatory CSR is Like “Privatizing Taxation” – Montek Singh Ahluwalia

The Planning Commission has been of the view that CSR should not be made mandatory; rather companies should take up CSR voluntarily. Making CSR mandatory will lead to corrupt practices and meddling by highhanded implementing authorities. Some members believe that making CSR mandatory would encourage companies to reduce wages, fudge accounts, or indulge in unfair practices. The best way would be to make them more accountable to the system and the society by rewarding good behavior, and the way do that is to empower SEBI to move towards global standards and enforce them strictly. Earlier, Planning Commission Deputy Chairman Montek Singh Ahluwalia has said that making CSR mandatory would amount to “privatizing taxation.” He said if the Government wants it can increase the rate of corporate tax to 32 per cent from the current 30 per cent rather than making it mandatory for companies to spend 2 per cent on CSR and add complications.

Experts also agree with the Planning Commission and ask when companies are already paying taxes, why the Government is not able to use that money effectively for social welfare activities? They also feel politicians and political parties too will be able to pressure the corporate if CSR becomes compulsory.

Corporate Reaction: CSR or “Corporate Social Compulsion?”

Corporate India feels that it would mean unwarranted intrusion into its affairs and lead to harassment through vexatious inquiries by government inspectors to verify the mode and

extent of compliance with the law. It has been vociferously claiming the right to decide its CSR for itself and according to its own enlightened self-interest and conscience.

The overall corporate sentiment on the issue is neatly summed up by a prominent corporate figure who called this provision “*corporate social compulsion.*”

Wipro Chairman Azim Premji protested on behalf of the India Inc “the people on the board are sufficiently conscious regarding the matter and corporate social responsibility cannot be created with statutory requirements.”

Suggestions to strengthen the 2% CSR Model

1. So far Indian government has been failed to show any specific purpose for adopting such model or any objective for which expenditure is to be made.

If government has to get corporate money into societal cause, it must present real picture of social problems and why at all firms should see it as a sustainable investment not an expense.

2. Government should show some intent for reduction of burden of taxes by applying this model or the treatment of saving if any on part of the government due to adoption of such result.
3. In this era companies should not be measured on the basis of their financial performance only conversely they should be measured by their financial & social performance. Hence there should be some unified index to measure financial as well as social performance of the companies.

There is dearth of scholarly study on CSR indexing in India. However, Government, consulting firms and NGOs are working on CSR indexing based on new CSR model (in accordance with Company Act 2013)

In an effort to facilitate greater corporate participation in corporate social responsibility (CSR) areas, BSE (formerly Bombay Stock Exchange Ltd.), on 23rd Sept, 2013, signed a memorandum of understanding (MoU) with Indian Institute of Corporate Affairs (IICA) to collaborate and develop a CSR index and increase awareness about CSR.

Since companies are now mandated to stick to the list of activities as per clause 135, section VII, CSR Impact Index that is proposed to measure the effectiveness of firm’s CSR should measure if the activities carried out by the firms are not merely done for compliance, but created net positive socio-economic impact(Ramendra et al., 2013).

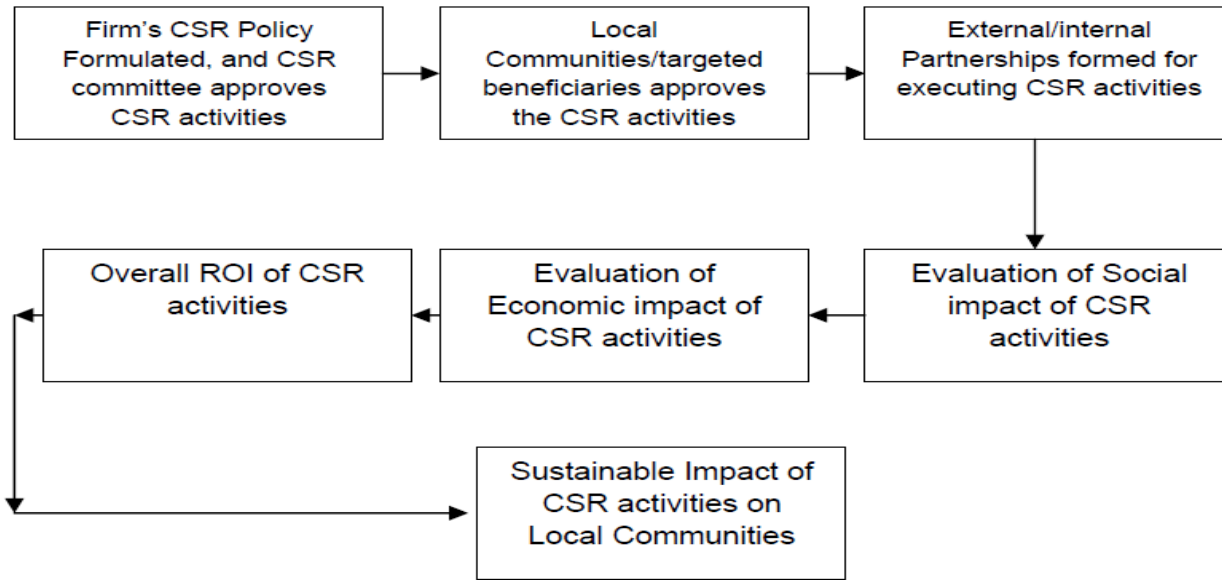
Normative guidelines to measure CSR Impact Index (CSRII)

- i. Does the CSR activities carried out as per the recommendations of the firms’ CSR committee and CSR policies?
- ii. Do the local communities that are the targeted beneficiaries (TB) require these CSR activities?
- iii. What forms of partnerships were developed or used for these CSR activities?
- iv. What is the social impact of the CSR activities (on TB)?

- v. What is the economic impact of the CSR activities on TB?
- vi. What is the ROI of the CSR activities?
- vii. Is the CSR impact sustainable?

These normative guidelines are presented in form of an executable plan in Figure 1 below.

Figure1: Planning and Executing CSR Impact Index



Source: Ramendra et al. 2013

Further researcher & academician should construct a CSR Indexing model which would constitute both financial and social variables.

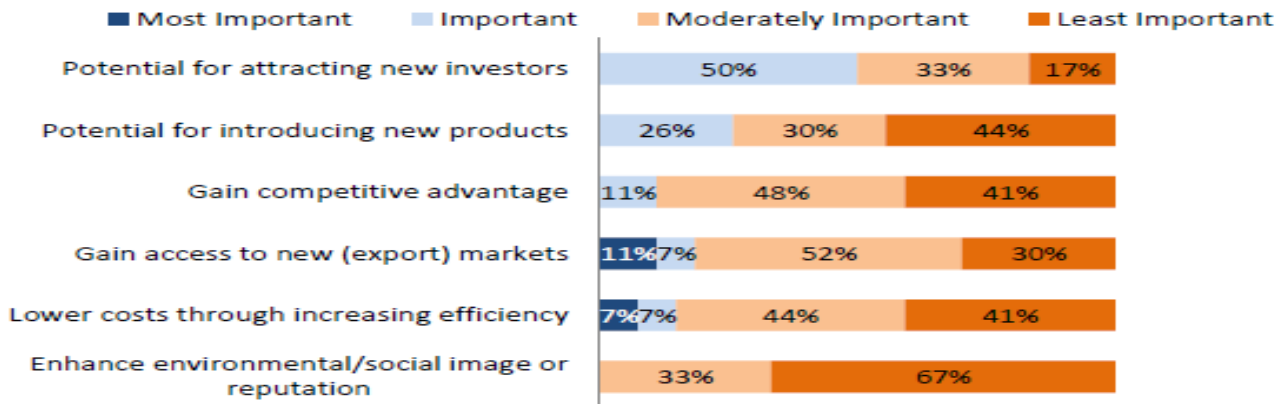
4. In the last 20 years, users of accounting information have demanded more information not only relating to economic activities but also to the impact of a firms' activities on society. Corporate Social Responsibility (CSR) evidenced through social responsibility accounting (SRA) is a means for attaining social responsiveness (Abrol, 2002). Hence, I would recommend policy maker for a good CSR disclosure system to be induced in financial statement of Indian firms irrespective of their sizes and operations.

Influenced by global dialogues and stimulated by the Indian policy makers, the Indian business diaspora has been, for the past few years, increasingly engaging in conversation and action on management and measurement of Environmental, Social and Governance (ESG) parameters. This shift in focus towards non-financial metrics comes amidst an increasing demand from global customers and investors for ESG disclosure along with the launch of the National Voluntary Guidelines for Social, Environmental and Economic Responsibilities of Businesses (NVG-SEE) which is applicable for all Indian businesses. In 2012, the Securities and Exchange Board of India (SEBI) mandated the filing of an annual Business Responsibility Report (BRR), which focuses on ESG performance, for the 100 largest publicly traded firms.

Opportunities, Risks and Drivers of ESG management and disclosure

Across the target sectors, gaining access to new (export) markets and gaining competitive advantage ranked high among the opportunities firms perceived from ESG management.

Table 1: Opportunity for organization presented by ESG



Source: Sustainable Business Leadership Forum, 2013

Disclosures by Indian firms on environmental and social management systems and corporate governance are welcomed by investors as i) a signal to that firm are actively seeking to mitigate operational risk and ii) providing additional data that allows investors to build more sophisticated risk models.

Table 2: Investors reasons to integrate ESG indicators in decision making



Source: Sustainable Business Leadership Forum, 2013

Companies face an increasingly complex landscape of standards, frameworks, and regulations related to ESG disclosure. This guidance varies from mandatory to voluntary and while some are more focused on a specific aspect of business responsibility others are very holistic in nature. However, despite the existence of these standards, frameworks and regulations, ESG disclosure

is still in a nascent stage in the Indian context. The current need is a combination of “carrot and stick” approach to ensure increased uptake of ESG management and disclosure by stakeholders (businesses, investors, etc.).

Conclusion

The great thinkers like Friedman, Hansman, or Mercey, who would ridicule the idea of Mandatory CSR spending and reporting. We need to understand that we live in globalized world as the revenue from business increase along with the prospect for the further business opportunities, care should be taken to complement them with overall improvement of human development index (Arup et al. 2013). If a product or services which earlier was only available in the developed nations is now easily available in India then similarly the quality of life of Indian should tends to be at par with that of people of developed nations.

Since, the concept of mandatory CSR spending has been criticized by the business community, I would like to point out that if India is such huge country having 1.21 billion populations and perceived as country of poor people despite of having maximum millionaires & billionaires. Hence, we need to fill the gap between poor and rich in our country. This can not be solved by government alone. If we look at comparative figure with USA on CSR spending against GDP , India is spending abysmally low of its GDP in comparison to USA.

Table 3: GDP and CSR in 2006(Comparative between India & USA

Country	GDP in US\$	CSR expenditure in % age	Value in US\$	Population in Million
India	916251738112	0.6%	5497510429	1122
USA	13163899650048	2.0%	263277993001	299

Source: http://www.geohive.com/charts/ec_gdp1.aspx

Hence, it is the right time that corporate should take the concept of mandatory CSR(However unusual it may be seem to be) positively in their stride and start visulizing the India of 2050 not only in the form of revenue and economic point of view but in the more holistic way.

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