

Corporate Social Responsibility as Legal Obligation: An Indian Perspective

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Abstract

The concept of Corporate Social Responsibility (CSR) as a voluntary or mandatory measure has invited attention of corporate watchers for long. In India, large corporates have generally been contributing to CSR activities on voluntary basis in the form of charities and other initiatives. The industry has been resenting any regulation on CSR spending by the government. The advocates of mandatory form of CSR have, on the other hand, been arguing that if CSR has to make a demonstrable impact on societal needs, it can be done only by legislation. The regulation will also remove differences in understanding of CSR activities and streamline spending on CSR. The Government of India has finally promulgated a legislation mandating 2% of net profit as CSR expenditure by the corporates every year. It makes CSR reporting mandatory though compliance is not mandatory. The corporates are required to constitute a CSR Committee at Board level to help in formulation of CSR policy for implementation by the company. This is a step in the right direction but real key will be its implementation by the administrative machinery. This paper examines various nuances of the issue.

Key words: Corporate Social Responsibility, Mandatory provisions, Voluntarism, India

Goodness is the only investment that never fails – Henry David Thoreau

Introduction

The concept of Corporate Social Responsibility (CSR) originated when companies emerged as a form of business entity and became integral constituent of the society. CSR has taken various definitions and interpretations in its fold. No common definition has so far emerged but there is positive commonality in almost all elaborations. CSR spells corporate altruism. It has now moved beyond corporate philanthropy to corporate responsibility encompassing all aspects of business - employees, market, environment, society etc. Corporate philanthropy and responsibility connote two different things, the latter being much wider than the former. Passive philanthropy no longer constitutes social responsibility. In today's scenario, CSR is not regarded as charity but a long term strategy embedded to core values and principles of the corporate entity.

Corporate Social Responsibility Defined

A well-accepted definition of the concept was given by World Business Council of Sustainable Development: “Corporate Social Responsibility is the continuing commitment by business to behave ethically and contribute to economic development while improving the quality of life of the workforce and their families as well as of local community and society at large” (WBCSD, 1998). Further, CSR is understood to be the way companies integrate social, economic and environmental concerns in to their business decision making –it is all about doing business in a responsible manner (Datta, 2012).

All the governments, world bodies, non-governmental organizations (NGOs) and voluntary associations have been forcefully pressing the corporate sector to espouse CSR in the overall interest of human establishment and sustainable development. The United Nations has defined CSR in a broad sense as the overall contribution of business to sustainable development (UN, 2007). The World Bank Institute (WBI) explains ‘Corporate Social Responsibility (CSR) is the commitment of business to contribute to sustainable economic development, working with employees, their families, the local community and society at large to improve quality of life, in ways that are both good for business and good for development’ (WBI, 2003).

The European Union defines CSR as “... the concept that an enterprise is accountable for its Impact on all relevant stakeholders. It is the continuing commitment by business to behave fairly and responsibly and contribute to economic development while improving the quality of life of the work force and their families as well as of the local community and society at large...” (EU Green Paper: 2001). International Labour Organisation (ILO) defines CSR as a way in which entrepreneurs give consideration to the impact of their operations on society and affirm their principles and values both in their own internal methods and processes and in their interaction with other actors. CSR is a voluntary, enterprise-driven and refer to activities that are considered to exceed the compliance with law (ILO, 2006). CSR involves short-term costs which do not provide immediate financial benefit to the company, but has long term social and environmental impact on community. It is something that creates long-term sustainable development for the society.

What emerges from such expositions is that CSR permeates corporations towards stakeholders other than shareholders also. It expects the enterprises to contribute to welfare of not only capital contributing shareholders but also to other stakeholders like consumers, employees, society in general. In doing so, it has to pay unencumbered attention to societal concerns in areas of environment, sustainable development, labour conditions, human rights and consumer rights.

Corporate Perspective on CSR

The corporate sector has also responded to the need for CSR in more than one way, though the espousal varies across the board. CSR is now widely debated in the board rooms. In India, there is no dearth of large corporations taking lead in CSR endeavours. Contrary arguments have also come to the fore. The role of corporate management is to maximize shareholders’ value and cannot go beyond such legal requirement. The management has to see whether existing legal requirement provide incentive that cause enterprise to act in a

socially desirable manner (Friedman, 1970). However, subsequently stakeholder definition also gained currency and extended to variety of social and environmental concerns.

CSR – Voluntary or Mandatory

Mandatory CSR refers to existence of legal framework for compliance by companies with penal action for acting in variance. Voluntary CSR, on the other hand, is a non-binding concept which motivates companies to pursue CSR without any regulatory pressure. There is enough evidence suggesting that Indian businesses have been engaging in CSR for years without any legal mandate. Leading Indian corporate houses like Tata, Birla, Ambanis etc. have contributed to CSR activities since inception. Many companies have imbibed CSR in their corporate strategy, but some still view it as a public relations or image building tool. Many other organizations have been doing their part for the society through donations and charitable interventions/programmes.

CSR Programs could range from overall development of a community to supporting specific causes like education, environment, healthcare etc. Many CSR initiatives are executed by corporates in partnership with non-governmental organizations (NGOs) who are well versed in working with the local communities and handling specific social problems. Although some companies like the Tata, Birla, ITC, Wipro and Infosys etc. have a solid history of contributing to India's development and social welfare, many companies have hesitated to contribute more than what is minimally required. In Indian regulations neither there had been a legal mandate for CSR contribution nor any guidance on what constituted CSR activity. This resulted in activities relating to employee welfare, canteen and safety facilities in factory compound being labelled under CSR domain. Some even viewed doing statutory activities like minimum wages, gratuity and bonus as CSR.

CSR has been for long a voluntary concept and not mandatory in India. Notwithstanding its voluntary stance, a number of leading corporates have imbibed CSR in their corporate strategy. The vexed question- whether CSR should be voluntary or mandatory, is main focus of this paper. Should CSR spend be a legal requirement or it should be left to the volition of corporate management. Which is better means of promoting CSR – voluntary or regulatory? Such debate has been engaging attention of intellectuals and corporate experts in India and abroad for long and opinions continue to be divided.

Rationale of Mandatory CSR

It will be interesting to start with the well talked statement – the only obligation of business is to make profit (Friedman, 1970). This statement had many supporters and continues to be so even today. It was advocated that a Manager's role is to maximize shareholder value and he cannot go beyond the legal requirements. Friedman also contended that "the idea of social responsibility means nothing for businesses; in fact, since CSR spending involves managers "taxing" shareholders and spending their money without their consent, it is actually an immoral business practice". Many traditional corporate scholars at that time were in unison with above concept. The basic objection against CSR was that applying the shareholders' funds in any way other than the company's business is contrary to the fiduciary duty of company's directors.

Some critics claim CSR to be a tax on consumers saying that it is irresponsible to deploy corporate assets for social cause (Betsy Atkins, 2006). In India, mandatory CSR is a solution to reach places that State cannot reach on its own (Villamayer, 2010). CSR is a kind of stealth tax that impacts on companies' value creation. We already have regulation across certain elements of CSR like carbon commitments in some European countries, environmental protection laws in India and outside. Law does not just aim to achieve a given result but also intended to prevent widely differing and contradictory treatment of same or similar situations. Such a goal is obviously true of CSR as well. But CSR cannot be regulated by conventional legal instruments (ILO, 2008). Thus, law has also to provide a uniform definition of CSR. However, laws may not be sensitive or supportive to real intent of CSR. Indeed cutting edge CSR practices are often not motivated by strict legal requirements but by strong corporate governance and management actions.

More often one can observe a trend in discussion on CSR that voluntary measures can help improve private-sector behaviour, but voluntary activity is no substitute for regulation and there is evidence that companies that espouse voluntary approaches to meet environmental standards are frequently involved in resisting external regulations, mainly in developing countries, where national legislation framework is weak. Even if necessary laws do exist, many governments including those in developed countries do not have political will or effective instruments to enforce (Mazurkiewicz, 2004). As far as compliance of social and environmental conditions is concerned, a study of Nordic companies revealed that Nordic CSR pioneers are sceptical towards CSR and voluntary approaches in global governance and strongly prefer hard law (Gjølberg, 2011). The Standing Committee on Finance of India also suggested CSR to be mandatory for corporates above a specified threshold.

In many instances, CSR initiatives simply consist of unilateral or ad hoc projects from companies, such as developing a code of conduct, a CSR report, or specific projects to improve social and environmental practices in the company without any wider governance implications. The law is necessary to combat the shareholder primacy drive and get across to companies that social responsibility is in its essence, its core, not a voluntary matter (Beate Sjøfjell, 2011).

Logic of Voluntary CSR

On the other hand, there is no dearth of contrary view –the voluntary concept of CSR. By definition CSR is a voluntary commitment. It defines dialogue with stakeholders. Whether companies choose to be responsible or not, has to be left to their discretion. Sooner or later, they will be aware of the benefits of being responsible (Villamayer, 2010). Business has tendency to resist any increased social, environmental regulation, preferring voluntary or soft law approach to good governance (Gjolberg, 2011). Most CSR activities are based on voluntary approach. CSR is connected with values and values cannot be forced by law (Villamayer, 2010). In India, voluntary donations and charities towards temples, social causes by business houses have been prevalent for long. It is also argued that a mandatory CSR will compel corporates to camouflage their financial statements to show compliance of regulation which may even dilute their existing voluntary commitment to CSR. It may open doors for unfair practices and window dressing of accounts.

Business houses recognize CSR contribution but are against its mandatory stipulation in any way. They claim that businesses should not be governed on aspects other than business. Any legal binding on CSR may prompt companies to discover ways and means of skirting it. Voluntary CSR emanates from corporate soul whereas mandatory CSR is imposed from outside and is seen with repulsion particularly as shareholders are concerned about return from providing the risk capital. In businesses, CSR is generally not seen as matter for lawyers. Another view is that CSR cannot be constrained in legal liability as it requires flexibility for its implementation. Some experts espouse both legal and voluntary domain for CSR saying that CSR requires companies to go beyond what the law requires to achieve. CSR is a business imperative whether pursued as a voluntary corporate initiative or for legal compliance reason (KPMG, 2008).

International Perspective on CSR

The European laws require from companies certain disclosures of their performance relating to society, employees and environment. In USA, CSR is voluntary. France has regulations on non-financial reporting. In Denmark, law requires large companies to publish social and environmental information in their activities. There are laws on Directors' duties concerning CSR in some European countries. Hongkong has declared sustainability Development Policy. China has mandatory CSR reporting. New laws are emerging in many countries to incorporate CSR and sustainable development principles and existing laws are being extended to cover the same.

Spain has voluntary CSR approach that has worked well in as much as Spanish companies have figured in the list of global hundred sustainable performance leaders (Villamayor, 2010). UK's Companies Act has now included a provision on Directors' duty in respect of environmental and social impact of their business. This obligation applies to all Directors. In the context of environmental aspects of CSR, there are a number of international treaties and conventions aiming at protection from environmental hazards and related issues. Some well-known principles emanate from OECD, ILO, UN Declaration. In Europe and North America, some States have started legislating in respect of CSR principles. States are tempted to fill the void if CSR continues to be seen as unregulated issue. There are domestic laws in CSR derivatives like anti-corruption, environment, human rights etc. Many laws also apply extra territorially like Foreign Corrupt Practices Act of USA, Bribery Act of UK. Most countries have also local laws for dealing with environmental aspects.

International Finance Corporation (IFC) Washington, has evolved performance standards on environment and social sustainability, which are subject to revision from time to time in the light of changing circumstances. A very important code is Equator Principles formulated in 2003 by a group of international banks in consultation with IFC Washington Standards. Equator Principles envisage voluntary guidelines for managing social and environmental risks in project financing. UN Global Compact is another voluntary framework in the areas of human rights, labour and environment. It encourages businesses to adopt sustainable and socially responsible policies.

The Shanghai Stock Exchange and Shenzhen Stock Exchange have also taken several steps to promote CSR-related activities and their disclosure. Indonesia has passed a law requiring all public companies to issue CSR reports. The U.S. Security Exchange Commission (SEC) had

directed all U.S. public companies to regularly disclose climate related risks in their annual reports to investors (Robinson, 2010).

Indian Legal Scenario vis-à-vis CSR

India's erstwhile Companies Act of 1956 was a comprehensive law but did not contain any provision in regard to contribution towards CSR. It did not even provide a clear definition of what constituted CSR and most provisions focused on investor protection. The Companies Act failed to deliver any important directive connected with CSR in India (Kaul and Gupta, 2011). Companies were therefore left to decide on their own, the policy and spending on CSR. There had, however, been some provision, dealing with charitable contributions by corporates. Section 293(1) (e) allowed for contribution to charitable and other funds (not directly related to business of company) for an amount higher of Rs. 50,000 or 5% of its net profit during last three financial years, with the approval of Board of Directors. Any contribution in excess of this limit required approval of shareholders. This was merely an enabling provision leaving any choice of making donation with the management of company.

In 2009, Ministry of Corporate Affairs in India issued Voluntary Guidelines on CSR for companies. While stating that the business sector also needs to take the responsibility of exhibiting socially responsible business practices that ensures the distribution of wealth and well-being of the communities in which the business operate, the guidelines envisaged that each business entity should formulate a CSR policy to guide its strategic planning and provide a roadmap for its CSR initiatives, which should be an integral part of overall business policy and aligned with its business goals. The CSR policy should, inter-alia, cover the interest of shareholders, workers, environment and focus on ethical behaviour.

In August, 2013, Indian Parliament enacted a new law, Companies Act, 2013, that has attempted to make CSR provision for certain companies. In terms of section 135 of the new legislation, a company having net worth of Rs. five hundred crore or more or turnover of Rs. one thousand crore or more or a net profit of Rs. five crore or more, during any financial year, will be required to constitute a Corporate Social Responsibility Committee of the Board consisting of three or more directors, with at least one independent director. The composition of the Committee has to be disclosed in Board report. It further provides that 2% of average net profits of the previous three years will have to be spent on CSR activities with disclosure to shareholders about the CSR policy along with reasons on failure of implementation, if so. The CSR Committee shall formulate a CSR Policy, indicating the activities to be undertaken by the company as specified in Schedule VII. The CSR Committee will recommend the amount of expenditure to be incurred on the activities referred to above and monitor the CSR Policy of the company from time to time.

The CSR policy has to be approved by the Board on the basis of recommendations of the said committee. Board has to ensure to disclose contents of such Policy in its report and also place it on the company's website and ensure that the CSR activities are undertaken by the company. The Board should make every endeavour to ensure that the company spends, in every financial year, at least two per cent of the average net profits of the company made during the three immediately preceding financial years, in pursuance of its CSR Policy. If the company fails to spend such amount, the Board shall, in its report specify the reasons for

not spending the amount. Some of the activities covered in CSR policy (Schedule VII) relate to eradicating hunger and poverty, promotion of education, gender equality and empowering women, contribution to the Prime Minister's National Relief Fund.

Conclusion

CSR started as voluntary concept but some aspects of it have been given mandatory nature like antitrust laws, minimum wages, competition laws, health and safety of workers, environmental issues, human rights etc. Some critics favour legal framework for CSR while others advocate its voluntary role. In the absence of mandatory rule, vagueness about CSR spending and activities eligible to be called CSR persisted. If CSR concept has to deliver desired result for all stakeholders, it cannot be left to be entirely at the volition of shareholders and therefore Government intervention is essential. Regulation is intended to prevent widely differing treatment of CSR dispensation. The Union Government in India has, despite lot of resentment and anxiety rhetoric by industry, moved ahead with the passing of legislation dealing with mandatory regulation on CSR. While the new law does not make CSR compliance mandatory, its reporting is made mandatory. In a developing country like India, where Government cannot be expected to do all for welfare of community, a mandatory CSR measure is considered a step in right direction to reach places where State cannot reach on its own. Despite some good initiatives by some large corporations, the concept of voluntary CSR which operated in last 60 years, had not really worked well.

Some issues like tax exemption still need elaboration and may elicit better response from the corporate world. Corporates would be expected to set up special departments to operationalise new provisions and monitor the expenditure. Good corporates will think in terms of developing long and short term implementation plans as well as evaluation system to measure the impact of its CSR initiatives. The enumeration in the law of activities qualifying as CSR clarifies considerable vagueness. It also offers lot of flexibility to industry to adopt CSR in compliance of new regulation. While the mandatory concept of CSR is laudable, the real key lies in its implementation. How the Government is going to monitor CSR spending over a large number of companies. Whether necessary administrative machinery will be in place. Unfair practices or window dressing may not be ruled out, more so in periods of recession. While these issues will be addressed over time, a concrete step has been initiated by the Union Government and now it is the turn of corporate management to ensure its implementation in letter and spirit. Only time will speak about actual implementation of a well-meaning legislation.

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