**Corporate governance & CSR under the new legal regime**

Management of company affairs has undergone fundamental changes since the invention of limited liability companies. Traditionally considered a western phenomenon[[1]](#footnote-1), many scholars are quick to dismiss that corporate social responsibility (hereinafter “CSR”) could have been a part of ancient Indian[[2]](#footnote-2) administration/governance. Dearth of literature in this field only enhances ones skepticism in this regard. However, it is generally agreed that Indian businesses have traditionally being socially responsible[[3]](#footnote-3).

Often perceived as an extension of ethics in business, CSR today have assumed new dimensions for companies not just to build reputation and goodwill in the market but to improve company’s access to finance.[[4]](#footnote-4) The Companies Act, 2013 (hereinafter “the 2013 Act”) brings about fundamental changes in the realm of corporate social responsibility in India.

This article in Part I analyze the general nature of corporate social responsibility with reference to the Corporate Social Responsibility Voluntary Guidelines in 2009 and Companies Act 2013 in India. Part II describes Section 135 of the 2013 Act, the current legal regime and the CSR obligations from corporate governance[[5]](#footnote-5) point of view. Part III of the article deals with the observations of the author. Part IV concludes the article. A substantive analysis of advantages/disadvantages is beyond the scope of this article. This article only attempts to analyze the law relating to CSR as it stands today.

**Part I- The Precursor- Corporate Social Responsibility Voluntary Guidelines in 2009**

The Ministry of Corporate Affairs introduced the Corporate Social Responsibility Voluntary Guidelines in 2009. The fundamental principle of the CSR Voluntary Guidelines was to persuade companies to chalk out a roadmap for its CSR initiatives and align its business goals with such initiatives. The implementation strategy as found in the CSR Voluntary Guidelines of 2009 included identification of activities, setting measurable targets within specified time, allocating financial resources, responsibilities and monitoring.[[6]](#footnote-6) The core elements of the CSR Voluntary Guidelines were to care for all stakeholders, ethical functioning, respect for worker’s rights and welfare, respect for human rights, respect for environment, activities for social and inclusive development.

The 2013 Act now provides teeth to the abovementioned guidelines. The 2013 Act requires companies to formulate a robust CSR policy and incur a minimum expenditure on social initiatives. Section 135 of the 2013 Act[[7]](#footnote-7) contains the crux of the CSR obligations.

**Part II- Section 135 of the 2013 Act**

Section 135 states the criteria to which companies the CSR obligations apply to. It seeks to broaden the scope of CSR activities from mere charity to a more community focused social initiatives by the companies to whom the regime applies. These initiatives include promotion of education, gender equality, women empowerment, ensuring environmental sustainability, enhancing vocational skills, combating poverty, child mortality amongst other community oriented services.

Section 135 of the 2013 Act, states that every company having a net worth of Rupees 500 crore or more or a turnover of Rupees 1000 crore or more, or a net profit of Rupees Five crore or more, during any financial year shall constitute the corporate social responsibility committee. This CSR Committee shall comprise three or more directors (of which one will be an independent director) who shall formulate the policy, including activities specified in Schedule VII.[[8]](#footnote-8) The Board of every company who fall within the criteria mentioned above shall spend 2% of average net profits of last 3 years mandatorily on CSR activities. The specified amount should preferably be spent in the local area of the company’s operations. In case of failure to spend the specified percentage, explanation for such failure needs to be given in the director’s report. In short, the amendments in the new Act seeks to operationalize CSR by way of a reporting regime i.e. comply or disclose.

**Section III - Observations**

The above amendments bring about a fundamental change in the realm of corporate social responsibility in India. Scholars opine that India is the first country to make a minimum expenditure on CSR activities mandatory. It could be argued that the changes in the 2013 Act seeks to make companies socially responsible entities. Though the effectiveness of this disclosure/reporting regime is yet to be ascertained, the author is of the belief that the current obligations fail to address pertinent aspects. The 2013 Act does not define CSR. Schedule VII only contains only a list of aspirations/goals. The 2013 Act nowhere describes what would amount to working towards “combating human immunodeficiency virus” for a company. The 2013 Act leaves it open to the company to ascertaining if a corporate training programme[[9]](#footnote-9) for its employees would amount to “enhancing vocational” skills. The 2013 Act fails to address the consequences of non compliance. An explanation of failure to meet the CSR obligations in the director’s report is not much of a motivation for companies to spend on CSR activities. A tax break in case of compliance could have been a stronger motivation for companies. It also appears to be a distorted effort to compel companies to foray into social governance (government responsibilities). It would have been more effective to increase corporate taxation directly than compel companies to obliquely incur more expenditure. The 2013 Act also fails to clarify if meeting existing obligations (say under environmental laws) could also overlap with CSR obligation of “ensuring environmental sustainability”.

**Conclusion**

The gap between the haves and the have-nots in India is ever widening. Obviously, decreasing economic inequality, eradicating extreme hunger and poverty in India remains a priority not just as government responsibilities but also as shared values of humanity. The CSR ideals/goals are laudatory but mandating companies (a legal fiction invented to make profits) is not an effective way to achieve them. CSR is about taking into consideration the stakeholders (including the society) and conducting business whilst safeguarding their interests but CSR obligations should not be enforced as some sort of mandatory corporate charity. It then not only becomes counter effective but also a liability- which companies are likely to find a way out of.

1. Chapple, W. and J. Moon: 2005, ‘Corporate Social Responsibility in Asia: A Seven-Country Study of CSR Web Site Reporting’, Business & Society 44 (4), 415–441 [↑](#footnote-ref-1)
2. Balakrishnan Muniapan & Mohan Dass, Corporate Social Responsibility: a philosophical approach from an ancient Indian perspective, Int. J. Indian Culture & Business Management, Vol 1, No. 4, 2008. [↑](#footnote-ref-2)
3. Corporate Social Responsibility Voluntary Guidelines in 2009, Ministry of Corporate Affairs, Government of India, available at

<http://www.mca.gov.in/Ministry/latestnews/CSR_Voluntary_Guidelines_24dec2009.pdf> [↑](#footnote-ref-3)
4. Cheng, Beiting and Ioannou, Ioannis and Serafeim, George, Corporate Social Responsibility and Access to Finance (May 19, 2011). Strategic Management Journal, 35 (1): 1-23.. Available at SSRN: [http://ssrn.com/abstract=1847085](http://ssrn.com/abstract%3D1847085) or <http://dx.doi.org/10.2139/ssrn.1847085> [↑](#footnote-ref-4)
5. The Organization for Economic cooperation and Development (OECD) defines corporate governance as the “Procedures and processes according to which an organisation is directed and controlled. The corporate governance structure specifies the distribution of rights and responsibilities among the different participants in the organisation – such as the board, managers, shareholders and other stakeholders – and lays down the rules and procedures for decision-making.” [↑](#footnote-ref-5)
6. Corporate Social Responsibility Voluntary Guidelines in 2009, Ministry of Corporate Affairs, Government of India, available at

<http://www.mca.gov.in/Ministry/latestnews/CSR_Voluntary_Guidelines_24dec2009.pdf> [↑](#footnote-ref-6)
7. (1) Every company having net worth of rupees five hundred crore or more, or turnover of rupees one thousand crore or more or a net profit of rupees five crore or more during any financial year shall constitute a Corporate Social Responsibility Committee of the Board consisting of three or more directors, out of which at least one director shall be an independent director.

(2) The Board's report under sub-section (3) of section 134 shall disclose the composition of the Corporate Social Responsibility Committee.

(3) The Corporate Social Responsibility Committee shall,—

(a) 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;

(b) recommend the amount of expenditure to be incurred on the activities referred to in clause (a); and (c) monitor the Corporate Social Responsibility Policy of the company from time

to time.

(4) The Board of every company referred to in sub-section (1) shall,—

(a) after taking into account the recommendations made by the Corporate Social Responsibility Committee, approve the Corporate Social Responsibility Policy for the company and disclose contents of such Policy in its report and also place it on the company's website, if any, in such manner as may be prescribed; and

(b) ensure that the activities as are included in Corporate Social Responsibility Policy of the company are undertaken by the company.

(5) The Board of every company referred to in sub-section (1), shall 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 Corporate Social Responsibility Policy:

Provided that the company shall give preference to the local area and areas around it where it operates, for spending the amount earmarked for Corporate Social Responsibility activities:

Provided further that if the company fails to spend such amount, the Board shall, in its report made under clause (o) of sub-section (3) of section 134, specify the reasons for not spending the amount.

Explanation —For the purposes of this section “average net profit” shall be calculated in accordance with the provisions of section 198. [↑](#footnote-ref-7)
8. Schedule VII includes the following activities:

Activities relating to:—

(i) eradicating extreme hunger and poverty;

(ii) promotion of education;

(iii) promoting gender equality and empowering women;

(iv) reducing child mortlity 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 [↑](#footnote-ref-8)
9. #  Aneel Karnani, Mandatory CSR in India: A Bad Proposal, Stanford Social Innovation Review, May 2013.

 [↑](#footnote-ref-9)